

THE CONCESSION AGREEMENT

THIS CONCESSION AGREEMENT, dated as of 21 February 1997, (this “agreement”) is made between the Metropolitan Waterworks and Sewerage System (“MWSS”), a government corporation organized and existing pursuant to Republic Act No. 6234, as amended, (the “Charter”), and Manila Water Company, Inc., a corporation organized and existing under the laws of the Philippines (the “Concessionaire”).

WHEREAS, pursuant to the Charter, MWSS has jurisdiction, supervision and control over all waterworks and sewerage system within Metropolitan Manila, the entire province of Rizal and a portion of the province of Cavite; and portion of Bulacan.

WHEREAS, pursuant to Republic Act no. 8041 (the “National Water Crisis Act of 1995”), as implemented by Executive order 286 (December 6, 1995) and Executive order 311 (March 20, 1996), MWSS was mandated to enter into arrangements that will result in the involvement or participation of the private sector in any or all of the segments, operations and/or facilities of the MWSS;

WHEREAS, Article 3(j) of the Charter authorizes MWSS, among other things, to dispose of real and personal property, including rights and franchises, consistent with the purpose for which MWSS was created and reasonably required for the transaction of the lawful business of the same;

WHEREAS, MWSS has determined to grant concessions to private sector corporations, at least 60% of the outstanding capital stock which is owned and controlled by Philippine nationals, which shall act as contractors to perform certain functions, and as agents for the exercise of certain rights and powers, of MWSS under its Charter, to operate the system of waterworks and sewerage services referred to in the Charter;

WHEREAS, pursuant to a process of open public bidding and selection, the Concessionaire has been awarded the right to enter into this Agreement with respect to the service Area East, as identified in Schedule 1 hereto (the “Service Area”); and

WHEREAS, MWSS and the Concessionaire wish to record the terms on which the Concessionaire is being granted the right to operate the waterworks and sewerage services in the Service Area for the period specifies herein;

NOW, THEREFORE, in consideration of the mutual promises and undertakings described herein, the parties hereto agree as follows:

ARTICLE 1. DEFINITIONS

When used herein, the following terms shall have the meanings ascribed to those terms below:

“Appeals Chairman” means the chairman for the time being of the Appeals Panel.

“Appeals Panel” has the meaning given to that term in Section 12.2 hereof.

“Appropriate Discount Rate” means, at any time, the real (i.e., not inflation adjusted) weighted average cost of capital (after taxes payable by the concession business). In determining the Appropriate Discount Rate, the Regulatory Office shall apply conventional and internationally accepted methods, and in particular shall make estimates of the cost of debt in domestic and international markets, the cost of equity for utility businesses in the Philippines and abroad and shall make adjustments to such estimates to reflect country risk, exchange rate risk and any other project risks. The Regulatory Office, at its sole discretion, may consider the Concessionaires rate of return, either stated or implied in its bid, in determining the Appropriate Discount Rate.

“Asset Condition Report” has the meaning given to that term in Section 6.5.2 hereof.

“Bulk Water” means any water supplied in bulk.

“C” means the percentage change in the Consumer Price Index for the Philippines as published by the National Statistical Office between July of the Weighting Year and July of the Prior Year.

“Cash Flows” means (i) in the context of historical cash flows, both Receipts and Expenditures efficiently and prudently incurred by the Concessionaire in the course of carrying out its obligations under this Agreement, and (ii) in the context of future cash flows, (A) both anticipated Receipts and Expenditures efficiently and prudently incurred by the Concessionaire in the course of carrying out its obligations under this Agreement and (B) from and after the second Rate Rebasing Date, any Expiration Payment agreed to be paid by MWSS to the Concessionaire on the Expiration Date pursuant to Section 9.4.3; it being understood that Expenditures “efficiently and prudently incurred” does not include, among other things, payments for (X) Disapproved Assets or (Y) fees for management or consulting services required by the Concessionaire in order to carry out its obligations under this Agreement payable to any shareholder or affiliate of the Concessionaire to the extent, in the judgment of the Regulatory Office, that such fees do not represent the best value available in the market for such services.

“**CERA**”_ means the Currency Exchange Rate Adjustment of one Peso per cubic meter of water consumed above the Standard Rates as permitted by Section 9.1.

“**Charging Year**”_ means any year beginning on January 1 following the first anniversary of the Commencement Date.

“**Charter**” means the Charter of the MWSS set out in Republic Act No. 6234 (as amended), as the same may be further amended or supplement from time to time.

“**Closing Date**” means May 6, 1997, or such later date (not to exceed September 30, 1997) on which the conditions set out in Article 15 hereof have been satisfied.

“**Commencement Date**”_ means the day immediately following the Closing Date.

“**Common Purpose Facilities**” means the Facilities upstream of Angat dam established under the UATP project and the Facilities downstream of the auxiliary hydropower plant of Norzagaray, Bulacan, including the Ipo reservoir facilities, the Ipo-Bicti tunnels Bicti basins and Bicti-Novaliches aqueducts, up to and including the Novaliches portal interconnection Facilities.

“**Concession**”_ has the meaning given to that term in Section 2.1 hereof.

“**Concessionaire Event of Termination**” has the meaning given to that term in Section 10.2.

“**Concession Fee**”_ has the meaning given to that term in Section 6.4 hereof.

“**Concessionaire**” means Manila Water Company, Inc.

“**Concessionaire Employee**” has the meaning given to that term in Section 3.1 hereof.

“**Concessionaire Loans**” means any indebtedness incurred by the Concessionaire to finance or refinance the construction or refurbishment of the Facilities, or employee severance costs or other transitional costs incurred by the Concessionaire following the Commencement Date related to the Concession.

“**Concession Lenders**” means the providers of the Concessionaire Loans.

“**Connection**” has the meaning given to that term in Section 9.5 hereof.

“**Connection Charge**”_ has the meaning given to that term in Section 9.5 hereof.

“Consumer Price Index” or “CPI” mean, for any year, the Consumer Price Index for the Philippines for that year published by the National Statistical Office of the Republic or such successor index as the parties may agree pursuant to Section 2.4.

“Cost Overruns” means any amount paid by the Concessionaire related to an Existing Project or UATP which is neither covered by an MWSS Loan or identified as Local Component costs in Schedule 9.

“Customer” means (i) as of the date hereof, any customer of MWSS or (ii) thereafter, any customer of the Concessionaire, in each case for the supply of water and/or sewerage services in the service Area.

“Disapproved Assets” means any assets acquired by the Concessionaire following the Commencement Date which are not, in the reasonable opinion of the Regulatory office, needed for the efficient and prudent performance by the Concessionaire of its obligations under this Agreement and are so identified in a writing sent to the Concessionaire by the Regulatory Office.

“Dispute Notice” has the meaning given to that term in Section 12.4 (i) hereof.

“E” means any Extraordinary Price Adjustment determined in accordance with Section 9.3.

“Early Retirement Incentive Package” means the separation package approved by the Board of Trustees of MWSS pursuant to its resolutions numbered 24-96 dated February 3, 1996 and 68-96 dated April 18, 1996 (providing for computation of benefits based on creditable service in Government).

10.3.2. **“Early Termination Amount”** has the meaning given to that term in Section

10.3.1. **“Early Termination Date”** has the meaning given to that term in Section

“ESOP” has the meaning given to that term in Section 6.1.4

“ESOP Shares” has the meaning given to that term in Section 6.1.4(i)

16.10.1 **“Event of Force Majeure”** has the meaning given to that term in Section

“Existing Projects” means the projects (or any separable component or project, including only the non-revenue water component of the Umiray Angat Transbasin

Project) in the Service Area identified in Schedule 9, which have been funded by MWSS from bilateral or multilateral sources prior to the Commencement Date.

“Expenditures” means pre-operating and operating expenditures, capital maintenance and investments expenditures, Concession Fees and Philippine business taxes of the Concessionaire (including the Concessionaire’s portion of any such items incurred by the Joint Venture), excluding penalties, interest charges on late payments, financing costs, bad debt provisions and depreciation provisions.

“Expiration Date” means May 6, 2022.

“Expiration Payment” has the meaning given to that term in Section 9.4.4.

“Extraordinary Price Adjustment” has the meaning given to that term in Section 9.3 hereof.

“Facilities” means all fixed and movable assets, including Movable Property, required to provide water delivery services and sewerage services in the Service Area but excluding the Retained Assets. For purposes of this definition, it is understood that the Magallanes Sewerage Treatment Plant and related infrastructure shall be a Facility of Service Area East, and the Central Collecting System and related infrastructure shall be a Facility of Service Area West.

“Future Cash Flows” means, for any Rate Rebasing Date, Cash Flows of the Concessionaire expected to arise after such Rebasing Date in the course of carrying out its obligations under the Concession Agreement as at such Rebasing Date, excluding any revision to those obligations that has been the subject of an Extraordinary Price Adjustment determination due to come into effect on such Rebasing Date.

“Grounds for an Extraordinary Price Adjustment” or **“GEA”** has the meaning given to that term in Section 9.3.1 hereof.

“IPO” has the meaning to that term in Section 6.4.1 (ii).

“Interconnection Agreement” has the meaning to that term given in Section 6.3

“International Water Operator” Means United Utilities PLC.

“Inventory” means the spare parts, pipes and accessories, pumps, meters and other similar items owned by MWSS just prior to the Commencement Date related to the Service Area, and any other terms allocated to the Concessionaire by MWSS prior to bidding on the Concession from the shared facilities with the Other Operator, as set forth in the document captioned “Summary of Construction Materials/Office Supplies”, undated December 2, 1996.

“**Joint Venture**” means the joint venture arrangement to be entered into by the Concessionaire and Other Operator pursuant to Section 3.8 hereof.

“**KKMK**” has the meaning given to that term in Section 6.1.1(v).

“**LBT**” means the La Mesa/Balara Tunnel project-4. Notwithstanding the geographical location of the LBT project, it shall be treated as an Existing Project of Service Area East.

“**Local Component**” means the scheduled costs associated with an Existing Project of the UATP project which is not covered by an MWSS Loan.

“**Low-income Customers**” means Customers with an annual household income of P50,000 or less, which amount shall automatically be adjusted on January 1st of each year by the percentage change in the Consumer Price Index for the preceding year.

“**Major Dispute**” has the meaning given to that term in Section 12.4 (ii).

“**Minor Dispute**” has the meaning given to that term in section 12.4(ii).

“**Movable Property**” means the vehicles, furniture, maintenance equipment, computers and other similar items owned by MWSS just prior to the Commencement Date related to the Service Are, and any items allocated to the Concessionaire by MWSS prior to bidding on the Concession from the shared facilities with the Other Operator, as such property shall be designated by MWSS in the document captioned “General Administration Equipment, Physical Inventory,” undated, distributed December 2, 1996.

“**MWSS**” means the Metropolitan Waterworks & Sewerage System.

“**MWSS Event of Termination**” has the meaning given to that term in Section 10.1.

“**MWSS Loans**” means the indebtedness listed in Schedule 8 hereto for which MWSS is the primary obligor.

“**MWSSSA**” means the MWSS Supervisors Association.

“**NAPOCOR**” means the National Power Corporation, a Government owned and controlled corporation organized and existing under Republic Act No. 6395, as amended.

“**National Building Standards**” means the building standards promulgated or issued pursuant to the National Building Code (Presidential Decree No. 1096, as amended) and related laws, rules and regulations.

“**Net Present Value**” means the net present value calculated at a specified date by discounting real Cash Flows expected to occur at and subsequent to that date,

and inflating real Cash Flows occurring prior to that date, at the Appropriate Discount Rate, using the same discount rate for Cash Flows occurring at any point during any calendar year.

5.3. **New Third Party License** has the meaning given to that term in Section

NIA means the National Irrigation Administration.

NWRB means the National Water Resources Board.

Opening Cash Position means (i) with respect to the first Rate Rebasing Date, the Net Present Value as at June 30 following such Rate Rebasing Date of the real Cash Flows occurring between the Commencement Date and such Rate Rebasing Date in connection with the Concessionaire's carrying out its obligations under this Concession Agreement using the Appropriate Discount Rate determined as of the Commencement Date and (ii) with respect to any subsequent Rate Rebasing Date, the Net Present Value as at June 30 following such Rate Rebasing Date of Cash Flows occurring since the last Rate Rebasing Date together with the Opening Cash Position determined with respect to the last Rate Rebasing Date in connection with the Concessionaire's carrying out its obligations under this Concession Agreement, using the Appropriate Discount Rate determined at the last Rate Rebasing Date. For purposes of calculating the Opening Cash Position, any prior negative Rebasing Convergence Adjustments shall be deemed to have been applied in full in the first Charging Year of the Respective Rate Rebasing period, and not over the five year period set forth in Section 9.4.3 (ii).

Other operator means Benpres-Lyonnaise Waterworks, Inc., in its capacity as the concessionaire appointed pursuant to that certain agreement captioned "Concession Agreement (Service Area West)," between MWSS and Benpres-Lyonnaise Waterworks, Inc., dated as of the date hereof.

Other Operator Employee has the meaning given to that term in Section 3.1 hereof.

Other Service Area means the area in which the other Operator shall provide water and sewerage services in its capacity as the concessionaire pursuant to that certain agreement captioned "Concession Agreement (Service Area West)" between MWSS and Benpres-Lyonnaise Waterworks, Inc., dated as of the date hereof.

Performance Bond has the meaning given to that term in Section 6.9 hereof.

Pesos or "**P**" refers to the lawful currency of the Republic of the Philippines.

Peso Equivalent has the meaning given to that term in Section 6.4.

Prior Year means the year beginning on the first day of January of the year prior to the commencement of each Charging Year.

“Qualified Replacement Operator” means a corporation, or a consortium of corporations, (i) that has the technical and financial capacity to perform all of the obligations of the Concessionaire under this Agreement and (ii) that meets the requirements of Philippine law concerning foreign ownership and management of a public utility.

“R” means any Rebasing Convergence Adjustment determined in accordance with Section 9.4.3.

“Rates Adjustment Limit” means the percentage, either positive or negative, equal to the sum of C, E and R.

“Rate Rebasing Date” means each of January 1, 2003, January 1, 2008, January 1, 2013 and January 1, 2018.

“Rate Rebasing Period” means, in the case of the first Rate Rebasing Period, the period commencing on the Commencement Date and ending on December 31, 2002, and, in the case of subsequent Rate Rebasing Periods, the period commencing on the last Rate Rebasing Date and ending on December 31 of the fifth year thereafter; provided, however, that the last Rate Rebasing Period shall end on the Expiration Date.

“Raw Water” means any untreated water.

“Raw Water Dispute” has the meaning given to that term in Section 12.4 (iv) hereof.

“Rebasing Adjustment” has the meaning given to that term in Section 9.4.2.

“Rebasing” Convergence Adjustment” has the meaning given to that term in Section 9.4.3.

“Rebasing Dispute” has the meaning given to that term in Section 12.4(iii).

“Receipts” means all cash receipts from Customers and grants from third parties (including from the Republic) to the Concessionaire, excluding any interest and dividends received by the concessionaire.

“Regulatory Office” has the meaning given to that term in Section 11.1 hereof.

“Republic” means the Republic of the Philippines.

“Retained Assets” means those assets that are retained by MWSS following the Closing Date, which are set forth in the document captioned **“Allocation of Fixed Assets,”** dated December 6, 1996.

“Retained Employee” has the meaning given to that term in Section 3.1 (i).

“**Rules**” means the arbitration rules of the United Nations Commission on International Trade Law as in effect on the date of this Concession Agreement. “**Service Area**” means the area identified as Service Area East on the map attached to Schedule 1 hereto, and “**Service Area West**” means the areas identified as such on the map attached to Schedule 1 hereto.

“**Service Area Loans**” means the credits listed in Schedule 8 hereto for which MWSS is the primary obligor.

“**Service Obligations**” means the obligations of the Concessionaire of the kind referred to in Article 5 hereof, as such Service Obligations may be revised from time to time by the Regulatory Office in accordance with this Agreement.

“**Shared Facilities**” has the meaning given to that term in Section 3.11.

“**Sponsor**” means Ayala Corporation.

“**Standard Rates**” mean the rates set out in Schedule 5 hereto for the supply of water and sewerage services in the Service Area from the Commencement Date, as amended from time to time in accordance with the provisions of Article 9.

“**Technical Submission**” means the concessionaire’s technical submission submitted to MWSS on January 6, 1997 in connection with the bidding for the Concession.

“**Termination Date**” means the Expiration Date or the Early Termination Date, as the case may be.

“**UATP**” means the Raw Water conveyance component of the Umiray Angat Transbasin Project, as described in Schedule 9.

“**Undertaking Letter**” has the meaning given to that term in Section 15.3 (iii)(d).

“**Weighted Average Rates Increase**” means the percentage difference, either positive or negative, between (i) the revenue that would have accrued to the Concessionaire in the Weighting Year had the Standard Rates to be applied in the Charging Year been applied in the Weighting Year and (ii) the revenue that would have accrued to the Concessionaire in the Weighting Year had the Standard Rates applied by the Concessionaire or, as the case may be, MWSS in the Prior Year been applied in the Weighting Year.

“**Weighting Year**” means the year beginning on the first day of January two years prior to the commencement of each charging year.

ARTICLE 2. APPOINTMENT

2.1 Grant of Concession

On the terms and subject to the conditions set forth herein, MWSS hereby grants to the Concessionaire, as contractor to perform certain functions and as agent for the exercise of rights and powers under the Charter, the sole right to manage, operate, repair, Decommission and refurbish the Facilities in the Service Area, including the right to bill and collect water and sewerage services supplied in the Service Area (the "Concession"). The Concessionaire shall perform its functions and exercise its rights under this Agreement directly or, in respect of functions and rights delegated to the Joint Venture. The rights and benefits of the Concessionaire under this Agreement shall be deemed to apply with equal force to the Joint Venture to the extent that the Joint Venture is performing functions delegated to it under this Agreement.

2.2 Acceptance of Appointment

On the terms and subject to the conditions set forth herein, the Concessionaire hereby accepts the Concession and its appointment as the Concessionaire hereunder.

2.3 Terms of Appointment

The Concession shall take effect on the Commencement Date and, subject to the provisions of Article 10 hereof, shall continue in effect until the Termination Date.

2.4 Consumer Price Index Adjustments

In the event that the Concessionaire and the Regulatory Office determine that the CPI is for any period not an accurate reflection of the rate of inflation in the Philippines as it relates to this Agreement, the Concessionaire and the Regulatory Office may select an alternative index.

ARTICLE 3. TRANSITIONAL ARRANGEMENTS

3.1 Designation of Employees

- (i) Prior to bidding on the Concession, MWSS shall have provided the Concessionaire with a list of MWSS permanent employees (and salary/benefit levels/length of service) who shall be hired by the Concessionaire effective on the Commencement Date (each a "Concessionaire Employee") and a list of MWSS permanent employees who shall be hired by the Other Operator effective on the Commencement Date (each an "Other Operator").

Employee”). The list of prospective Concessionaire Employees and the Other Operator Employees shall be updated at the reasonable Discretion of the Administrator of MWSS within 30 days of the signing hereof such that all current permanent employees of MWSS shall have been designated as either a Concessionaire Employee, Other Operator Employee or retained employee of MWSS (each, a “Retained Employee”). The Concessionaire shall not, without the consent of the Other Operator, hire any Other Operator Employees during a period of one year after the Commencement Date.

- (ii) MWSS shall, within 15 days of the Commencement Date, Supply the Concessionaire with information sufficient to permit the Concessionaire to calculate its maximum exposure for severance payments under Section 6.1.2 below.

3.2 Liabilities/Revenues

MWSS shall bear all liabilities, including the collection of accounts receivable, contingent liabilities relating to environmental contamination, and shall (subject to Section 3.4) be entitled to receive and to retain all revenues, arising out of the operation of the Facilities prior to the Commencement Date. MWSS shall, on the Commencement Date transfer to the concessionaire all Customer deposits then held by MWSS for Customers in the Service Area.

3.3 Conduct of the Business Pending the Closing

MWSS hereby covenants that, from the date hereof and until the Commencement Date, unless the Concessionaire shall otherwise consent in writing (which consent shall not unreasonably be withheld), MWSS shall conduct the business and operations of MWSS in the ordinary and usual course in a manner consistent with past best practice and, without limiting the generality of the foregoing, MWSS shall:

- (i) use its reasonable efforts to preserve and maintain the Facilities and Inventories;
- (ii) maintain in accordance with its normal best practices all documents, agreements, contracts and other corporate records of MWSS relevant to its business and operations;
- (iii) at all times comply with all material laws, statutes, rules, regulations, orders and directives of any

governmental authority having jurisdiction over MWSS or its businesses, except in cases where the application thereof is being contested in good faith or is the subject of an appeal or other legal challenge;

- (iv) give prompt written notice to the Concessionaire of the commencement of any dispute or proceeding between MWSS and any governmental body which, if determined adversely to MWSS, could reasonably be expected to have a material adverse effect on MWSS business or financial condition; (b) the occurrence of any material event of default in any material agreement of MWSS or any event which, upon a lapse of time or the giving of notice or both, would become a material event of default under any such agreement; and (c) the occurrence of any other event which has or could reasonably be expected to have a material adverse effect on MWSS' business or financial condition;
- (v) not waive any valuable right owed to MWSS or enter into any material contract which could affect the Concessionaire; or
- (vi) not reorganize departments or otherwise its organizational structure or employee salaries or benefits in any material fashion, other than any such reorganization consistent with the terms hereof.

3.4 Accounts Receivable

Until the first anniversary of the Commencement Date, the Concessionaire shall have the exclusive right to collect any accounts receivable from Customers for water and sewerage services outstanding as of the Commencement Date. The Concessionaire shall remit to MWSS, on a monthly basis, all amounts collected in respect of such accounts receivable less a collection fee of (i) for any receivable that has been outstanding for 60 days or less as of the Commencement Date, a fee equal to 3% of the amount collected and (ii) for any receivable that has been outstanding for more than 60 days as of the Commencement Date, a fee equal to 6% of the amount collected.

3.5 Inventory

Effective on the Commencement Date, the Concessionaire shall have the Right to use any items of Inventory in carrying out its responsibility under the Concession. Any consumable items owned by MWSS and inventory not identified for use by the Concessionaire shall be subject to the retention or disposal by MWSS and the

applicable rules and procedures of the Commission on Audit shall be complied with in the event of any such disposition of assets by MWSS.

3.6 Movable Property

Legal title to all Movable Property in existence at the Commencement Date shall be retained by MWSS. The Concessionaire is hereby granted the right to operate, maintain, in good working order, repair, decommission and refurbish the Movable Property required to provide the water and sewage services under this Agreement; provided, however, that upon expiration of the useful life of any such Movable Property as maybe determined by the Concessionaire, such Movable Material shall be returned to MWSS in its then-current condition at no charge to MWSS or the Concessionaire.

3.7 Commencement Fee

The Concessionaire shall pay a commencement fee of U.S. \$5 Million to MWSS on the Commencement Date.

3.8 Joint Venture

Prior to the Commencement Date, the Concessionaire and Other Operator shall enter into a joint venture arrangement in such form as they shall select (e.g., a contractual arrangement, a special purpose company incorporated in the Philippines or other arrangement) (the "Joint Venture") subject to the approval of MWSS to assure that (i) the Joint Venture arrangement identifies the party which shall bear each material responsibility and liability of the Joint Venture and (ii) the Joint Venture enters into appropriate contractual undertakings with MWSS regarding the Common Purpose Facilities (including recourse to the Performance Bonds of the Concessionaire and the other Operator). The Joint Venture shall have the responsibility to:

- (i) operate, maintain, renew and, as appropriate, decommission the Common Purpose Facilities in a manner consistent with the National Building Standards and best industrial practices so that, at all times, the water and sewerage system in the Service Area is capable of meeting the Service Obligations (as such obligations may be revised from time to time by the Regulatory Office following Consultation with the Concessionaire) and
- (ii) perform such other functions relating to the Concession (and the Concession of the Other Operator) as the Concessionaire and the Other Operator may choose to delegate to the Joint Venture, subject to approval by MWSS.

In addition, the Concessionaire and the Other Operator shall enter into bilateral arrangements relating to the billing and collection for any services provided by either of

them in the other's Service Area and interconnection arrangements as provided in Section 6.3.

3.9 Raw Water Supplies

- (i) Arrangements with respect to the terms and conditions of the supply of Raw Water to the Concessionaire and the Other Operator are set forth in the letter from MWSS to NWRB dated November 27, 1996, which letter was acknowledged and approved by the MWSS Board of Trustees on December 2, 1996.
- (ii) Whenever MWSS receives notice of meeting with NWRB at which an issue affecting the Concessionaire is scheduled to be discussed, MWSS shall promptly give the Concessionaire notice of that meeting and shall make all reasonable efforts to permit a representative of the Concessionaire to attend such meeting and to express views on behalf of MWSS. On any issue put to vote at any such meeting which affects only the Concessionaire and not the Other Operator, MWSS shall vote in a manner consistent with the Concessionaire's interest. On any issue which affects both the Concessionaire and the Other Operator, MWSS shall vote in such manner as consistent with the interests of the Concessionaire and the Other Operator.

3.10 Cash and Marketable Securities

MWSS shall retain, and not transfer to the Concessionaire, all cash and Marketable securities in existence on the Commencement Date.

3.11 Shared Facilities

The Concessionaire and Other Operator shall have equal access to those MWSS facilities involved in the provision of water supply and sewerage services in both Service Area East and Service Area West including, but not limited to, the MWSS management information system, billing system, telemetry system, central control room and central records (the "Shared Facilities")

MWSS shall also make its corporate headquarters available to the Concessionaire and the Other Operator during one-year period beginning on the Commencement Date (subject to renewal with the consent of all parties).

ARTICLE 4. REPRESENTATIONS AND WARRANTIES

4.1 Representations and Warranties of MWSS

MWSS hereby represents and warrants to the Concessionaire as follows:

4.1.1 Corporate Organization

MWSS is a government corporation duly organized, validly existing and in good standing under the laws of the Republic.

4.1.2 Authorization

MWSS has full power and authority to execute and deliver this Agreement and to consummate the transactions contemplated hereby. The execution and delivery of this Agreement by MWSS and the consummation by MWSS of the transactions contemplated hereby have been duly authorized by all necessary action of MWSS and no further action or proceeding on the part of MWSS is necessary to authorize the execution and delivery by MWSS of this Agreement or the consummation by MWSS of the transactions contemplated hereby. This Agreement has been duly executed and delivered by MWSS and has been approved by the President of the Republic and, under the laws of the Republic in effect as of the date of this Agreement, is a legal, valid and binding obligation of MWSS, against MWSS in accordance with its terms.

4.1.3 No violations: No Consents or Approvals Required

- (i) Neither the execution and delivery of this Agreement nor the transactions contemplated hereby will (a) conflict with or violate any provision of the Charter, (b) conflict with or violate any law, rule, regulation, ordinance, order, writ, injunction, judgment or decree applicable to MWSS or by which any of MWSS properties or assets are bound or affected or (c) conflict with or result in any breach or constitute a default (or an event which with notice or lapse of time or both would become a default) under, or give to others any rights of termination, cancellation or acceleration of, or result in the creation of any lien, charge or encumbrance on any of its assets or properties pursuant to any of the terms, conditions or provisions of any note, bond, mortgage, indenture, permit, license, franchise, lease, contract, agreement or other instrument or provisions of, any note, bond, mortgage, indenture, permit, license, franchise, lease, contract, agreement or other instrument or obligation to which MWSS is a party or by which MWSS or any of its properties or assets is bound or affected.
- (ii) Except for the approval of the President of the Republic referred to in Section 4.1.2 above, no notice, declaration, report or other filing or registration with, and no waiver, consent, approval or authorization of, any governmental or regulatory authority or instrumentality is required to be

submitted, made or obtained by MWSS in connection with the execution, delivery or performance of this Agreement by MWSS and the consummation of the transactions contemplated hereby.

4.1.4 Financial Statements

The financial statements of MWSS for the fiscal year ending December 31, 1995, previously provided to the Concessionaire, fairly present the financial position of MWSS as of such dates and the results of operations of MWSS for the periods covered by those statements. Since December 31, 1995 there has been no material adverse change in the business, financial position, results of operations or prospects of MWSS. (The representation and warranty contained herein will be deemed to be repeated as of the Closing Date with reference to the financial statements of MWSS dated December 31, 1996). In addition, the disaggregated pro forma statements with respect to the Concession, the Other Service Area and the retained functions of MWSS previously provided to the Concessionaire have been prepared in a manner consistent with generally accepted accounting principles in the Philippines.

4.1.5 Brokers and Finders

Neither MWSS, nor any of its officials or employees, has incurred any liability for any brokerage fees, commissions, finders' fees or similar fees or Expenses in connection with the transactions referred to in its Agreement for which the Concessionaire may be liable.

4.1.6 NO OTHER REPRESENTATIONS OR WARRANTIES

EXCEPT FOR THE REPRESENTATIONS AND WARRANTIES CONTAINED IN THIS ARTICLE 4, NEITHER MWSS NOR ANY PERSON ACTING FOR MWSS MAKES ANY OTHER REPRESENTATION OR WARRANTY, EXPRESS OR IMPLIED, AND MWSS HEREBY DISCLAIMS ANY SUCH REPRESENTATION OR WARRANTY, WHETHER BY MWSS OR ANY OF ITS OFFICIALS, EMPLOYEES, AGENTS OR REPRESENTATIVES OR ANY OTHER PERSON, WITH RESPECT TO THE EXECUTION, DELIVERY OR PERFORMANCE BY MWSS OF THIS AGREEMENT OR WITH RESPECT TO THE TRANSACTIONS CONTEMPLATED HEREBY, NOTWITHSTANDING THE DELIVERY OR DISCLOSURE TO THE CONCESSIONAIRE OR ANY OF ITS OFFICERS, DIRECTORS, EMPLOYEES, AGENTS OR REPRESENTATIVES OR ANY OTHER PERSON OF ANY DOCUMENTATION OR OTHER INFORMATION (FINANCIAL OR OTHERWISE) BY MWSS OR ANY OF ITS OFFICIALS, EMPLOYEES, AGENTS OR REPRESENTATIVES OR ANY OTHER PERSON WITH RESPECT TO ANY ONE OR MORE OF THE FOREGOING.

4.2 Representations and Warranties of the Concessionaire

The Concessionaire hereby represents and warrants to MWSS as follows:

4.2.1 Corporate Organization

The Concessionaire is a corporation duly organized, validly existing and in good standing under the laws of the Republic of the Philippines. The Concessionaire has full corporate power and authority to carry on its business as required under the terms of this Agreement and is duly qualified to do business in all jurisdictions where the ownership of its assets or the conduct of its business requires such qualification. The outstanding voting capital stock of the Concessionaire is at least 60% owned by citizens of the Philippines or by corporations that are themselves at least 60% owned by citizens of the Philippines.

4.2.2 Authorization

The Concessionaire has full power and authority to execute and deliver this Agreement and to consummate the transactions contemplated hereby. The execution and delivery of this Agreement by the Concessionaire and the consummation by the Concessionaire of the transactions contemplated hereby have been duly authorized by all necessary action of the Concessionaire and no further action or proceeding on the part of the Concessionaire is necessary to authorize the execution and delivery by the Concessionaire of this Agreement or the consummation by the Concessionaire of the transactions contemplated hereby.

This agreement has been duly executed and delivered by the Concessionaire and is a legal, valid and binding obligation of the Concessionaire, enforceable against the Concessionaire in accordance with its terms.

4.2.3 No Violations; No Consents or Approvals Required

- (i) Neither the execution and delivery of this Agreement nor the transactions contemplated hereby will (a) conflict with or violate any provisions of the Articles of Incorporation or By-Laws of the Concessionaire, (b) conflict with or violate any law, rule, regulation, ordinance, order, writ, injunction, judgment or decree applicable to the Concessionaire or by which any of the Concessionaire properties or assets are bound or affected or (c) conflict with or result in any breach or constitute a default (or an event which with notice or lapse of time or both would become a default) under, or give others any rights of termination, cancellation or acceleration of, or result in the creation of any lien, charge or encumbrance on any of its assets or properties to any of the terms, conditions or provisions of, any note, bond, mortgage, indenture, permit, license, franchise, lease, contract, agreement or other instrument or obligation to which the Concessionaire is a party or by which the Concessionaire or any of its properties or assets is bound or affected.

- (iii) No notice, declaration, report or other filing or registration with, and no waiver, approval or authorization of, any governmental or regulatory authority or instrumentality is required to be submitted, made or obtained by the

Concessionaire in connection with the execution, delivery or performance of this Agreement by the Concessionaire and the consummation of the transactions contemplated hereby, other than those which have already been obtained and are in full force and effect.

4.2.4 Brokers and Finders

Neither the Concessionaire, nor any of its officials or employees, has incurred any liability for any brokerage fees, commissions, finder's fees or similar fees or expenses in connection with the transactions referred to in this Agreement for which MWSS may be liable.

ARTICLE 5. SERVICE OBLIGATIONS OF THE CONCESSIONAIRE

5.1 General Obligations Regarding the Provision of Water Services

The Concessionaire shall have the obligations set forth in this Article 5 in respect of the provision of water services in the Service Area. The Regulatory Office may defer the implementation of specific Service Obligations in any situation where, in the opinion of the Regulatory Office such a deferment is warranted in light of unforeseen circumstances (e.g., material delay in the completion of the UATP project beyond June 30, 1999 or a material delay in the completion of the LBT project, if such project is amended pursuant to Section 6.13.1 (ii)(B) hereof, beyond June 30, 1999).

5.1.1 Water Supply; New Connections

The Concessionaire shall offer water supply services to all existing Customers in the Service Area on the Commencement Date and, in addition, the Concessionaire shall make at least sufficient connections (net of any disconnections) to meet the coverage target percentages of the population in the designated municipality at the time of the target (excluding users who obtain water from a legal source other than the MWSS system) set out in Schedule 2 hereto by the dates specified in that Schedule. Further, the Concessionaire shall provide data and supporting evidence to the Regulatory Office that demonstrates compliance with such coverage targets, along with the method by which such compliance was calculated, prior to each Rebasing Date in accordance with Section 9.4.1.

5.1.2 Continuity of Supply

As soon as practicable, but in any event not later than June 30, 2000, the Concessionaire shall ensure the availability of an uninterrupted 24 hour supply of water to all connected Customers in the Service Area, subject to interruptions resulting from the temporary failure of items of the Facilities (where the Concessionaire acts promptly to remedy such failure) or required for the repair or construction of the Facilities where such repairs or construction cannot be performed without interruption to the supply of water. At all times, such water shall be supplied at a level of positive pressure sufficient

to secure the system against the ingress of untreated water or other contaminants; provided, however, that such pressure shall be at a minimum of 11 meters (16 psi) for all areas connected by new primary or secondary conveyance pipelines and, from the tenth anniversary of the Commencement Date, for all pipelines throughout the Service Area. Water pressures shall be determined by measuring service pressure on the Customer's side of the water meter inside of the water meter box.

5.1.3 Obligation to Make Connections to a Water Main

Upon request from the owner or occupant of premises located in the Service Area for a connection to a water main, the Concessionaire shall make such a connection as soon as reasonably practicable. For such connection to a water main located less than 25 meters from the connection point for such main, the Customer shall pay the connection fee set out in Section 9.5(i). For all other connections, the Customer shall pay a fee determined in accordance with Section 9.5 (ii).

5.1.4 Drinking Water Quality Standards

The Concessionaire shall ensure at all times that the water supplied to Customers in the Service Area complies with Philippine National Drinking Water Standards as published by the Department of Health of the Republic (or successor entity responsible for such standards) and prevailing at such time; provided, however, that the Regulatory Office, after consultation with any appropriate governmental authorities, shall have the discretion to consent to a phase-in of compliance with these standards over a period of not more than 12 months from the Commencement Date. The Concessionaire shall observe any requirements regarding sampling, record keeping or reporting as may be specified by law in the Philippines.

5.1.5 Obligation to Supply Water for Public Purposes

The Concessionaire shall make available an adequate supply of water for fire-fighting and other public purposes as the municipalities comprising the Service Area may reasonably request. The Concessionaire shall not assess a charge for such water used for fire-fighting purposes but may charge for all other water used for public purposes.

5.1.6 Provision of Water Other Than Through a Water Main

The Concessionaire shall make a supply of water available to Customers other than through a water main in circumstances where (i) supplies through a water main have been or will be interrupted for more than 24 hours, or (ii) supplies through a water main have been or will be subject to contamination. The charges for these services shall not exceed the Standard Rates for piped water supplies. In circumstances where no connection to a water main exists, the Concessionaire may make a supply of water available to Customers other than through a water main at a fee equal to the costs reasonably and efficiently incurred by the Concessionaire in supplying such water.

5.2 General Obligations Regarding the Provisions of Sewerage Services

The Concessionaire shall have the following obligations in respect of the provision of sewerage services in the Service Area:

5.2.1 Supply of Sewerage Service; New Connections

The Concessionaire shall offer to supply sewerage services to all Customers in the Service Area who have sewerage connections on the date hereof for domestic sewage and industrial effluents compatible with available treatment processes and, in addition, the Concessionaire shall meet the coverage target percentages of the total population in the designated municipality connected to the Concessionaire's water system at the time of the targets set out in Schedule 3 below by the dates specified in that Schedule.

5.2.2 Obligation to Make connections to a Public Sewer

Upon request from the owner or occupant of premises located in the Service Area for a connection to a public sewer, the Concessionaire shall make such a connection as soon as reasonably practicable. For such connection to a public sewer located less than 25 meters from the connection point, the Customer shall pay the connection fee set out in Section 9.5 (i). For all other connections, the Customer shall pay a fee determined in accordance with Section 9.5(ii).

5.2.3 Wastewater Standards

The Concessionaire shall comply with all national and local environmental laws and standards relating to treated wastewater in the Service Area and in accordance with a schedule of compliance provided by the Regulatory Office as the same may be modified or supplemented from time to time in consultation with the Concessionaire, and the Concessionaire shall have the sole liability for any changes or fines that may be assessed in connection with violations thereof.

5.2.4 Septic and Sanitation Cleaning

The Concessionaire shall offer septic and sanitation cleaning services in the Service Area, and, in addition, the Concessionaire shall meet the coverage target percentages of the total population in the designated municipality at the time of the target for such services set out in Schedule 4 below by the dates specified in that Schedule; provided, however, that Customers who requests such services of the Concessionaire shall have first priority over those who do not request them. Septic and sanitation cleaning services are defined as the emptying of domestic septic tanks and subsequent sludge disposal at regular intervals of five to seven years.

5.3 Exclusivity

Subject to (i) and (ii) below, the Concessionaire shall have the exclusive right to provide water and sewerage services in the Service Area:

- (i) Any license granted by the NWRB with the consent of MWSS to a third-party provider of water and sewerage services in effect on the Commencement Date shall remain in effect in accordance with its terms.
- (ii) In the event of any application to the NWRB for which MWSS consent is sought by a third party for a license to provide water and sewerage services to a new development after the Commencement Date (a "New Third Party License"), MWSS shall consent to the grant by the NWRB to the Concessionaire of the right to provide such services to such new development if the Concessionaire agrees to provide such services on (a) substantially similar terms as set forth in the proposed New Third Party License and (b) at the Standard Rates then in effect for such services. If the conditions set out in the previous sentence are not met, or if the Concessionaire voluntarily declines to provide the services to such new development, MWSS may consent to the grant of a license to the third-party service provider for a term not longer than 10 years, subject to revocation upon not less than 60 days' notice to such third party provider if the Concessionaire notifies MWSS and the NWRB in writing that the Concessionaire is in a position to provide such services in accordance with the conditions of this clause (ii)..

To the extent feasible, MWSS shall authorize and facilitate direct communication between NWRB and the Concessionaire with respect to the matters referred to in this Section 5.3.

5.4 Other Customer Service Standards

At all times, the Concessionaire shall provide the highest quality services to its Customers that are practically achievable subject to guidelines issued by the Regulatory Office, including, but not limited to:

- (i) giving prompt responses to Customer inquiries and complaints;
- (ii) giving notices to Customers at least 48 hours in advance of any planned interruptions in water supply;
- (iii) making alternative water supplies available for planned interruptions in service of more than 24 hours;
- (iv) effecting urgent restoration of water supplies for any unplanned interruptions in service and informing Customers on progress in

making necessary repairs and treatment of potentially contaminated supplies;

- (v) taking measures to prevent sewage flooding from the sewerage network; and
- (vi) providing invoices to Customers which clearly identify services, charges, period covered, forms of payment and penalties for late or non-payment.

ARTICLE 6. OTHER OBLIGATIONS OF THE CONCESSIONAIRE

6.1 Employee Matters

The Concessionaire shall have the following obligations in respect of employee matters:

6.1.1 Hiring

- (l) Effective as the end of business hours on the day prior to the commencement Date, the employment of each Concessionaire Employee with MWSS shall be terminated and each such Employee shall (upon receipt by MWSS of a release and quitclaim from such Employee) be entitled to;
 - (a) for Concessionaire Employees eligible for retirement pay in accordance with existing retirement laws (RA 660, 1146 or 1616); and
 - (b) for Concessionaire Employees not eligible for retirement, a severance payment equivalent to one month basic pay for every full year of service.

Such retirement and severance payments shall be the sole responsibility of MWSS.

- (ii) One month prior to the Commencement Date, the Concessionaire Shall make an offer to employ each Concessionaire Employee, subject to a probationary period of six months following the Commencement Date, at a salary or pay scale and with benefits atleast equal to those enjoyed by such Employee on the date of his or her separation from MWSS. Within a period of six months from the Commencement Date, the Concessionaire, in consultation with the Other Operator, shall effect a new compensation structure comparable to those prevailing in the utilities/infrastructure industry in the Philippines.
- (iii) The concessionaire shall pay any Concessionaire Employees who do not accept the Concessionaire's offer of employment the difference between the severance pay that they previously received in accordance with clause (i)(b)

above and the severance benefits offered by MWSS pursuant to the Early Retirement Incentive Package, without prejudice to any salary adjustment that may be granted by the Republic.

- (iii) The Concessionaire shall hire, on a probationary basis, as if the Commencement Date, all those Concessionaire Employees who accept the offer of employment.
- (iv) Not later than six months after the Commencement Date, the Concessionaire will choose which employees to retain on regular status in accordance with the Philippine Labor Code and after due consultation with the Kapatiran ng mga Mangagawa at Kawani sa MWSS ("KKMK") and the MWSS Supervisors Association ("MWSSSA"). KKMK, as the accredited and certified labor union of the rank and file MWSS employees, and MWSSSA shall be recognized, as of the Commencement Date, by the Concessionaire as the representative of the rank and file and supervisory employees, respectively, until such time as an appropriate union has been formed and certified as a bargaining agent. As such, KKMK and MWSSSA may take up with the management of the Concessionaire any and all issues affecting the rights and welfare of their respective members.
- (v) Those employees retained after six months from the Commencement Date shall then begin employment with the Concessionaire as regular employees. In all cases, the Concessionaire shall recognize and respect the rights of its employees to self organization and collective bargaining.
- (vi) Any Retained Employee who notifies the Concessionaire and MWSS in writing within three years following the Commencement Date of his or her desire to be employed by the Concessionaire shall, upon the release of MWSS, promptly be hired by the Concessionaire and entitled to the same treatment as other Concessionaire Employees under this Section 6.1.

6.1.2 Mandatory Severance Payments

- (i) Concessionaire Employees not retained by the Concessionaire after the six-month probation period following the Commencement Date shall be paid by the Concessionaire an amount equal to the difference between the severance pay they previously received in accordance with Section 6.1.1 (i)(b) above and the severance benefits offered by MWSS pursuant to the Early Retirement Incentive Package, without prejudice to any salary adjustment that may be granted by the Republic;
- (ii) For a period of one year beginning at the end of the six month probationary period from the Commencement Date, any Concessionaire Employee who is affected by any

reduction in personnel (e.g. redundancy, installation of labor savings devices, closure, retrenchment or other authorized causes as provided under the Labor Code) shall be paid separation pay equal to the greater of (a) that prescribed by the Labor Code and (b) the difference between the severance pay they previously received in accordance with Section 6.1.1(i)(b) above and the severance benefits offered by MWSS pursuant to the Early Retirement Incentive Package, without prejudice to any salary adjustment that may be granted by the Republic, whichever is higher.

Severance payments due to Concessionaire Employees under this section 6.1.2 shall be the sole responsibility of the Concessionaire.

6.1.3 Non-Diminution of Benefits

The Concessionaire shall grant to all Concessionaire Employees employee benefits no less favorable than those granted to such employees by the MWSS at the time of their separation from MWSS, particularly those set forth in Exhibit F and the following:

- (i) The Concessionaire shall institute, under terms and conditions which are no less favorable than those provided in the MWSS Employees Savings and Welfare Plan, a welfare fund, to which it shall constitute no less than 5% of the monthly basic salary of a member of the Fund who authorizes the Concessionaire to deduct from his or her monthly basic salary 5% thereof as a contribution to the Fund.
- (ii) The Concessionaire shall permit deductions from the salaries of those employees who are members of ESLA/Health Cooperative and Consumers Cooperative/KKMK and MWSSSA of their contributions for capital subscriptions and loan repayments or membership dues in favor of those institutions. The Concessionaire shall likewise, to the extent feasible, provide to those institutions office facilities free of charge.

6.1.4 Employee Stock Option Plan

The Concessionaire shall, within a period of no more than six months from the Commencement Date, adopt an Employee Stock Option Plan ("ESOP") that shall ensure the ownership by its regular employees equal to six percent of the total outstanding capital stock of the Concessionaire. The Concessionaire shall decide

whether these shares will be sourced from original Filipino shareholders, an issue of previously authorized but unissued shares or through a capital increase. The ESOP shall have the following features:

- (i) Coverage and Allocation. All regular employees of the Concessionaire and its affiliates shall be entitled to participate in the ESOP. Employees may only subscribe shares under the ESOP (the “ESOP Shares”) pursuant to the Annual Stock Purchase Bonus referred to in clause (iii) below. The ESOP shares shall comprise a portion of the Filipino equity ownership of the Concessionaire.
- (ii) Subscription Price. During the first year of the ESOP, the subscription price of each ESOP Share shall be the issued price of the Concessionaire’s common shares at the time of incorporation of the Concessionaire. Thereafter, and until an initial public offering (an “IPO”) of the Concessionaire’s shares is conducted, the ESOP Share subscription price shall be adjusted at the end of each fiscal year by the Concessionaire’s external auditors according to established and generally accepted accounting principles applicable to comparable ESOPs in the Philippines.
- (iii) Manner of Payment. The Concessionaire shall grant to every regular employee who has rendered continuous satisfactory service during the full prior year an Annual Stock Purchase Bonus equal to not less than the last basic monthly salary of the employee during that year. This Bonus shall automatically be applied to the purchase of ESOP Shares for the account of that employee. This Bonus shall be paid until all ESOP Shares available for subscription under the ESOP have been prescribed.
- (iv) Vesting. The ESOP Shares shall be issued in the name of the purchasing employees upon full payment for such ESOP Shares.
- (v) Holding Period. For a period of five years from the date of issuance of each ESOP Share, employees may not sell or transfer that ESOP Share. Thereafter, an employee may only sell that ESOP Share to the Concessionaire at a price equal to that determined in the same manner as in Section 6.1.4(ii). Should the Concessionaire conduct an IPO within or after this five-year period, all outstanding ESOP Shares shall be included in the relevant registration statement and each employee holding ESOP Shares may then freely sell or transfer the ESOP Shares held by that employee. In the event of the death of an employee, the balance of the

foregoing holding period shall likewise apply to the employee's successors-in-interest.

- (vi) Separation from the Concessionaire. In the event that an employee resigns, retires or is otherwise separated for any reason (other than death) from the Concessionaire or its affiliates prior to the expiration of the five-year holding period or, if earlier, the implementation of an IPO, the ESOP Shares then held by the resigned, retired or separated employee shall be purchased by the Concessionaire at the then-applicable subscription price under the ESOP.
- (vii) Voting Rights. The ESOP shall comprise a class of shares which, during the first five years after commencement of the ESOP, shall have no voting rights except for the matters provided for under Section 6 of the Corporate Code; provided, however, that if the ESOP Shares are included in an IPO during this five-year period, this restriction on voting rights shall automatically terminate.
- (viii) New Employees. Regular Employees who join the Concessionaire after the institution of the ESOP are eligible to participate on a first-come, first-served basis if there are still ESOP Shares available for subscription. Subject to rules to be issued by the Concessionaire, available ESOP Shares may be allocated on a pro-rata basis if it is not possible in Section 6.1.4(i) hereof.

6.2 Taxes

Subject to the Undertaking Letter, the Concessionaire shall be responsible for all income and withholding taxes and other forms of taxes arising from payments by Customers for services rendered on and after the Commencement Date and from any other income associated with the Concession arising on or after the Commencement Date. The Concessionaire shall be responsible for the payment of all documentary stamp taxes payable in connection with the execution of this Agreement and any related agreements or instruments; all customs, import duties and other taxes or assessments relating to the importation into the Philippines of plant and equipment to be used in connection with the Concession; and all local transfer taxes on property acquired through the exercise of rights pursuant to Section 7.2. In addition, the Concessionaire shall pay, for and on behalf of MWSS, or shall reimburse MWSS within 10 days of demand therefor, any real property taxes and other taxes or assessments payable by MWSS on MWSS property or assets in the Service Area used for the supply of water and sewerage services.

6.3 Interconnection

Within thirty days following the date hereof, the Concessionaire shall enter into an interconnection agreement with the Other Operator, in form and substance satisfactory to MWSS (the "Interconnection Agreement"). The Interconnection Agreement shall address the matters summarized in Schedule 10 in a manner consistent with that Schedule.

6.4 Concession Fee

By January 15 of each calendar year, MWSS shall provide the Concessionaire with a schedule of all anticipated amounts due in connection with the Concession Fee payable during that year, as described in (a) and (b) below:

- (a) Not later than 14 days prior to the date on which any scheduled payment of principal, interest, fees or other amount is due under an MWSS Loan, MWSS shall notify the Concessionaire in writing of the total amount due on that payment date and of the Peso equivalent thereof (the "Peso Equivalent") calculated at the then prevailing exchange rate. Not later than one business day prior to each such payment date, the Concessionaire shall remit to such account as MWSS shall instruct an amount, in Pesos, exclusive of any penalties or default interest charges not attributable to a late payment of the Concession Fee by the Concessionaire (each such payment being referred to herein as a "Concession Fee"), equal to the sum of:
 - (i) 10% of the aggregate Peso Equivalent due under any MWSS Loan which has been disbursed prior to the Commencement Date (including MWSS Loans for Existing Projects and the UATP project) on the relevant payment date set forth on Schedule 8; plus
 - (ii) 10% of the aggregate Peso Equivalent due under any MWSS Loan designated for the UATP project which has not been disbursed prior to the Commencement Date on the relevant payment date set forth on Schedule 8; plus
 - (iii) 10% of the Local Component costs and Cost Overruns related to the UATP project in accordance with Schedule 9; plus
 - (iv) 100% of the aggregate Peso Equivalent due under any MWSS Loan designated for Existing Projects, which have not been disbursed prior to the Commencement Date and have been either awarded to third party bidders in accordance with Section 6.13.1(i)

or been elected by the Concessionaire for continuation in accordance with Section 6.13.1(ii);plus

- (v) 100% of the Local Component costs and Cost Overruns related to Existing Projects in accordance with Schedule 9.

- (b) Not later than five days after the Commencement Date, the Concessionaire shall pay to MWSS the amount of 50 million Pesos, which MWSS shall use and allocate in accordance with Section 11.2 for the establishment and budget of the Regulatory Office during 1997. In addition, the Concessionaire shall pay to MWSS on the first business day of January of each year thereafter an amount equal to one-half of the annual budget for MWSS for that year, provided that such annual budget shall not for any year exceed million Pesos, subject to annual CPI adjustments. MWSS may request adjustments to the level of the annual contribution of the Concessionaire provided in this Section 6.4(b). If the Concessionaire objects to any such requested revision, it may refer the matter to the Appeals Panel.

Each Concession Fee shall be treated as an Expenditure of the Concession and the Concessionaire's payment obligation in respect thereof shall rank at least pari passu with its unsecured payment obligations under all other debt instruments that may be executed by the Concessionaire. In the event the Concessionaire does not make a timely payment of a Concession Fee, the U.S. dollar equivalent of such unpaid amount may be drawable under the Performance Bond in accordance with Section 6.9 below.

6.5 Asset Management Obligations

The Concessionaire shall have the following obligations concerning the management of the Facilities:

6.5.1 General

During the term of the Concession, the Concessionaire shall:

- (i) operate, maintain, renew and, as appropriate, decommission Facilities in a manner consistent with the National Building Standards and best industrial practices so that, at all times, the water and sewerage system in the Service Area is capable of meting the Service Obligations (as such obligations may be revised from time to time by the Regulatory Office following consultation with the Concessionaire);

- (ii) repair and correct, on a priority basis, any defect in the Facilities that could adversely affect public health or welfare, or cause damage to persons or third-party property; and
- (iii) ensure that at all times the Concessionaire has sufficient financial, material and personnel resources available to it to meet its obligations under this Agreement.

6.5.2 Asset Condition Disclosure

Not later than the second anniversary of this Agreement, the Concessionaire shall provide a report (the "Asset Condition Report") to the Regulatory Office, in form and substance satisfactory to the Regulatory Office, classifying (on a graded scale) the condition of infrastructure Facilities in the Service Area. This Report shall cover:

- (i) Facilities related to the provision of water supply services, distinguishing among dams, Bulk Water transfer, water treatment plants, pumping stations, trunk potable water systems, service reservoirs and distribution mains; and
- (ii) Facilities related to the provision of sewerage services, distinguishing among interceptor sewers, other sewers, rising mains, pumping stations, sewage treatment and disposal assets.

6.5.3 Audit

The Regulatory Office shall have the right at any time to commission an independent technical audit of the accuracy and completeness of any Asset Condition Report and/or the Concessionaire's compliance with its obligations under Section 6.5.1 above. The Concessionaire shall cooperate fully with any such audit. The cost of any such audit shall be borne by the Concessionaire and treated as an Expenditure.

6.5.4 Remedial Works

Commencing five years subsequent to the Commencement Date, if, based on an audit report commissioned pursuant to Section 6.5.3 above and any other information coming to the attention of the Regulatory Office, the Regulatory Office reasonably concludes that the Concessionaire is not meeting its obligations under Section 6.5.1 above, then the Regulatory Office shall give the Concessionaire written notice of this conclusion and the Concessionaire shall have 60 days (or such longer period as the Regulatory Office may provide) thereafter to commence appropriate action to correct the problem to the satisfaction of the Regulatory Office. Failing such correction, the Regulatory Office shall have the authority to commission appropriate remedial works by third parties. The costs of such remedial works shall be borne by the Concessionaire but shall not constitute an Expenditure or qualify as a Ground for an Extraordinary Price

Adjustment. In the event the Concessionaire does not make a payment within 30 days of written notice pursuant to this Section 6.5.4 of the cost of such remedial works, the U.S. dollar equivalent of such unpaid amount shall be drawable under the Performance Bond in accordance with Section 6.9 below.

6.6 Disconnections

The Concessionaire may disconnect any Connection for the supply of water services or sewerage services in the Service Area if charges billed to the Customer therefor remain unpaid for a period of 60 days after their due date. The Concessionaire shall provide the Customer with not less than seven days' prior written notice of any such disconnection. Upon the payment in full of all outstanding charges (including late payment penalties and reconnection charges), the Concessionaire shall reconnect any Customer whose services have previously been disconnected within five days following receipt of a request for reconnection.

6.7 Insurance

The Concessionaire shall at its own expense effect and maintain, or require to be effected and maintained throughout the term of the Concession insurance coverage in such amounts as are reasonable and customary throughout the industry internationally; provided however, that the Concessionaire shall at all times comply with Administrative Order #141 regarding insurance of Government properties by the General Insurance Funds of the Government Service Insurance System.

6.8 Compliance with Laws

The Concessionaire shall comply with all Philippine laws, statutes, rules Regulations, orders and directives of any governmental authority that may affect the Concession from time to time.

6.9 Performance Bond

On the Commencement Date, and on each Rate Rebasing Date, the Concessionaire shall post a bond, bank guarantee or other security acceptable to MWSS (a "Performance Bond") in favor of MWSS to secure the Concessionaire's performance of its obligations under Section 3.8 (Joint Venture), Section 6.4 (Concession Fee), Section 6.5.4 (Remedial Works), Section 10.3.2 (Early Termination), Section 10.4 (Penalties for Failure to Meet Service Obligations) Section 11.2.2 (Annual Contribution), Section 12.6 (Costs of the Appeals Panel) during the Rate Rebasing Period commencing on that date. The aggregate amount drawable in one or more installments under each such Performance Bond during the Rate Rebasing Period to which it relates is set out below:

<u>Drawable Rate Rebasing Period Under Performance Bond</u>	Aggregate	Amount
	(in U.S. \$ millions)	
	East	
First	70	
Second	70	
Third	60	
Fourth	60	
Fifth	50	

Within 30 days of the Commencement of each calendar year, the Concessionaire shall cause the Performance Bond to be reinstated in full amount set forth above applicable for that year.

Upon not less than 10 days' written notice to the Concessionaire, MWSS may take one or more drawings under the Performance Bond relating to a Rate Rebasing Period to cover amounts due to MWSS during that period; provided, However, that no such drawing shall be made in respect of any claim that has been submitted to the Appeals Panel for adjudication until the Appeals Panel has handed its decision in the matter.

In the event that any amount payable to MWSS or the Regulatory Office by the Concessionaire hereunder is not paid when due, such amount shall accrue interest at a rate equal to that of a 364 days Treasury Bill for each day it remains unpaid from and including the due date thereof to but excluding the date on which such amount shall be paid (including payment through a drawing under the Performance Bond) in full.

6.10 Procurement

During the course of the Concession, other than with respect to existing Projects, the Concessionaire shall make available for public tender any contract involving the procurement of goods or services, in one or more installments, having a value in excess of P 250,000,000, which amount shall be adjusted on January 1st of each year by the percentage change in the Consumer Price Index for the preceding year. The Concessionaire, at its sole discretion, shall determine the specifications upon which contractors will bid and the criteria, including price and quality, by which the winning bid is selected.

6.11 Equity Capital

Unless waived in writing by the Regulatory Office:

- (i) until December 31, 2002 (the first Rate Rebasing Date), the International Water Operator and the Sponsor shall each (directly or through a subsidiary that is at least 51% owned, and controlled, by the International Water Operator or the Sponsor, respectively) at least 20% of the outstanding capital stock of the Concessionaire. After the first Rate Rebasing Date and throughout the Concession, the International Water Operator and the Sponsor shall each own (directly or through a subsidiary that is at least 51% owned, and controlled, by the International Water Operator or the Sponsor, respectively) at least 10% of the Outstanding capital stock of the Concessionaire;
- (ii) the Concessionaire shall have an equity paid-in cash capital of not less than P 1 billion at the Commencement Date and by the first anniversary of the Commencement Date shall have an equity paid-in cash capital of not less than P 2 billion; and
- (iii) the Concessionaire shall consider the feasibility of making a public offering of a portion of its equity in the Philippines with a view toward broadening the ownership base of the Concessionaire.

6.12 Concessionaire Debt

The Concessionaire shall not, without the prior approval of MWSS, incur any debt or liability that would mature after the Expiration Date.

6.13 Existing Projects/UATP

The Concessionaire shall have the following responsibilities with respect to Existing Projects of UATP.

6.13.1 Existing Projects

- (i) For the Existing Projects set forth on Schedule 9 which MWSS has awarded a contract to a third party through a public tender prior to the Commencement Date:
 - (A) the Concessionaire shall assume supervisory responsibility for such Existing Projects (subject to the provisions of the relevant MWSS Loan documentation); and
 - (B) the interest, principal and fee obligations related to the disbursed amounts of MWSS Loans designated for such Existing Projects, together with the Local Component costs identified in Schedule 9 and Cost Overruns, shall be covered by the Concession Fee.

- (ii) For Existing Projects set forth on Schedule 9 which MWSS has not awarded a contract to a third party through a public tender prior to the Commencement Date the Concessionaire shall have the option within 30 days following the Commencement Date to:
 - (A) continue with the project design and funding in the same manner as initially contemplated by MWSS and the lender to such Project;
 - (B) amend the project design and funding in collaboration with MWSS and the respective lender to such Project; or
 - (C) notify MWSS and the lender to such Project of the Concessionaire's intent to cancel such Project and its related financing.

In the event the Concessionaire does not cancel such Project pursuant to sub-clause (C) above;

- (1) the Concessionaire shall assume supervisory responsibility for such Existing Projects (subject to the provisions of the relevant MWSS Loan documentation);

- (2) the interest, principal and fee obligations related to the disbursed amounts of MWSS Loans designated for such Existing Projects together with the Local Component costs identified in Schedule 9 and Cost Overruns, shall be covered by the Concession Fee; and
- (3) MWSS and the Concessionaire shall, with the consent of the respective order, set out in writing the details relating to the exercise of the Concessionaire's supervisory responsibility for such Existing Project.

6.13.2 UATP

- (i) MWSS shall retain supervisory responsibility for the UATP project and the Other Operator shall assist and support, to the best of its ability, MWSS to exercise the completion of the UATP project at or under budget.
- (ii) The interest, price and fee obligations related to the disbursed Amounts of the MWSS Loans designated for the UATP project, together with related Cost Overruns and the Local Component costs identified on Schedule 9, shall be covered by the Concession Fee.
- (iii) Cost Overruns or any material delay after June 30, 1999 in the completion of the UATP project and the supply of the related incremental Raw Water shall be considered, upon completion of the UATP project, grounds for a deferment of Service Obligations Adjustment in accordance with Section 9.3.1.
- (iv) The Joint Venture shall be responsible for the operation, maintenance and renewal of all related facilities upon completion of UATP.

6.13.3 Performance Penalties

Any liquidated damages or other performance penalties paid to MWSS under any Existing Project or UATP shall promptly be paid over the Concessionaire and treated as a Receipt under the Concession.

6.14 Technical Submission/Financial Model

The Concessionaire shall provide to the Regulatory Office, not later than 30 days after the Commencement Date, a copy of its Technical Submission. In addition, the financial model supporting the Concessionaire's Rate Bid and Technical Submission (including discount rates, return on equity, projected income statements, balance sheets, sources and uses of funds and relevant ratios) which accompanied the Concessionaire's bid shall be kept in a sealed envelope which may not be opened by the Regulatory Office prior to 30 days after the Commencement Date. The Regulatory Office may treat this information as relevant in carrying out its responsibilities under Article 9 hereof.

6.15 NEW ASSETS

Legal title to all fixed assets contributed to the MWSS system in the Service Area by the Concessionaire during the term of the Concession shall remain with the Concessionaire until the Expiration Date (or the Early Termination Date) at which time all right, title and interest in such assets shall automatically vest in MWSS. The Concessionaire may mortgage or create security interest over such assets solely for the purpose of financing (or refinancing) the acquisition or construction thereof; provided, however, that no such mortgage or security interest shall extend beyond the Expiration Date and, provided further, however, that no such mortgage or security interest shall be subject to foreclosure except following an Event of Termination. The Concessionaire shall not, without the prior approval of MWSS, create a security interest of any kind over all or any part of the Facilities to which MWSS has legal title. Legal title to all facilities (including any fixed assets resulting from the exercise of rights and powers referred to in Section 7.2 below) other than new assets contributed by the Concessionaire shall remain with MWSS.

ARTICLE 7. OBLIGATIONS OF MWSS

7.1 Cooperation with Concessionaire

Subject to the requirements of the Charter, MWSS shall, upon request of the Concessionaire, cooperate in all reasonable ways to facilitate the Concessionaire's carrying out of its responsibilities under the Concession. Pursuant to the authority given to MWSS by Section 3(h) of the Charter, and subject to the restrictions contained in Section 12 of the Charter, this cooperation shall include, but not be limited to, cooperation with actions undertaken by the Concessionaire to implement changes to the Standard Rates for water and sewerage services as instructed by the Regulatory Office or, as appropriate, by the Appeals Panel.

The cooperation to be rendered by MWSS to the Concessionaire shall not require MWSS or any of its affiliates to finance (or guarantee the financing of) any expenditure required in connection with the Concession, or to undertake any liability in favor of a third party other than those expressly provided for in this Agreement.

7.2 Easements, Eminent Domain, Right of Way and Similar Powers

MWSS hereby appoints the Concessionaire as its agent and representative, for purposes of, among others, Section 3 (K) of the Charter in its name, place and stead, to apply for and exercise its easement, eminent domain, right of way and similar rights and powers given to MWSS under its Charter in connection with infrastructure projects and works undertaken relating to the Concession by the Concessionaire in the Service Area pursuant to this Agreement. The Concessionaire shall be solely responsible for the payment of any compensation to third parties occasioned by the exercise of such rights and powers.

ARTICLE 8. RETAINED FUNCTIONS OF MWSS

8.1 Retained Functions

MWSS shall retain, among others, the following operational responsibilities during the period of the Concession (other than the responsibilities assigned to the Regulatory Office).

- (i) facilitating the exercise by the Concessionaire of its agency powers, upon appropriate notification to MWSS by the Concessionaire as provided in Sections 7.1 and 7.2 above;
- (ii) carrying out accounting and notification functions;
- (iii) monitoring, reporting and administering the MWSS Loans, and performing related functions in connection with the Existing Projects;
- (iv) providing such other services or functions as are assigned by this Agreement, or by the Regulatory Office following the Commencement Date, to MWSS;
- (v) managing and/or disposing of the Retained Assets; and
- (vi) managing and operating UATP.

ARTICLE 9. RATES AND CONNECTION CHARGES

9.1 Standard Rates/CERA Fee

Subject to the limitation of Section 12 of the Charter, Standard Rates may be adjusted from time to time in accordance with the rate adjustment provisions set forth in Sections 9.2, 9.3 and 9.4 below. In the event that the Standard Rates chargeable under this Agreement during any period would exceed the limitation of Section 12 of the Charter applicable to that period, the Charter limitation shall be observed but the Regulatory Office shall treat the excess amount (and interest accrued thereon at the Appropriate Discount Rate) as an Expiration Payment; provided, however, that the Concessionaire may agree to forgo such Expiration Payment in exchange for some other benefit, such as an adjustment to one or more of the coverage targets, that the Regulatory Office may at the time offer to the Concessionaire. Without prejudice to the obligation of MWSS to pay any such Expiration Payment on the Expiration Date, it is the intention of MWSS, should it choose to solicit bids from private parties for the right to operate the system following the Expiration Date, to obtain a lump-sum cash payment from such parties as part of the consideration for the awarding of such rights and to fund any Expiration Payment required by this Section from the proceeds of such cash payment.

The Concessionaire may charge Customers a CERA payment of one Peso per cubic meter of water consumed above the Standard Rates. Although CERA has historically been used by MWSS to adjust for exchange rate movements, that function will be performed through the operation of Section 9.3.1 (vi) of this Agreement.

9.2 Rate Adjustments

The Standard Rates for water and sewerage services shall be adjusted each year effective January 1 of each Charging Year, in accordance with (i) the Rates adjustment Limit forth in Section 9.2.2, (ii) the adjustment principles set forth in Section 9.2.2 and (iii) the procedures set forth in Section 9.2.3.

9.2.1 Rate Adjustment Limit

The Weighted Average Rates Increase implied by the Standard Rates proposed by the Concessionaire in respect of any Charging Year may not exceed the Rates Adjustment Limit.

If an any Charging Year the Weighted Average Rates Increase is less than the Rates Adjustment Limit, that shortfall shall not be recoverable in any way by the Concessionaire in a future Charging Year.

For purposes of calculating Weighting Year revenue, where the Weighting Year is 1996 or 1997, MWSS shall provide to the Concessionaire all information necessary to make the calculation in respect of periods occurring prior to the Commencement Date.

9.2.2 Rate Structure Adjustments

Other than adjustments pursuant to Section 9.2.3 below, all Standard Rates will be revised annually by the same percentage adjustment; provided, however, that the Concessionaire may, subject to the overall Rates Adjustment Limit, propose to the Regulatory Office that certain Standard Rates be revised by different percentage adjustments. In proposing different percentage adjustments, the Concessionaire shall have regard to the following:

- (i) the impact of the proposed adjustment upon the ability of low income domestic households to afford such charges;
- (ii) the desirability of sending economically efficient price signals to Customers;
- (iii) the desirability of reducing cross-subsidies between different Customers or groups of Customers (including cross-subsidies between water and sewerage Customers);and
- (iv) the desirability of removing any cross-subsidy between domestic Customers, as a group, and non-domestic Customers, as a group, as soon as practicable.

9.2.3.2 Different Rate Adjustments

Following the submission of proposed Standard Rates in accordance with Section 9.2.3 and if the Concessionaire is proposing that Standard Rates be revised by different percentage adjustments, the Regulatory Office shall notify the Concessionaire of its acceptance or rejection of the proposed Standard Rates, including verification that the proposal complies with the Rates Adjustment Limit, within 30 days. In the event that notification has not been given within 30 days, the Regulatory Office shall be deemed to have accepted the proposed rates and to have verified that they comply with the Rates Adjustment Limit.

In either accepting or rejecting the proposed Standard Rates, the Regulatory Office shall have regard to the principles described in Section 9.2.2 above, and in any case may not withhold approval if the proposed adjustments entail a reduction in cross-subsidies between Customers or groups of Customers and are likely to have no detrimental impact on affordability efficiency.

In the event that the concessionaire's Standard Rate proposals are rejected by the Regulatory Office, the Concessionaire may submit revised proposals based on uniform percentage adjustments within seven days of notification of the rejection. The Regulatory

Office shall verify the revised proposal complies with the Rates Adjustment Limit and notify the Concessionaire accordingly within 7 days.

9.2.4 Changes to Basis of Rates

In the event the Concessionaire proposes to make a change (other than one which relates solely to the level of Standard Rates in Section 9.2.3 above) to the basis on which the Concessionaire makes or calculates any Standard Rate (including a change in the application of discounts and surcharges to Standard Rates), the Concessionaire shall notify the Regulatory Office and submit sufficient supporting information to enable the Regulatory Office to verify that the proposal is consistent with the Rates Adjustment Limit for that Charging Year.

Upon receipt of such a proposal, the Regulatory Office shall determine within 60 days whether or not to accept the proposal. In the event the Regulatory Office cannot verify whether the proposal is consistent with the Rates adjustment Limit for that Charging year, the Concessionaire may either submit an interim Standard Rates adjustment proposal for the following Charging Year, in accordance with Section 9.2.5 below, or defer its proposed change for consideration under the rate adjustment provisions set forth in Section 9.2.

9.2.5 Interim Standard Rate Adjustments

Without prejudice to Section 9.2.3 above, the Concessionaire may at any time make an interim Standard Rates adjustment proposal to the Regulatory Office, for Implementation during the Charging Year, but not before the first day of the calendar month following 90 days from submission of such proposal. The Concessionaire shall submit sufficient supporting information to enable the Regulatory Office to verify that the Standard Rates proposal is consistent with the Rates Adjustment Limit.

In verifying that the interim Standard Rates proposal is consistent with the Rates Adjustment Limit, the Regulatory Office shall recalculate the Weighted Average Rates Increase for the Charging Year in which the interim Standard Rates adjustment is to apply as though the interim Standard Rates adjustment had been part of the original proposed Standard Rates for the Charging Year.

The Regulatory office shall notify the Concessionaire of its acceptance or rejection of the interim Standard Rates proposal, including verification that such proposal complies with the Rates Adjustment Limit, within 30 days.

In either accepting or rejecting the interim Standard Rates proposal, the Regulatory Office shall have regard to the principles described in Section 9.2.2 above, and in any case may not withhold approval if the proposed adjustments entail a reduction in cross-subsidiaries between Customers or Groups of Customers and are likely to have no detrimental impact on affordability and economic efficiency.

In the event that the Concessionaire's interim Standard Rates proposal is rejected by the Regulatory Office, the Standard Rates already agreed for that Charging Year shall continue to apply.

9.3 Extraordinary Price Adjustments

It is the intention of the parties that should certain unforeseen events occur during the term of the Concession, rates may be adjusted (up or down) to account for the financial consequences of such events. Such adjustments may occur from time to time as described in this Section 9.3.

In the event that one or more Grounds for Extraordinary Price Adjustment ("GEA"), as defined in Section 9.3.1 below, has occurred or is expected to occur, the Regulatory Office shall either (i) determine, in accordance with Section 9.3.2 below, an extraordinary price adjustments (an "Extraordinary Price Adjustment" or an "E") for the purposes of calculating the Rates Adjustment Limit to be applied to the Standard Rates appropriate adjustment to the Service Obligations.

The Concessionaire may at any time require the Regulatory Office to consider circumstances that the Concessionaire believes constitute Grounds for Extraordinary Price Adjustment. The Regulatory Office may also at any time notify the Concessionaire of circumstances that the Regulatory Office believes constitute Grounds for Extraordinary Price Adjustment, as set forth in Section 9.3.1 below.

9.3.1 Grounds for Extraordinary Price Adjustment

A Ground for Extraordinary Price Adjustment ("GEA") means any of the following circumstances(whether or not treated as an Expenditure or Receipt under this Agreement):

- (i) the Regulatory Office, following consultation with the Concessionaire, determines that amendments should be made to the Service Obligations;
- (ii) there is any change in law, government regulation, rule or order, or interpretation thereof, that affects or is likely to affect the Cash Flow of the Concessionaire;
- (iii) the Regulatory Office determines that a breach of this Concession Agreement has occurred and an appropriate remedy has not been made and will not be made;
- (iv) the Concessionaire has been or will be in receipt of a grant or below-market financing from any multilateral or bilateral source that may be used to finance or offset any Expenditures, where such grant or below-market financing was not known or anticipated at the Commencement Date,

or at the last Rate Rebasing Date, whichever is the most recent;

- (v) in the reasonable opinion of the Regulatory Office, a material change has been made to the basis of calculation or definition of the Consumer Price Index or replacement index agreed to pursuant to Section 2.4 above, which would render that index inappropriate for the purposes contemplated by Section 9.2.1 above;
- (vi) without regard to the CERA adjustment referred to in Section 9.1, (a) in respect of any MWSS Loan, a change of more than 2% has occurred after December 6, 1996 (the date of the distribution to the Concessionaire of the technical and business assumptions set forth in Exhibit E) in the rate of exchange between the Philippine peso and the currency in which such Concessionaire Loan is denominated, and, in either case, such change in exchange rates has not previously been the subject of an Extraordinary Price Adjustment.
- (vii) there exists an unpaid penalty amount owed by the Concessionaire to the Regulatory Office pursuant to Section 10.4;
- (viii) in the reasonable opinion of the Regulatory Office, the bidding assumptions distributed to the Concessionaire prior to the bid (and attached hereto as Exhibit E) have proven to be incorrect in a material way during any period prior to the first general rate rebasing pursuant to Section 9.4.2;
- (ix) an increase has occurred in the Concession Fee as a result of Cost Overruns for the UATP project;
- (x) the financial performance of the Concessionaire has been materially affected as a result of a delay in the completion of the UATP project beyond June 30, 1999; or
- (xi) the Concessionaire has incurred significant additional costs as a result of an Event of Force Majeure which are not covered by insurance.

In order to qualify for an Extraordinary Price Adjustment to be incorporated into the Rates Adjustment Limit for any Charging Year, notification by the Regulatory Office and/or, as the case may be, the Concessionaire, that one or more GEAs have occurred or are expected to occur shall be made by March 31 of the previous Charging Year.

9.3.2 Determination of Extraordinary Price Adjustment

Upon determination by the Regulatory Office that one or more GEAs have occurred, the Regulatory Office shall, by taking into account all information available at the time, and by making reasonable projections of all factors relevant to the future Cash Flows of the Concessionaire, calculate:

- (i) the Cash Flows which would be caused by the GEA or GEAs (and, for this purpose, the circumstances referred to in Section 9.3.1 (iv) any exchange rate movement of the kind referred to in Section 9.3.1 (vi) shall be deemed to affect Cash Flows);
- (ii) the Net Present Value of those Cash Flows as at June 30 of the following Charging Year; and
- (iv) what Extraordinary Price Adjustment, positive or negative, made to the Rates Adjustment Limit for the following Charging Year would cause the Net Present Value as at June 30 of the Charging Year of the expected Receipts of the concessionaire for the period beginning January 1 of that Charging Year until the Expiration Date to change by an amount equal but opposite in sign to the Net Present Value of Cash Flows referred to in (ii) above.

In the event that such calculation indicates that the appropriate Extraordinary Price Adjustment is between zero and plus 1% then the Regulatory Office shall determine that the Extraordinary Price Adjustment is zero.

The Regulatory Office shall determine what Extraordinary Price Adjustment should be made for any Charging Year by May 31 prior to the beginning of that Charging Year and shall notify the Concessionaire in writing setting out the basis for such determination.

9.3.3 Concessionaire's Right of Appeal

In the event that the Concessionaire:

- (i) has notified the Regulatory Office that, in the opinion of the Concessionaire, one or more GEAs have occurred or are expected to occur but the Regulatory Office has not concurred with that opinion; or
- (ii) objects to the Regulatory Office's determination of an Extraordinary Price Adjustment or adjustment to the Service Obligations, then

the Concessionaire may, not later than June 30 of that year, refer the matter to the Appeals Panel. Within 30 days after any such referral, the Concessionaire and the Regulatory Office shall each file its submission with the Appeals Panel and the Appeals Panel shall thereafter conduct an investigation into the matter in accordance with Article 12. Consequently, the Appeals Panel shall render a decision as to whether one or more GEAs have occurred and, if so, the appropriate level of Extraordinary Price Adjustment or adjustment to the Service Obligations, by September 30 of the year in which the referral is made.

9.3.4 General Rates Setting Policy/Rate Rebasing Determination

The maximum rates chargeable by the Concessionaire for water and sewage services hereunder applicable to the period through the Second Rate Rebasing Date (subject to interim adjustment's as described in this Article 9) are set out in Schedule 5 to this Agreement. It is the intention of the parties that, from and after the Second Rate Rebasing Date, the rates for water and sewerage services provided by the Concessionaire shall be set at level that will permit the Concessionaire to recover over the 25-year term of the Concession (net of any grants from third parties and any possible Expiration Payment) operating, capital maintenance and investment expenditures efficiently and prudently incurred, Philippine business taxes and payments corresponding to debt service on the MWSS Loans and Concessionaire Loans incurred to finance such expenditures, and to earn a rate of return (referred to herein as the "Appropriate Discount Rate") on these expenditures for the remaining term of the Concession in line with the rates of return being allowed from time to time to operators of long-term infrastructure concession arrangements in other countries having a credit standing similar to that of the Philippines. The parties further agree that the maximum rates chargeable for such water and sewerage services shall be subject to general adjustment at five-year intervals commencing on the second Rate Rebasing Date; provided that the Regulatory Office may exercise its discretion to make a general adjustment of such rates on the First Rate Rebasing Date, but, if it does not do so, the Regulatory Office shall implement the assumptions set out in paragraph 2 of Exhibit E on the fifth anniversary of the Commencement Date. It is understood that the determination of the appropriate rate of return will be made separately at the time of each generalized rate rebasing.

It is also the intention of the parties that rates be set in such a way as to provide appropriate efficiency incentives to the Concessionaire, with a view toward benefiting both the Customers and the Concessionaire.

The Regulatory Office shall determine the Rebasing Adjustment to be used for the purposes of calculating the Rates Limit for each of the five Charging Years of each Rebasing Period, in accordance with the provisions set forth below.

9.4.1 Concessionaire's Information

Not later than March 31 preceding each Rate Rebasing Date, the Concessionaire shall supply the Regulatory Office with information on its Expenditures, Receipts, Cash

Flows, Opening Cash Position and Future Cash Flows in a form and manner, and covering such time periods, as the Regulatory Office may determine.

The Concessionaire shall also provide such other information as the Regulatory Office may reasonable request or as the Concessionaire may wish to provide.

9.4.2 Rebasing Adjustment

For the purpose of determining the Rates Adjustment Limit to apply to Standard Rates to come into effect on a Rate Rebasing Date commencing with the second Rate Rebasing Date, and the Rates Adjustment Limits for the following four Charging Years, the Regulatory Office shall, by taking into account all information available at the time, and by making reasonable projections of all factors relevant to the future Cash Flows of the Concessionaire, determine;

- (i) the Net Present Value, which may be either positive or negative, of the Opening Cash Position, as at June 30 following that Rate Rebasing Date;
- (ii) the amount, either positive or negative, which if made to the Rates Adjustment Limit for the following Charging Year would cause the Net Present Value of the Future Cash Flows, as at June 30 following that Rate Rebasing Date, to be equal but opposite in sign to the Net Present Value of the Opening Cash Position as determined in (i) above (the "Rebasing Adjustment")

Notwithstanding the foregoing, the regulatory Office may, in its sole discretion, implement a general rate rebasing consistent with this Section 9.4.2 on the first Rate Rebasing Date if the Regulatory Office determines that circumstances warrant such an action.

9.4.3 Rebasing Convergence Adjustment

The "Rebasing Convergence Adjustment" to be used for the purposes of calculating the Rates Adjustment Limit for each of the five Charging Years of the Rebasing Period shall be determined as follows;

- (i) where the Rebasing Adjustment is found to be positive, the Rebasing Convergence Adjustment for the first Charging Year of the Rate Rebasing Period shall be equal to the Rebasing Adjustment, and the Rebasing Convergence Adjustment for each of the following four Charging Years shall be zero; and

- (ii) where the Rebasing Adjustment is found to be negative, the Rebasing Adjustment for each of the five Charging Years of the Rebasing Period shall be equal to the Rebasing Adjustment divided by five.

The Regulatory Office shall notify the Concessionaire in writing of each of the rebasing Convergence Adjustments that will apply in respect of the following Rate Rebasing Period by June 30 prior to the Rate Rebasing Date.

9.4.4 Expiration Payment

In the event that the Regulatory Office determines, at any time from and after the second Rate Rebasing Date, that the Concessionaire shall incur significant capital expenditures in carrying out the Concessionaire's responsibilities under this Agreement which (in the judgment of the Regulatory Office) should not be recovered through immediate rate adjustments, the

Regulatory Office may propose to the Concessionaire that this Agreement be amended to provide for the payment to the Concessionaire on the Expiration Date of a lump-sum amount designed to reimburse the Concessionaire for all or a portion of such unforeseen capital expenditure (the "Expiration Payment"). Any Expiration Payment shall be treated by the Regulatory Office as an anticipated Receipt for purposes of making rate adjustment calculations under this Article 9. Any Expiration Payment may be discharged through the delivery to the Concessionaire of a U.S. Dollar-denominated debt instrument issued by MWSS or by another public-sector entity owned by the Republic but, in either case, with the full faith and credit guarantee of the Republic, ranking at least pari passu with all other unsecured and unsubordinated external debt obligations of the Republic, having a cash value to such Expiration Payment.

9.4.5 Concessionaire's Right of Appeal

If the Concessionaire disputes a determination by the Regulatory Office made in accordance with Section 9.4.2, the Concessionaire shall have until July 31 prior to the Rate Rebasing Date to refer the matter to the Appeals Panel for determination, as described in Section 12.4 (ii) below.

9.5 Connection Charges

- (i) For connections or reconnections to a water main or a public sewer (each a "Connection") that are both located less than 25 meters from the connection point and are to residential Customers the Concessionaire shall have the right to charge each Customer requesting such a Connection a fee not to exceed P3,000, which amount shall automatically be adjusted on January 1st of each year by the percentage change in the Consumer Price Index for the preceding year (each a "Connection Charge"). Within three months after

the Commencement Date, the Concessionaire shall with the approval of the Regulatory Office promulgate rules that permit payment of Connection Charges in installments over a five-year period by Low-Income Customers.

- (iii) For Connections to a water main or a public sewer located more than 25 meters from the connection point or for Connections to non-residential Customers, the Concessionaire shall have the right to charge each Customer requesting such a Connection a fee equal to the costs reasonably and efficiently incurred by the Concessionaire in making that Connection, including the costs of upgrading or restoring existing connections or metering facilities to acceptable technical standards.

Notwithstanding anything to the contrary in this Section 9.5, there shall be no connection charge for public standpipes.

9.5.1 Notification to Customer

Within five days after receiving a request from a customer for a Connection, the Concessionaire shall notify the Customer in writing of the proposed charge for making that Connection. Subject to Section 5.1.3 and Section 5.2.2, Connections shall be carried out by the Concessionaire as promptly as may be practicable following the Customer's written acceptance of the related charge. A Customer shall have the right to notify the Regulatory Office if it objects to the charge proposed by the Concessionaire and the Regulatory Office shall determine in its sole opinion whether such Charge is reasonable and notify the Concessionaire whether an adjustment is required.

9.5.2 Authority to Prescribe Maximum Connection Charges

If the Regulatory Office determines at any time that the Concessionaire is setting charges for connections that are inconsistent with the standards set out in Section 9.5 (ii) above, the Regulatory Office, upon not less than 30 days' prior written notice to the Concessionaire, shall have the authority to prescribe a schedule of maximum charges consistent with those standards.

ARTICLE 10. EVENTS OF EARLY TERMINATION; PENALTIES

10.1 MWSS Event of Termination

Each of the following events shall constitute an "MWSS Event of Termination" under this Agreement:

- (i) MWSS, acting on its own behalf or at the direction of any Philippine governmental authority, shall make an assignment

for the benefit of creditors, petition or apply to any tribunal for a receiver or a trustee for itself or for any substantial part of its property, commence any judicial or other legal proceedings by reason of its financial difficulties under any reorganization, arrangement, readjustment of debt, dissolution, or liquidation law or statute of any jurisdiction, whether now or hereafter in effect; or there shall be commenced against such party any such proceeding which shall remain undismissed for a period of 60 days, or such party shall by any act indicate its consent to, approval of, or acquiescence, in any such proceeding or the appointment of any receiver of, or trustee for, it or any substantial part of its property, or shall suffer any such receivership or trusteeship to continue undischarged for a period of 60 days; or there shall be any reorganization, arrangement, readjustment of debt, dissolution, or liquidation with respect to such party which does not involve a judicial proceeding and the occurrence of any or all of the above events shall materially impair the rights of the concessionaire under this Agreement;

- (ii) The Undertaking Letter, or any governmental authorization or approval necessary to enable MWSS perform any of its material obligations under this Agreement, shall be revoked, withdrawn or withheld or shall otherwise fail to be issued or to remain in full force and effect; and
- (iii) MWSS shall fail to perform an obligation under this Agreement of a kind or to a degree that such failure effectively prevents the Concessionaire from carrying out its responsibilities under this Agreement and such failure continues for a period of not less than 30 days after written notice from the concessionaire to MWSS.

10.2 Concessionaire Event of Termination

Each of the following events shall constitute a "Concessionaire Event of Termination" under this Agreement:

- (i) The Concessionaire shall make an assignment for the benefit of creditors, petition or apply to any tribunal for a receiver or a trustee for itself or of any judicial or other proceedings by reason of its financial difficulties under any reorganization, arrangement, readjustment of debt, dissolution, or liquidation law or statute of any jurisdiction, whether now or hereafter in effect; or there shall be commenced against such party any such proceeding which

shall remain undismissed for a period of 60 days, or such party shall by any act indicate its consent to, approval of, or acquiescence in, any such proceeding or the appointment of any receiver of, or trustee for, it or any substantial part of its property, or shall suffer any such receivership or trusteeship to continue undischarged for a period of 60 days; or there shall be any reorganization, arrangement, readjustment of debt, dissolution, or liquidation with respect to such party which does not involve a judicial proceeding;

- (ii) The Concessionaire shall fail to perform an obligation under this Agreement of a kind or to a degree such that (a) in the reasonable opinion of the Regulatory Office, such failure amounts to an effective abandonment of the Concession Agreement because it jeopardizes the provision of essential water and sewerage supply services in all or any significant part in the Service Area and (b) such failure continues for a period of not less than 30 days after written notice from the Regulatory Office to the Concessionaire;
- (iii) The Concessionaire shall in the reasonable opinion of the Regulatory Office, fail to perform any material obligation of the Concessionaire set out in this Agreement (other than an obligation described in (ii) above) for which the Regulatory Office shall have determined that a financial penalty pursuant to Section 10.4 would be inappropriate or ineffective, if such failure shall continue for a period of not less than 180 days after written notice from the Regulatory Office to the Concessionaire;

10.3 Early Termination Procedures

10.3.1 Notice

If a Concessionaire Event of Termination shall have occurred and be Continuing, the Regulatory Office may give written notice of the early termination of the Concession to the Concessionaire (with a copy to the Appeals Chairman), and the Concession granted hereby shall terminate 60 days after the date of such notice unless such termination is stayed by the Appeals Panel or the Concession Lenders notify MWSS of their intention to exercise their right to nominate a Qualified Replacement Operator pursuant to Section 10.3.2 (iii)(A). If an MWSS Event of Termination shall occur and be continuing the Concessionaire may give written notice of the early termination of the Concession to MWSS (with a copy to the Appeals Panel), and the Concession granted hereby shall terminate on the date set out in such notice (which date shall not be less than 60 days, nor more than 180 days, after the date of such notice) unless such termination is stayed by the Appeals Panel. The date of early termination specified in a notice delivered

pursuant to this Section 10.3.1, as such date may be extended by the Appeals Panel as a result of a stay, is referred to herein as the “Early Termination Date”.

10.3.2 Early Termination

- (i) Within 30 days after the giving of any notice terminating the Concession pursuant to Section 10.3.1, the Regulatory Office shall determine the amount (the “Early Termination Amount”) payable in accordance with clause (ii) of this Section 10.3.2 following an MWSS Event of Termination, or payable in accordance with clause (iii) of this Section 10.3.2 following a Concessionaire Event of Termination. The Regulatory Office shall promptly give written notice to each of MWSS, the Concessionaire and the Appeals Panel of the Early Termination Amount and shall furnish a copy of all supporting calculations.

- (ii) Following an MWSS Event of Termination:
 - (A) the then-outstanding amount of all Concessionaire Loans (including the short-term portion thereof) shall be assumed by MWSS or by another public-sector entity owned by the Republic, but in either case, with a full faith and credit guarantee of the Republic, ranking at least pari passu with all other unsecured and unsubordinated external debt obligations of the Republic;

 - (B) the Concession (including all fixed assets existing as of the Early Termination Date but excluding all current assets and current liabilities other than the short-term portion of the Concessionaire Loans) shall revert to MWSS for a payment to the Concessionaire (the “Early Termination Amount”) equal to an amount, determined by an outside auditor appointed by the Regulatory Office, equal and opposite in sign to the Net Present Value as at the Early Termination Date of the Cash Flows occurring between the Commencement Date and the Early Termination Date of the Cash Flows occurring between the Commencement Date and the Early Termination Date less the then-outstanding amount of the Concessionaire Loans (in the event that such Early Termination Amount is a negative

number, the Early Termination Amount shall be deemed to be zero); and

- (C) the Early Termination Amount payable by MWSS under this Section 10.3.2 (ii) may either:
 - (1) be paid by MWSS in a lump sum payment not later than 45 days after the Early Termination Date or
 - (2) at the option of MWSS, be discharged through the delivery to the Concessionaire of a U.S. Dollar denominated debt instrument issued by MWSS or by another public-sector entity owned by the Republic but, in either case, with the full faith and credit guarantee of the Republic, ranking at least pari passu with all other unsecured and unsubordinated external debt obligations of the Republic, having a cash value (if discounted in the secondary market on the date of delivery thereof to the Concessionaire) equal to the Early Termination Amount.
- (iii) Following a Concessionaire Event of Termination:
- (A) All of the concessionaire's right, title and interest in the Concession shall be assigned by the Concessionaire to a Qualified Replacement Operator (acceptable to the Regulatory Office) nominated by the Concessionaire Lenders; provided however, that if the Concessionaire Lenders do not nominate such a Qualified Replacement Operator within 6 months of a notice terminating the Concession pursuant to Section 10.3.1, MWSS shall pay to the Concessionaire the Early Termination Amount (set forth in sub-clause (B) below) and the Concession shall thereupon automatically terminate and revert to MWSS with no further liability or obligations on the part of MWSS to the Concessionaire or to the Concessionaire Lenders. In either case, MWSS may draw upon the Performance Bond to recover from the Concessionaire an amount equal to the out-of-pocket costs and expenses incurred by MWSS as a result of such Concessionaire Event of Termination.

- (B) In the event that the Concessionaire Lenders do not nominate Qualified Replacement Operator pursuant to sub-clause (A) above, the Concessionaire and MWSS agree that it would not be feasible to determine the total amount of losses, costs and expenses that MWSS would incur as a result of a Concessionaire Event of Termination. Accordingly, MWSS and the Concessionaire agree that, as a reasonable pre-estimate of such losses, costs and expenses, following a Concessionaire Event of Termination, the Concession (including all current and fixed assets existing as of the Early Termination Date, but excluding any liabilities associated therewith) shall revert to MWSS for a discounted payment, (the “Early Termination Amount”), which shall equal 75 percent of the value of such current assets and 75 percent of the depreciated value of all fixed assets installed by the Concessionaire in the Service Area after the Commencement Date (excluding Disapproved Assets) and all improvements to such fixed assets existing in the Service Area on the Commencement Date, determined as of the Early Termination Date by an outside auditor appointed by the Regulatory Office in accordance with Philippine generally accepted accounting principles, provided, however, that the Early Termination Amount shall not exceed the then-outstanding Concessionaire Loans and any other indebtedness incurred by the Concessionaire in connection with the Concession and provided further, however, that such Early Termination Amount (or the cash proceeds from the sale of the debt from the sale of the debt instrument referred to in clause (C) (2) below) shall be applied to repay then-outstanding Concessionaire Loans and any such other indebtedness.
- (C) the Early Termination Amount payable to the Concessionaire by MWSS under sub-clause (B) of this Section 10.3.2 (iii) may either:
- (1) be paid by MWSS in a lump sum payment not later than 45 days after the Early Termination Date or
 - (2) at the option of MWSS, be discharged through the delivery to the Concessionaire of a U.S. Dollar-

denominated debt instrument issued by MWSS or by another public –sector entity owned by the Republic, ranking at least pari passu with all other unsecured and unsubordinated external debt obligations of the Republic, having a cash value (if discounted in the secondary market on the date of delivery thereof to the Concessionaire) equal to the Early Termination Amount.

10.3.3 Appeal

- (i) Upon receipt of a notice of early termination pursuant to Section 10.3.1 above (other than a notice which specifies an MWSS Event of Termination of the kind described in Section 10.1 (i) or a Concessionaire Event of Termination of the kind described in Section 10.2 (i) above), the recipient shall have the right within 30 days thereafter to refer the matter to the Appeals Panel and to seek a stay in connection with such Appeal. The Appeals Panel shall have 60 days from receipt of such notice to deliver its determination by written notice to the Regulatory Office and the Concessionaire in accordance with Article 12. Until such determination is made by the Appeals Panel, the Concession shall continue and the parties shall continue to perform their respective obligations hereunder.
- (ii) Either the Concessionaire or MWSS may challenge the calculation of the Early Termination Amount by written referral to the Appeals Panel made within 30 days after receipt of the Regulatory Office’s calculation of the Early Termination Amount. The challenging party shall indicate in its referral the amount that it believes is the appropriate termination amount calculated in a manner consistent with Section 10.3.2 above. Within 60 days of any such referral, the Appeals Panel shall either confirm the Early Termination Amount determined by the Regulatory Office or confirm the termination amount proposed by the Challenging Party, whichever the Appeals Panel finds is most consistent with the requirements of Section 10.3.2 above.

10.4 Penalties for Failure to Meet Service Obligations

A failure by the Concessionaire to meet any Service Obligation which continues for more than 60 days (or 15 days in cases where the failure could adversely affect public health or welfare) after written notice thereof from the Regulatory Office to the Concessionaire shall constitute a basis for the Regulatory Office to assess financial penalties against the Concessionaire. The amount of any such penalty shall be equal to 25% of the costs that, in the reasonable opinion of the Regulatory Office, the Concessionaire will incur in order to meet the Service Obligation in question; provided, however, that if the Concessionaire does not meet such Service Obligation within 180 days, the amount of the penalty shall be equal to 50% of such costs. The Concessionaire shall pay any penalties assessed in connection with this Section to the Regulatory Office within 30 days after receipt of a demand thereof. Such penalties shall not be regarded as an Expenditure of the Concession. In the event the Concessionaire fails to make timely payment of an assessment pursuant to this Section 10.4, the Regulatory Office may draw the U.S. dollar equivalent of such unpaid amount under the Performance Bond in accordance with Section 6.9 above or may treat such non-payment as a GEA in accordance with Section 9.3.1. Notwithstanding the foregoing, no penalties will be assessed in respect of any failure to meet water quality standards identified by this Section 10.4 unless such failure continues after 12 months following the Commencement Date. All penalties received by the Regulatory Office pursuant to this Section 10.4 shall be rebated to Customers affected by the Concessionaire's failure to meet Service Obligations in such manner as the Regulatory Office deems appropriate.

ARTICLE 11. REGULATORY OFFICE

11.1 Organization

The MWSS Board of Trustees shall establish and fund a regulatory Office (the "Regulatory Office") to be organized and operated in a manner consistent with the MWSS Board of Trustees may make from time to time, and shall have the functions and powers described in that Exhibit. Decisions of the Regulatory Office requiring action by the MWSS Board of Trustees, including decisions affecting the level of Standard Rates, shall promptly be submitted to the Board in accordance with Section 7.1 hereof.

11.2 Funding

Not later than 10 days after the Commencement Date, MWSS shall allocate from the Concession Fees received from the Concessionaire and the Other Operator the amount of 100 Million Pesos which shall constitute the budget of the Regulatory Office for the year 1997. Not later than January 10 of each subsequent year, MWSS shall allocate from the Concession Fees paid in that year by the Concessionaire and the Other Operator the annual budget for the Regulatory Office and MWSS for that year, provided that such annual budget shall not for any year exceed 200 Million

Pesos, subject to annual CPI adjustments, 100 Million Pesos of which, as so adjusted, shall be allocated by MWSS for the Regulatory Office.

ARTICLE 12. DISPUTE RESOLUTION

12.1 Consultation

The parties hereto agree to use reasonable efforts to resolve any disagreements or disputes concerning the interpretation or implementation of this Concession Agreement through mutual consultation and negotiation.

12.2 Arbitration

All disagreements, disputes, controversies or claims arising out of or relating to this Agreement or the interpretation hereof or any arrangements relating hereto or contemplated herein or the breach, termination or invalidity hereof (including all decisions by the Regulatory Office with respect to the Concession) which cannot be resolved through consultation and negotiation among the parties hereto shall be finally settled by an arbitration proceedings in accordance with the arbitration rules of the United Nations Commission on International Trade Law as in effect on the dates of this Agreement (the "Rules"), except insofar as the Rules conflict with the provisions of this Agreement.

12.3 Composition of Appeals Panel

Not less than 30 days to the commencement of each Rate Rebasing period, the Concessionaire and the Regulatory Office shall each appoint one member of the Appeals Panel to serve for the following Rate Rebasing Period. If either party fails to appoint a member shall be appointed by the President (for the time being) of the International Chamber of Commerce. (in the case of disputes between the Concessionaire and the Other Operator, on the one hand, and MWSS, on the other, the Concessionaire and the Other Operator shall jointly agree on the appointment of one member to the Appeals Panel). For matters involving Major Disputes (as defined below), the President (for the time being) of the International Chamber of Commerce shall designate a third member shall act as the chairman of the Appeals Panel (the "Appeals Chairman"). For matters involving Minor Disputes (as defined below), the two members so appointed shall designate a third member and the third member shall act as the Appeals Chairman. Each member of the Appeals Panel (other than the Appeals Chairman) shall be a resident (but need not be a citizen) of the Philippines. Members appointed to the Appeals Panel shall be individuals of good business reputation who have no prior business connection with any party to this Agreement or with the Other Operator. In the event of the death, incapacity or resignation of any member of the Appeals panel, the appointing party (including, where appropriate, the President of the International Chamber of Commerce) for such members shall promptly appoint a successor to serve out the unexpired term of

such member. An individual may be reappointed to serve on the Appeals Panel for more than one Rate Rebasing Period.

12.4 Procedures

The Appeals Panel shall decide Disputes in accordance with the following procedure:

- (i) Disputes may be referred to the Appeals Panel by any party hereto by providing written notice to the Appeals Chairman of the Appeals Panel and the other parties hereto (each a "Dispute Notice") setting out in reasonable detail the circumstances of such dispute.
- (ii) Disputes related to (A) a Rebasing Dispute (described below), (B) an appeal of the determination of a GEA or Extraordinary Price Adjustment pursuant to Section 9.3.3, (C) an appeal of the calculation of the Termination Amount pursuant to Section 10.3.3, (D) the amount and price of Bulk Water transported from Service Area West to Service Area East, (E) the delegation of responsibilities between the concessionaire and the Other Operator in the Joint Venture or (F) a contested notice of termination pursuant to Section 10.3.1 (each a "Major Dispute") shall be referred to an Appeals Panel constituted under the chairmanship of a Appeals Chairman appointed by the President of the International Chamber of Commerce. All Disputes other than Major Disputes (each a "Minor Dispute") shall be referred to the Appeals Panel as provided in Section 12.3 above.
- (iii) Dispute Notices referred by the Concessionaire relating to Rate Rebasing Adjustments (each a "Rebasing dispute") shall include a detailed description of the Concessionaire's alternative description of the Concessionaire's alternative proposal for a Rate Rebasing Adjustment for the next Rate Rebasing Period, together with information as to how such Adjustment was calculated. The Regulatory Office shall have 15 days after receipt of notice of a Rebasing Dispute in which to submit to the Appeals Panel the Rate Rebasing Adjustment for the next Rate Rebasing Period determined by the Regulatory Office in accordance with Section 9.4.2 above, together with information as to how such Adjustment was calculated. After making such investigation and conducting such hearings into the matter as the Appeals Panel deems appropriate, the Appeals panel shall, by not

later than September 30 of the year in which a Rebasing Dispute is referred to it, accept either the Rate Rebasing Adjustment as determined by the Regulatory Office or the alternative Rate Rebasing Adjustment proposed by the Concessionaire.

- (iv) Dispute Notices may be referred by the Concessionaire or the Other Operator in connection with matters arising under the Interconnection Agreement or the supply of Raw Water pursuant to Section 3.9 (each a “ Raw Water Dispute”). The Raw Water Agreement shall contain a dispute resolution provision submitting all disputes under that Agreement to the Appeals Panel in a manner consistent with this Article 12.
- (v) All disagreements, disputes, controversies or claims referred to the Appeals Panel, other than those involving a Rebasing Dispute, shall be decided in such manner as the Appeals Panel determines in its sole discretion to be appropriate.
- (vi) Except as otherwise set forth herein, the Appeals Panel shall make a decision on any matter referred to it within a period of 90 days from receipt of a dispute Notice. Such decision period may be extended by mutual agreement of the parties to the dispute. Each decision must have the written concurrence of at least two of the three members of the Appeals Panel.
- (vii) The Appeals Panel may stay any termination of the Concession as notified pursuant to Section 10.2.2 pending its determination of the validity of such termination.
- (viii) The Appeals Panel may retain the services of legal, economic and technical consultants as the Panel deems appropriate.
- (ix) The Appeals Panel proceedings shall be held in English, and the place for the proceedings shall be Manila.
- (x) The appeals Panel may from time to time adopt procedural rules or guidelines consistent with the terms of this Concession Agreement, and such rules and guidelines shall be binding on the parties hereto.

12.5 Waiver of Right to Appeal

Any decision or award of the Appeals Panel shall be final and binding upon the parties hereto. To the maximum extent permitted by applicable law, each party hereby waives any right to seek any interlocutory or other relief from any judicial or regulatory body, or to appeal or seek the review of an Appeals Panel award by any court, regulatory body or other tribunal. Each of the parties hereto agrees that an award of the Appeals Panel may be enforced against it or its assets wherever they may be found and that judgment upon such award may be entered in any court having jurisdiction thereof. Each such party hereby waives and agrees not to plead any immunity (whether on the basis of sovereignty or otherwise) to which such party or its assets might otherwise be entitled in connection with any such enforcement proceeding.

12.6 Costs of the Panel

- (i) Incurred by the Appeals Panel in connection with any proceeding brought before it relating solely to the Concession (including the fees and expenses of panel members and legal, economic or technical consultants retained by the Appeals Panel), shall be apportioned between the parties as the Appeals Panel shall direct and the Concessionaire's share of such costs shall be treated as an Expenditure. One half of the estimated costs of each proceeding (as determined by the Appeals Panel) shall be due prior to the Commencement of such proceeding. The Appeals Panel shall invoice the appropriate party or parties for the balance of such costs within 30 days of delivering its decision in respect of each proceeding and such balance shall be payable within 10 days after receipt of the invoice.
- (ii) The Appeals Chairman shall be entitled to a per diem compensation at such rate as the President of the International Chamber of Commerce may recommend. The other members of the Appeals Panel shall each be entitled to a per diem compensation equal to 2,500 Pesos per day (or portion of a day) while in session. This per diem rate shall automatically be adjusted on January 1st of each year by the percentage change in the Consumer Price Index for the preceding year.
- (iii) In any proceeding in which the Concessionaire, the Other Operator or MWSS are parties, the Appeals Panel shall assess costs ratably to the parties to such proceeding.
- (iv) In the event the Concessionaire does not make timely payment of any charges payable by its pursuant to this Section 12.6., the U.S. dollar equivalent of such unpaid

amount may be drawn under the Performance Bond in accordance with Section 6.9 above

- (V) The Appeals Panel shall be entitled to use the secretarial and administrative support services of the Regulatory Office free of charge.

ARTICLE 13. INFORMATION AND REPORTING REQUIREMENTS

13.1 General Requirements to Provide Information

The Concessionaire shall have a general duty to provide to the Regulatory Office all information that the Regulatory Office may reasonably require in order to permit the Regulatory Office to monitor the Performance of the Concessionaire in relation to its obligations under this Agreement. Such information shall include, and not limited to:

13.1.1 Service Performance Information

The Concessionaire shall provide to the Regulatory Office not more than 30 days following the end of each calendar quarter a report of its performance with respect to the provision of water and sewerage services in the Service Area which shall contain the information specified in Schedule 6 hereto, as such Schedule may be revised by the Regulatory Office from time to time.

13.1.2 Financial Information

The Concessionaire shall provide to the Regulatory Office not later than 60 days following the end of each calendar year a report of the financial performance of the Concession. Such report shall include (i) an analysis of revenue by source and revenue from other sources, (ii) an analysis of operating costs which distinguishes between water supply, sewerage and other services, (iii) an analysis of capital expenditures and investments which distinguishes between water supply, sewerage and other services, and (iv) the other information specified in Schedule 7 hereto, as such Schedule may be revised by the Regulatory Office from time to time.

13.2 Audits

Not less frequently than once a year, the Concessionaire's books and records shall be audited by an independent auditor appointed by, or acceptable to, the Regulatory Office, pursuant to internationally accepted accounting practices. In addition, the Regulatory Office may, upon giving not less than 15 days' prior written notice to the Concessionaire, require that the Concessionaire, require that the Concessionaire's books and records relating to the Concession to be audited on an interim basis by the Regulatory Office or by an outside auditor. The Concessionaire shall cooperate fully with all such audits.

ARTICLE 14. INDEMNITIES

14.1 Concessionaire Indemnity

The Concessionaire shall indemnify and hold MWSS and its employees, servants and agents harmless from and against any and all liabilities, claims, demands, actions, suits, losses, damages, costs and expenses (including reasonable attorney's fees) payable to third persons resulting from the operation and maintenance of the Facilities by the Concessionaire, and the performance by the Concessionaire of its obligations under the Concession, on or after the Commencement Date, except to the extent of any foregoing results from the negligence or willful misconduct of MWSS.

14.2 MWSS Indemnity

MWSS shall indemnify and hold the Concessionaire and its respective employees, servants and agents harmless from and against any and all liabilities, claims, demands, actions, suits, losses, damages, costs and expenses (including reasonable attorney's fees) payable to third persons arising out of the operation and maintenance of the Facilities by MWSS prior to the Commencement Date.

14.3 Procedures for Indemnification

Each of MWSS and the Concessionaire shall promptly notify the other of any claim for indemnification pursuant to any of the above Sections in this Article 14 and shall include sufficient information to enable the other party to assess the circumstances relating to such claim or potential claim. Each of MWSS and the Concessionaire shall cooperate fully with the other party in defense of any such claims. The indemnifying party shall have the right to assume the defense, appeal or settlement of such claims with respect to which indemnify has been invoked within 20 days after receipt of notice thereof from such indemnified party.

ARTICLE 15. CONDITIONS PRECEDENT

15.1 General Conditions

The obligation of each party hereto to effect the transactions contemplated by this Agreement shall be subject to the satisfaction at or prior to the Closing Date of the following general conditions;

- (i) no order, statute, rule, regulation, executive order, injunction, stay, decree or restraining order shall have been enacted, entered, promulgated or enforced by any court of competent jurisdiction or governmental or regulatory authority or instrumentality having jurisdiction over the matter that restrains, prohibits or declares illegal the consummation of the transactions contemplated hereby, and no action, suit,

injury or proceeding shall have been instituted or threatened by any governmental or regulatory authority or instrumentality having jurisdiction over the matter that seeks to restrain, prohibit or declare illegal the consummation of the transaction contemplated hereby; and

- (ii) all waivers, consents, approvals or authorizations required to be obtained from, and all notices, declarations, reports or filings required to be made with, any governmental or regulatory authority or instrumentality in connection with the consummation of the transactions contemplated hereby, shall have been made or obtained.

15.2 Conditions to Obligations of MWSS

The obligations of MWSS to effect the transactions contemplated by this Agreement shall be subject to the satisfaction at or prior to the Closing Date of the following additional conditions, unless such conditions are waived by MWSS;

- (i) the Concessionaire shall have performed in all material respects the obligations required under this Agreement to be performed by it at or prior to the Closing Date;
- (ii) the representations and warranties of the Concessionaire contained herein be true and correct in all material respects at and as of the Closing Date as if made at and as of such date except to the extent that a different time is specifically stated in any such representation and warranty; and
- (iii) MWSS shall have received the documents and instruments set out below:
 - (a) an opinion from special Philippine counsel to the Concessionaire, acceptable to the Office of the Government Corporate Counsel dated as of the Closing Date and substantially in the form attached hereto as Exhibit B;
 - (b) a certificate, dated as of the Closing Date, from a duly authorized officer of the Concessionaire to the effect that the representations and warranties of the Concessionaire contained in this Agreement are true and correct in all material respects as of the Closing Date;
 - (c) all other documents, instruments, writings and other items required to be delivered by the

Concessionaire at or prior to the Closing Date pursuant to this Agreement or otherwise reasonably requested by MWSS in connection herewith;

- (d) certified true copies of resolutions adopted by the Board of Directors of the Concessionaire authorizing the execution, delivery and performance of this Agreement;
- (iv) and the Concessionaire and the Other Operator shall have entered into the Joint Venture.

15.3 Conditions to Obligations of the Concessionaire

The obligations of the Concessionaire to effect the transactions contemplated by this Agreement shall be subject to the satisfaction at or prior to the Closing Date of the following additional conditions, unless such conditions are waived by the Concessionaire:

- (i) MWSS shall have performed in all material respects the obligations required under this Agreement to be performed by it at or prior to the Closing Date;
- (ii) the representations and warranties of MWSS contained herein shall be true and correct in all material respects at and as of the Closing Date as if made at and as of such date except to the extent that a different date is specifically stated in any such representation and warranty;
- (iii) the Concessionaire shall have received the documents and instruments set out below:
 - (a) an opinion from the Office of the Government Corporate counsel, dated as of the Closing Date and substantially in the form attached hereto as Exhibit C;
 - (b) a certificate, dated as of the Closing Date, from a duly authorized officer of MWSS to the effect that the representations and warranties of MWSS contained in this Agreement are true and correct in all material respects as of the Closing Date;
 - (c) a copy of the letter setting forth Raw Water supply arrangements as described in Section 3.9 above;

- (d) an undertaking letter (the “Undertaking Letter”) from the Republic signed by the Secretary of Finance setting forth the undertaking of the Republic in connection with the transactions described in this Agreement substantially in the form of Exhibit D hereto;
- (e) copies of the releases and quitclaims referred to in Section 6.1.1 (i) above; and
- (f) certified true copies of resolutions adopted by the MWSS Board of Trustees authorizing the execution, delivery and performance of this Agreement.

ARTICLE 16. MISCELLANEOUS

16.1 Assignment

This Agreement and all the provisions hereof shall be binding upon and insure to the benefit of the parties hereto and their respective successors and permitted assigns. Neither this Agreement nor any rights hereunder shall be assigned by either party hereto, nor shall any party delegate any of its obligations hereunder, without the prior written consent of the other party, and any purported assignment or delegation absent such consent shall be void; provided, however, that the Concessionaire may assign its right to receive any payments or other consideration hereunder (including the right to receive any Termination Amount) as security for Concessionaire Loans.

16.2 Amendments

Any amendment of any provision of this Agreement shall be in a writing signed by the parties and acknowledged by the Republic acting through the Secretary of Finance.

16.3 Governing Law

THIS AGREEMENT SHALL BE GOVERNED BY AND CONSTRUED IN ACCORDANCE BY AND CONSTRUED IN ACCORDANCE WITH THE LAW OF THE REPUBLIC OF THE PHILIPPINES.

16.4 Notices

Any notices or other communications required or permitted hereunder or otherwise in connection herewith shall be in writing and shall be delivered personally (including by courier), telexed, sent by facsimile transmission or sent by certified or delivered personally, or if telexed or sent by facsimile transmission, when so transmitted or mailed, upon receipt, as follows:

If to MWSS to:

Metropolitan Waterworks and Sewerage System
Katipunan Road, Balara,
Quezon City 1105
Philippines

(with a copy to the Regulatory Office)
Attn: MWSS Administrator
Facsimile: 921-2887
Telephone: 922-3757 or 922-2959

If to the Concessionaire to:

Manila Water Company, Inc.
32/F, Tower One, Ayala Triangle, Ayala Avenue
Makati City, Metro Manila
Philippines

Attn:
Facsimile: 848-5646
Telephone: 848-5643

If to the Regulatory Office to:

Regulatory Office
c/o Metropolitan Waterworks and Sewerage System
Katipunan Road, Balara,
Quezon City 1105
Philippines

Attn: MWSS Administrator
Facsimile: 921-2887

or such other address as the person to whom notice is to given has furnished in writing to the other parties. A notice of change in address shall not be deemed to have been given until received by the addressee.

16.5 Counterparts

This Agreement may be executed in three counterparts or more, each of which when so executed shall be deemed an original, and all of which together shall constitute one and the same instrument.

16.6 Entire Agreement

This Agreement (including any Exhibits, Schedules, documents and instruments referred to herein) constitute the entire agreement and supersede all other prior agreements and understandings, both written and oral, among the parties. Each of the parties undertakes to execute such documents and perform such acts as may reasonably be necessary to give effect to this Agreement.

16.7 Headings

The descriptive headings of the several Articles and Sections of this Agreement are inserted for convenience only and do not constitute a part of this Agreement.

16.8 Expenses

Each party hereto shall bear its own expenses in connection with the preparation and negotiation of this Agreement and any related documents.

16.9 Third Party Beneficiaries

Except as otherwise expressly provided herein, this Agreement is not intended to confer upon any person other than the parties hereto any rights or remedies hereunder.

16.10 Force Majeure

No failure or omission to carry out or observe any terms, provisions or conditions of this Agreement shall give rise to any claim by any party against another party or be deemed to be a breach or default of this Agreement if the same shall be caused or arise out of an Event of Force Majeure, as defined below.

16.10.1 Events of Force Majeure

The following events shall constitute an "Event of Force Majeure": any war, declared or not, or hostilities or belligerence, blockade, revolution, insurrection, riot, public disorder, expropriation, requisition, confiscation, nationalization or prolonged obstruction of the exercise of rights or powers referred to in Section 7.2, export or import restrictions closing of harbors, docks, canals or other assistance to or adjuncts of shipping or navigation of or with any place, rationing or allocation, whether imposed by law, decree or regulation by, or by compliance of industry at the insistence of, any governmental authority of or within the Republic, or (B) fire, unusual flood, drought, earthquake, pollution of Raw Water (other than caused by the act or omission of the party invoking such Event of Force Majeure), volcanic eruption, storm, lightning, tide (other than normal tide), tidal wave, unusually severe weather conditions, perils of the sea, accidents of navigation or

breakdown or injury of vessels, accidents to harbors, docks, canals or other assistance to or adjuncts of shipping or navigation, epidemic, quarantine, strikes or combination of workmen, lockouts or other labor disturbances, or any other event, matter or thing wherever occurring, which shall not be within the reasonable control of the party affected thereby; provided, however, that no expropriation, requisition, confiscation, nationalization or prolonged obstruction of the exercise of rights or powers referred to in Section 7.2 by the Republic or any governmental authority of or within the Republic shall constitute an Event of Force Majeure relieving MWSS of any of its obligations hereunder.

16.10.2 Duties of Party Invoking an Event of Force Majeure

The party invoking an Event of Force Majeure shall (i) notify in writing each other party as soon as reasonably possible of the nature of the Event of Force Majeure and the extent to which the Event of Force Majeure suspends the affected party's obligations under this Agreement and (ii) resume performance of its obligations as soon as the effects of the Event of Force Majeure cease to exist.

16.10.3 Minimizing Loss Due to an Event of Force Majeure

The parties will consult with each other and take all reasonable steps to minimize the losses of either party resulting from an Event of Force Majeure.

16.11 Conduct of the Concessionaire Pending the Expiration Date

The Concessionaire hereby covenants that, from the date three months prior to and including the Expiration Date, unless MWSS shall otherwise consent in writing (which consent shall not unreasonably be withheld), the Concessionaire shall conduct the business and operations of the Concession in the ordinary and usual course in a manner consistent with past best practice and, without limiting the generality of the foregoing, the concessionaire shall:

- (i) use its reasonable efforts to preserve and maintain the Facilities and Inventories;
- (ii) maintain in accordance with its normal best practices all documents, agreements, contracts and other corporate records of MWSS relevant to its business and operations;
- (iii) at all times comply with all material laws, statutes, rules, regulations, orders and directives of any governmental authority having jurisdiction over the Concessionaire or its businesses, except in cases where the application thereof is being contested in good faith or is the subject of an appeal

or other legal challenge;

- (iv) give prompt written notice to MWSS of: (a) the commencement of any dispute or proceeding between the Concessionaire and any governmental body which, if determined adversely to the Concessionaire, could reasonably be expected to have a material adverse effect on the Concessionaire's business or financial condition; (b) the occurrence of any material event of default in any material agreement of the Concessionaire or any event which, upon a lapse of time or the giving of notice or both, would become a material event of default under any such agreement; and (c) the occurrence of any other event which has or could reasonably be expected to have a material adverse effect on the Concessionaire's business or financial condition;
- (v) not waive any valuable right owed to the Concessionaire; or
- (vi) not reorganize departments or otherwise revise its organizational structure in any material fashion, other than any such reorganization consistent with the terms hereof.

16.12 Reversion

Upon the expiration of this Concession on the Expiration Date, all of the rights duties and powers of the Concessionaire provided under the terms of this Agreement shall automatically revert to MWSS' successors or assigns; provided, however, that the Concessionaire bear all liabilities, and shall be entitled to receive and to retain all revenues, arising out of its operation of the Facilities prior to the expiration of the Concession. MWSS shall be solely responsible for any taxes, fees or duties payable in connection with such reversion. On the Expiration Date, the Concessionaire shall retain the all cash and marketable securities and Disapproved Assets (other than such assets which are integral to the MWSS system) and transfer to MWSS or its successors or assigns:

- (i) the Movable Property in its then-current condition;
- (ii) Inventory having a value (adjusted for CPI) at least equal to the Inventory made available to the Concessionaire on the Commencement Date pursuant to Section 3.5 hereof;
- (iii) Legal title (free of any liens or encumbrances) to new assets contributed by the Concessionaire pursuant to Section 1.15; and
- (iv) All reports, records, designs, manuals, asset registers, employment records, maps and plans associated with the provisions of water and sewerage services within the Service Area.

At the time of such expiration, MWSS shall have the option to rebid the Concession or undertake any other course of action it deems appropriate with respect to the Concession; it being understood that without their express approval at such time, neither MWSS nor the Republic shall incur any financial obligation in respect of such rebidding or other undertaking. This Agreement may not be renewed except with the express written consent of MWSS and the Republic.

16.13 Severability

The invalidity or unenforceability of any provision of this Agreement shall not affect the validity or enforceability of any other portion or provision. Any invalid or unenforceable portion or provision shall be deemed severed from this Agreement. The parties shall negotiate an equitable adjustment in the remaining portions or provisions of this Agreement to effect the underlying purposes of this Agreement.

IN WITNESS WHEREOF, each of the parties has caused this Concession Agreement to be executed on its behalf by its duly authorized officer, all as of the date first written above.

**METROPOLITAN WATERWORKS
AND SEWERAGE SYSTEM**

By: __ANGEL LAZARO III
Title: Administrator

MANILA WATER COMPANY, INC.

By: _____

Title: _____

