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Excellency,

I have the honor to confirm the following understanding recently reached between the representatives of the Government of Japan and of the Government of the Republic of the Philippines concerning Japanese loans to be extended with a view to promoting the economic stabilization and development efforts of the Republic of the Philippines.

I

A loan in Japanese yen up to the amount of seventy-nine billion eight hundred and sixty-one million yen (Y 79,861,000,000) (hereinafter referred to as "the Loan I") will be extended, in accordance with the relevant laws and regulations of Japan, to the Government of the Republic of the Philippines (hereinafter referred to as "the Borrower I") by the Japan Bank for International Cooperation (hereinafter referred to as "the Bank") to implement the projects enumerated in the List A attached hereto (hereinafter referred to as "the List A") according to the allocation for each project as specified in the List A.

(1) The Loan I will be made available by loan agreements to be concluded between the Borrower I and the Bank. The terms and conditions of the Loan I as well as the procedures for its utilization will be governed by the said loan agreements which will contain, inter alia, the following principles:

(a)

(i) the repayment period will be twenty (20) years after the grace period often (10) years;

(ii) the rate of interest will be one and eight-tenths per cent (1.8%) per annum;

(b) notwithstanding sub-paragraph (a) above, where a part of the Loan I is made available to cover payments to environmental portions of the projects mentioned in 2, 4, 10 and 11 of the List A, then the rate of interest of the said part will be one and three-tenths per cent (1.3%) per annum;

(c) notwithstanding sub-paragraphs (a) and (b) above, where a part of the Loan I is made available to cover payments to consultants of the projects mentioned in 1 to 11 of the List A, then:

(i) the repayment period of the said part will be thirty (30) years after the grace period of ten (10) years;

(ii) the rate of interest of the said part will be seventy-five-hundredths per cent (0.75%) per annum; and

(d) the disbursement period will be six (6) years with regard to the projects mentioned in 7, 9, 10 and 11 of the List A, seven (7) years with regard to the projects mentioned in 2, 4, 5, 6 and 8 of the List A, eight (8) years with regard to the project mentioned in 3 of the List A, and nine (9) years with regard to the project mentioned in 1 of the List A from the dates of coming into force of the relevant loan agreements.

(2) Each of the loan agreements mentioned in sub-paragraph (1) above will be concluded after the Bank is satisfied of the feasibility, including environmental consideration, of the project to which such loan agreement relates.

(1) The Loan 1 will be made available to cover payments to be made by the Philippine executing agencies to suppliers, contractors and/or consultants of eligible source countries under such contracts as may be entered into between them for purchases of products and/or services required for the implementation of the projects enumerated in the List A, provided that such purchases are made in such eligible source countries for products produced in and/or services supplied from those countries.

(2) The scope of eligible source countries mentioned in sub-paragraph (1) above will be agreed upon between the authorities concerned of the two Governments.

(3) A part of the Loan I may be used to cover eligible local currency requirements for the implementation of the projects enumerated in the List A.

With regard to the shipping and marine insurance of the products purchased under the Loan I, the Government of the Republic of the Philippines will refrain from imposing any restrictions that may hinder fair and free competition among the shipping and marine insurance companies.

II

A loan in Japanese yen up to the amount of fifty-five billion eight hundred and seventy-nine million yen (Y 55,879,000,000) (hereinafter referred to as "the Loan II") will be extended, in accordance with the relevant laws and regulations of Japan, to the Development Bank of the Philippines (hereinafter referred to as "the Borrower II") by the Bank to implement the programs enumerated in the List B attached hereto (hereinafter referred to as "the List B") according to the allocation for each program as specified in the List B.

(1) The Loan II will be made available by loan agreements to be concluded between the Borrower II and the Bank. The terms and conditions of the Loan II as well as the procedures for its utilization will be governed by the said loan agreements which will contain, inter alia, the following principles:

(a)

(i) the repayment period will be thirty (30) years after the grace period often (10) years;

(ii) the rate of interest will be seventy-five-hundredths per cent (0.75%) per annum;

(b) the disbursement period will be six (6) years with regard to the programs mentioned in 1 and 2 of the List B from the dates of coming into force of the relevant loan agreements.

(2) Each of the loan agreements mentioned in sub-paragraph (1) above will be concluded after the Bank is satisfied of the feasibility, including environmental consideration, of the program to which such loan agreement relates.

(1) The Loan II for the program mentioned in 1 of the List B will be made available to cover credits to be extended by the Borrower II to sub-borrowers under the said program.

(2) The Loan II for the program mentioned in 2 of the List B will be made available to cover credits already extended and/or to be extended by the Borrower II to sub-borrowers under the said program.

(1) Notwithstanding the provisions of paragraph 3 above, a part of the Loan II will be made available to cover payments to be made by the Borrower II to consultants of eligible source countries under such contracts as may be entered into between them for purchases of services required for the implementation of the programs enumerated in the List B, provided that such purchases are made in such eligible source countries for services supplied from those countries.

(2) The scope of eligible source countries mentioned in sub-paragraph (1) above will be agreed upon between the authorities concerned of the two Governments. projects enumerated in the List A and the programs enumerated in the List B.

(2) The Government of the Republic of the Philippines will, by itself or through its executing agencies, assume:

(a) all fiscal levies and taxes imposed in the Republic of the Philippines on the Japanese companies operating as suppliers, contractors and/or consultants with respect to the income accruing from

the supply of the products and/or services required for the implementation of the projects enumerated in the List A and the programs enumerated in the List B; and

(b) all fiscal levies and taxes imposed in the Republic of the Philippines on the Japanese employees engaged in the implementation of the projects enumerated in the List A and programs enumerated in the List B with respect to their personal income derived from Japanese companies operating as suppliers, contractors and/or consultants.

(3) In connection with such tax assumption, the Government of the Republic of the Philippines or its executing agencies will be responsible for the liquidation or settlement of such fiscal levies, duties, taxes and other similar charges.

The Government of the Republic of the Philippines will take necessary measures to ensure that:

(a) the Loan I and the Loan II be used properly and exclusively for the projects enumerated in the List A and for the programs enumerated in the List B respectively; and

(b) the facilities constructed under the Loan 1 be maintained and used properly and effectively for the purposes prescribed in this understanding.

(1) The Government of the Republic of the Philippines will, upon request, furnish the Government of Japan and the Bank with reports on the progress of the implementation of the projects enumerated in the List A and the programs enumerated in the List B respectively.

(2) The two Governments will jointly review from time to time, on the basis of the reports mentioned in sub-paragraph (1) above, the progress of the

III

The repayment of principal of the Loan II, as well as the payment of interest thereon, shall be guaranteed by the Government of the Republic of the Philippines.

The respective disbursement periods mentioned in sub-paragraph (1) (d) of paragraph 2 of Part I and sub-paragraph (1) (b) of paragraph 2 of Part II may be extended with the consent of the authorities concerned of the two Governments.

The Government of the Republic of the Philippines will ensure that the products and/or the services mentioned in sub-paragraph (1) of paragraph 3 of Part I and sub-paragraph (1) of paragraph 4 of Part II are procured in accordance with the guidelines for procurement of the Bank, which set forth, inter alia, the procedures of international tendering to be followed except where such procedures are inapplicable or inappropriate.

Japanese nationals whose services may be required in the Republic of the Philippines in connection with the supply of the products and/or the services mentioned in sub-paragraph (1) of paragraph 3 of Part I and sub-paragraph (1) of paragraph 4 of Part I will be accorded such facilities as may be necessary for their entry into the Republic of the Philippines and stay therein for the performance of their work.

(1) The Government of the Republic of the Philippines will exempt:

(a) the Bank from all fiscal levies and taxes imposed in the Republic of the Philippines on and/or in connection with the Loan and the Loan as well as interest accruing therefrom; and

(b) Japanese companies operating as suppliers, contractors and/or consultants from all duties and related fiscal charges imposed in the Republic of the Philippines with, respect to the import and re-export of their own materials and equipment needed for the implementation of the implementation of the Loan I and the Loan II and take, if necessary, appropriate measures to secure their smooth and effective utilization. The Bank will be invited to participate in such review.

The two Governments will consult with each other with respect to any matter that may arise from or in connection with this understanding should be grateful if Your Excellency would confirm the foregoing understanding on behalf of the Government of the Republic of the Philippines.

I avail myself of this opportunity to renew to Your Excellency the assurance of my highest consideration.

His Excellency Domingo L. Siazon, Jr.

Secretary of Foreign Affairs

Department of Foreign Affairs

Republic of the Philippines

(Sgd.) YOSHIHISA ARA

Ambassador Extraordinary and Plenipotentiary
of Japan to the Republic of the Philippines

LIST A

(Maximum amount
in million yen)

1

Secondary Education Development and Improvement Project

7,210

2

Rural Water Supply Project (Phase V)

951

3

Bohol Irrigation Project (Phase II)

6,078

4

Agrarian Reform Infrastructure Support Project (Phase II)

16,990

5

Arterial Road Links Development Project (Phase IV)

15,384

6

Cordillera Road Improvement Project

5,852

7

Philippines-Japan Friendship Highway Mindanao Section Rehabilitation Project (Phase II)

7,434

8

Rehabilitation and Maintenance of Bridges Along Arterial Roads Project (Phase IV)

5,068

9

Maritime Safety Improvement Project (Phase C)

4,714

10

Pinatubo Hazard Urgent Mitigation Project (Phase II)

9,013

11

Pasig-Marikina River Channel Improvement Project (Phase I)

1,167

Total

79,861

LISTB

(Maximum amount in million yen)

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1.

Industrial and Support Services Expansion Program (Phase II)

35,350

2.

Environmental Infrastructure Support Credit Program (Phase II)

20,529

Total

55,879

Record of Discussions

In connection with the Exchange of Notes dated 27 December 1999, (hereinafter referred to as "the Exchange of Notes"), concerning Japanese loans to be extended with a view to promoting the economic stabilization and development efforts of the Republic of the Philippines (hereinafter referred to as "the Loans"), the representatives of the Japanese Delegation and of the Philippine Delegation wish to record the following:

With reference to sub-paragraph (3) of paragraph 3 of Part I of the Exchange of Notes concerning the financing of eligible local currency requirements for the implementation of the projects mentioned in the said sub-paragraph, the representative of the Japanese Delegation stated that:

(1) such requirement of local currency as general administrative expenses, interest during construction, taxes and duties, expenses concerning office, remuneration to employees of the executing agencies and housing, not directly related to the implementation of the said projects, as well as purchase of land properties, compensation and the like, however, will not be considered as eligible for financing under the Loan I; and

(2) the procurement of products and/or services will be made in accordance with the procedures of international competitive tendering except where such procedures are inapplicable or inappropriate.

With reference to sub-paragraph (1) of paragraph 3 of Part I and sub-paragraph (1) of paragraph 4 of Part II of the Exchange of Notes, the representative of the Japanese Delegation stated that the consultants of eligible source countries mean nationals of the eligible source countries or juridical persons controlled by the nationals of the mentioned countries.

The representative of the Japanese Delegation stated that the consulting services partly supplied by consultants of countries other than the eligible source countries will be eligible for financing under the Loans, if they meet the following the total man-months supplied by consultants of countries other than the eligible source countries will be less than fifty per cent (50%) of those required for the said consulting services.

With regard to the Loans, the representative of the Japanese Delegation stated that any financial requirements of the projects and programs not being covered with the proceeds of the Loans under the loan agreements mentioned in sub-paragraph (1) of paragraph 2 of Part I and sub-paragraph (1) of paragraph 2 of Part II of the Exchange of Notes, will be duly met by the Government of the Republic of the Philippines to assure the smooth implementation of the projects enumerated in the List A attached to the Exchange of Notes (hereinafter referred to as the "List A") and programs enumerated in the List B attached to the Exchange of Notes (hereinafter referred to as the "List B").

The representative of the Japanese Delegation stated that the Philippine side should give such due consideration to the due and prompt procedure of importation of the products required for the implementation of the projects enumerated in the List A and the programs enumerated in the List B under the Loans, as it has given in the course of the implementation of the projects and programs under the successive Japanese loans for projects and programs.

The representative of the Japanese Delegation stated that the Philippine side should give due consideration to the local residents support for the projects enumerated in the List A and to the environmental impact which the said projects have, in order to assure the smooth implementation of the said projects.

With regard to Part II of the Exchange of Notes concerning a loan to be extended for the implementation of the programs enumerated in the List B, the representative of the Japanese Delegation stated that the Philippine side ensures that the Development Bank of the Philippines will establish a revolving fund and furnish the Government of Japan and the Bank with information and data on the progress of the said revolving fund periodically, according to the loan agreements mentioned in sub-paragraph (1) of paragraph 2 of Part II of the Exchange of Notes.

With reference to sub-paragraph (2) of paragraph 5 of Part II of the Exchange of Notes, the representative of the Japanese Delegation, in view of the Revenue Memorandum Circular No. 42-99 dated June 2, 1999 issued by the Bureau of Internal Revenue, Department of Finance, the Republic of the Philippines, stated that:

(1) Japanese companies operating as suppliers, contractors and/or consultants will be subject to the Value-Added Tax (hereinafter referred to as the "VAT") imposed in the Republic of the Philippines on their purchases including importations of products and/or services required for the implementation of the projects enumerated in the List A and the programs enumerated in the List B;

(2) the Philippine executing agencies will be subject to the VAT imposed in the Republic of the Philippines on their purchases of products and/or services required for the implementation of the said projects and the said programs from the Japanese companies operating as suppliers, contractors and/or consultants;

(3) the Philippine executing agencies will not withhold any part of fiscal levies and taxes including the VAT when making payments for their purchases of products and/or services to the Japanese companies operating as suppliers, contractors and/or consultants;

(4) the Japanese companies operating as suppliers, contractors and/or consultants will pay to the Government of the Republic of the Philippines the difference between the VAT paid to them by the Philippine executing agencies as provided in (2) above and the VAT to be paid by them for their purchases including importations of products and/or services as provided in (1) above; and

(5) the Japanese companies operating as suppliers, contractors and/or consultants will not be required to withhold the personal income tax on Japanese employees engaged in the implementation of the said projects and the said programs.

With reference to sub-paragraph (1) of paragraph 3 of Part II of the Exchange of Notes, the representative of the Japanese Delegation stated that the Loan II for the program mentioned in 2 of the List B may be made available to cover credits already extended and/or to be extended between March 19, 1999 and the previous day of coming into force of the loan agreement mentioned in sub-paragraph (1) of paragraph 2 of Part II of the Exchange of Notes, as well as credits to be extended on and after the day of coming into force of the said loan agreement, to sub-borrowers referred to in the said sub-paragraph.

With regard to paragraph 6 of Part III of the Exchange of Notes, the representative of the Japanese Delegation stated that the necessary measures referred to in the said paragraph include measures preventing any other, gift or payment, consideration or benefit which would be construed as a corrupt practice in the Republic of the Philippines from being made as an inducement to or reward for the award of the contracts referred to in paragraph 3 of Part t and sub-paragraph (1) of paragraph 4 of Part II of the Exchange of Notes.

The representative of the Philippine Delegation stated that the Philippine side had no objection to all of the above mentioned statements.

Ambassador Extraordinary and

Plenipotentiary of Japan to the
Republic of the Philippines Secretary of Foreign Affairs
Department of Foreign Affairs
Republic of the Philippines

(Sgd.) YOSHIHISA ARA (Sgd.) DOMINGO L. SIAZON, JR.

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