Palawan New and Renewable Energy Livelihood Support Project

**DESIGN RISK SHARING FINANCE MECHANISM**

**PILOT IMPLEMENTATION REPORT (FINAL)**

Prepared for

**UNITED NATIONS DEVELOPMENT PROGRAMME**

Makati, Philippines

by

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<th>Abbreviation</th>
<th>Full Form</th>
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<tr>
<td>CBP</td>
<td>Cooperative Bank of Palawan</td>
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<td>CBRED</td>
<td>Capacity Building for the Removal of Barriers to Renewable Energy Development</td>
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<td>CFI</td>
<td>Community Financial Intermediary</td>
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<td>CMFI</td>
<td>Community Micro Finance Institution</td>
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<td>CRREE</td>
<td>Center for Renewable Resources and Energy Efficiency</td>
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<td>DBP</td>
<td>Development Bank of the Philippines</td>
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<td>FI</td>
<td>Financial Institution</td>
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<td>GEF</td>
<td>Global Environment Facility</td>
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<td>GoP</td>
<td>Government of the Philippines</td>
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<td>IIEC</td>
<td>International Institute for Energy Conservation</td>
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<td>LRF</td>
<td>Loss Reserve Fund</td>
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<td>MFI</td>
<td>Micro Finance Intermediary</td>
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<td>NRE</td>
<td>New and Renewable Energy</td>
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<td>PGP</td>
<td>Provincial Government of Palawan</td>
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<td>PNRELSP</td>
<td>Palawan New and Renewable Energy and Livelihood Support Project</td>
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<td>RE</td>
<td>Renewable Energy</td>
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<td>RSM</td>
<td>Risk Sharing Mechanism</td>
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<td>SHS</td>
<td>Solar Home Systems</td>
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<td>SSPC</td>
<td>Shell Solar Philippines Corporation</td>
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<td>UNDP</td>
<td>United Nations Development Programme</td>
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1 INTRODUCTION

Task 1 Design and Implementation. This report details the design and pilot implementation of a funding mechanism to support the financing of direct sales of photovoltaic solar energy home systems (SHSs) in rural/off-grid areas of Palawan. The International Institute for Energy Conservation (IIEC) in joint partnership with Mr. John MacLean of the Energy Efficiency Finance Corporation (EEFC) collectively referred to as the IIEC Team has prepared this report pursuant to, and to fulfill Task 1 defined in, the Consultancy Agreement between IIEC and UNDP/CRREE for the Palawan New and Renewable Energy and Livelihood Support Project ("PNRELSP" or the "Project"). Task 1 involved the design of a risk sharing mechanism (RSM) for financing direct sales of SHSs. The contract was subsequently amended to include the pilot implementation. The Project targeted the delivery of SHSs to off-grid communities in Palawan on a pilot basis, with intent to demonstrate delivery mechanisms that would be replicable province-wide. This Project was supported with funding from the Global Environment Facility (GEF) and implemented by the United Nations Development Programme (UNDP).

The Provincial Government of Palawan (PGP) was also a partner in UNDP/GEF’s renewable energy and livelihood program. The PGP was preparing to establish a new and renewable energy (NRE) Trust Fund (the "Fund") from a portion of its expected share of the national Government’s Malampaya gas royalties. Thus, an important context for Task 1 was to design a pilot finance mechanism that can be replicated in the future, province wide with funding from NRE Trust Fund.

Shell Solar Philippines Corporation ("Shell" or "SSPC") was the only main active vendor and installer of SHSs in Palawan when the design of the Risk Sharing Mechanism (RSM) was developed and piloted. SSPC was at that time the commercial hub and a primary entrepreneurial driver of the SHS market in Palawan. The Project enjoyed the cooperation of SSPC in developing the SHS finance program. The general concept of the RSM was presented to other SHS vendors of the Philippines when it was being developed but since SSPC was the only SHS vendor at that time interested in developing its market in Palawan, SSPC became the major participant in the pilot SHS finance program as the primary Vendor. In the future, it is expected that other SHS vendors will be recruited to and become active in Palawan and can also use similar financing mechanisms supported with the PGP NRE Fund.

Design Criteria for Concessional Support of the SHS Finance Program. The need for risk sharing and credit enhancement for the SHS finance program was driven by real and perceived high credit risk amongst rural households and the relative lack of lending experience in this sector. Concessional finance sources, motivated by economic development, poverty alleviation and environmental concerns and seeking to meet the energy services needs of rural communities in economically viable and environmentally sound ways, were justified in promoting...
the SHS market. Strategic criteria used for designing a concessional finance support (e.g., from UNDP/GEF or PGP NRE Fund) for the SHS finance program included the following:

- It should address market barriers and RE/SHS market conditions, and support financing that is matched to the economics of SHS projects and the customer's ability to pay;
- It should meet the lending and investment criteria of domestic financial intermediaries (FIs) so as to engage their capacities and resources; and meet the specific needs and business objectives of the other key parties, namely the RE/SHS project sponsors and equipment vendors and the customers both at the household and community levels, achieving a distribution of roles and risks that meets the objectives of all parties;
- It should achieve reasonable (maximum) leverage of the concessional monies; be easily administered and managed; and be replicable and scalable using PGP NRE Fund monies, and define the pathway for declining concessional support, i.e., the pathway for commercial sustainability, over time.

Thus, the design of the appropriate financing mechanism took into account and balanced all variables and the interests and objectives of all parties: the commercial costs of the SHS, the ability of the households to pay, opportunities for grants to buy down the costs at the margin, the ability of commercial RE/PV companies to supply and service the systems, interests and capacities of local FIs to provide the necessary financing and the various government agencies involved in promoting RE and rural electrification. The economics of the SHSs was considered from the perspectives of each party, including the end-user, the community, the RE/PV business, the FI and the government agencies representing social interests.

**Design Methodology.** The design of the SHS finance program was based on international and local research and two mission trips to Manila and Palawan conducted November, 2002 by Mr. John MacLean, the foreign finance expert. Prior to this mission, a Task 1 Options Paper was prepared; this paper recommended a vendor finance program that incorporates a pilot RSM. The Task 1 Options Paper was presented in two separate workshops, one for RE vendors and one for local FI’s in Palawan. As a result of the workshops, IIIEC team had the opportunity to review and refine the finance mechanism concept

**The Designed SHS Finance Program.** The main elements of the designed financing structure, are as follows.

- **SHS Loans** whereby a financial institution (FI) will provide loans either (A) directly to households for acquiring the SHSs, or (B) to a community micro-
finance intermediary (CFI), such as a local cooperative, which in turn would make loans to and collect loan payments from households.

- **Vendor finance program**, whereby the SHS vendor plays defined roles in marketing the finance program at the point of sale to the customer, and further supports the financing through commitments to remarket or repurchase any SHSs that are repossessed due to default, thus providing a means to realize the collateral value of the SHS, and provides certain limited recourse to the financing.

- **Loss reserve fund**, will be established and co-funded by the UNDP/GEF and the vendor, to provide additional cash security for the SHS lending program as a whole, sharing risk with the FI and CMFI.

- **Technical assistance** support and funding provided by UNDP/GEF for (i) FIs and CMFIs, helping cover their costs for managing the finance program, and, as applicable, for (ii) CMFIs, to assist them to set up systems to perform their financial intermediary functions, i.e., management and payment collections for sub-loans to households in their community.

**Pilot Implementation.** To advance and fulfill its core purpose -- implementing a pilot commercially-based SHS finance program -- the Project involved key players such as:

- SHS vendor (Vendor)
- Retail Bank (Bank)
- Escrow Agent
- CRREE, as organizer and facilitator of technical assistance
- Household customers.

The IIEC Team sought to establish partnership(s) with several Philippine/Palawan financial institutions (FIs) -- rural banks, wholesale banks, equipment leasing companies, commercial banks, micro-finance and community financial intermediaries (CMFI's). Several FIs including Development Bank of the Philippines, Land Bank, Landbank Leasing, Rural Bank of Narra, Cooperative Bank of Palawan, Philacor Credit Corporation and Coron Stevedoring Employees Corporation were identified as prospective partners.

Implementing the SHS finance program required developing and concluding agreements between the final key parties as outlined herein.

- Proposal to Banks, including a brief description of the program and the bank role.
The Project, with funding from UNDP-GEF, provided the financial requirements for piloting the risk sharing mechanism. The Project had a budget of $150,000 for the implementation of the RSM. This was used to finance the Loss Reserve Fund (LRF), the technical assistance to the FI/CMFI and the consultancy service of the IIEC team.

**The Loan Portfolio Generated.** After almost a year of pilot implementation a total of 788 loans have been generated for the purchase of 789 SHS units. This resulted to a total Original Loan Principal Portfolio size of P 13,964.696 with one reported loan default amounting to P 7,736.70 equivalent to 0.05 % of the original principal amount as of June 2005.

**Organization of this Report.** This report will proceed by first explaining the key elements of the recommended SHS finance program, the final players in the pilot program, implementation steps undertaken, final terms of the agreements and the resulting Loan Portfolio generated and its performance to date.

## 2 The Solar Home Finance Program

Solar home systems (SHSs) are small scale solar photovoltaic (PV) energy systems sized for off-grid household applications ranging from approximately 15-75 peak watts and from P 15,000- P40,000 ($300-800) in cost. The SHS typically includes the PV panel(s), battery, charge controller, two to three light points (using low wattage efficient fluorescent lamps and related wiring, switches and installation structures. For rural, poorer households, the SHS provides dependable quality energy services, replacing lower quality and less convenient kerosene, candles and battery charging, but the SHS high first cost is a barrier to its acquisition. The potential for cash sales is therefore limited. A financing mechanism is required so that households can overcome the first cost barrier and pay for SHSs over time. Because of lack of experience of financial institutions (FIs) with providing loans and other types of finance to rural and poorer households, an RSM is needed to motivate and support the commercial and/or development FIs to enter this market.

In Palawan alone there are an estimated 85,000 households without electricity services; in the Philippines, this estimate is five to six million. Thus, the SHS market consists of large numbers of small projects and transactions.
To deliver financing to this market successfully and cost-efficiently, and in a way that will be creditworthy, the designed RSM addressed three key challenges:

- Security for the lender, including the creditworthiness of the households, how to assess and manage household credit, the collateral value of the SHS and how to realize it in default situations; and,

- Transaction costs, including managing the process and costs of originating many small transactions, and administering effective billing & collections systems.

- Expanding Geographic Market Coverage, as many rural areas lack available financial services.

### 2.1 Recommended SHS Financing Program.

The diagram in the succeeding page shows the relationship of the different elements of the financing program and the roles of the key player.

Figure 1

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2.1.1 **Key Parties and their roles**

Key parties to this recommended program are: SHS vendor (Vendor); Lending Bank either wholesale or retail (Bank); Community Finance Intermediary (CMFI); Household buyers; and CRREE as organizer and provider of technical assistance.

Their respective roles are as follows:

**Wholesale Banks/Funders**
- Enter into a Master Loan Agreement with the CMFI
- Enter into a Vendor Financing Agreement with the Vendor
- Provide refinancing to CMFI to support lending activity provided CMFI passes the credit assessment guidelines

**SHS Vendor**
- Enter into a Vendor Finance Agreement with the Bank
- Market the SHS lending program to household borrowers
- Assist household borrowers in completing all loan documentation requirement
- Deliver and install the system
- Provide warranty to the unit and after sales service
- Buys the repossessed unit at an agreed collateral price
- Contribute to the loss sharing fund

**Community Finance Intermediary (CMFI)** such as cooperatives and other registered community organization performing collection functions will:
- Assist in organizing and educating the community about the SHS program
- Credit check and assess the household borrower
- Make the credit approval decision
- Collect payment
- Match loan payment to the wholesale banks with loan collections from household borrowers
• Assumes full recourse of the loan in case of default
• Assigns all its loan portfolio to the bank
• Assist the SHS vendor in repossessing the unit in case of default
• Enter into a Master Loan Agreement with the Bank

CRREE- The Center for Renewable Resources and Energy Efficiency will:

• Manage the provision of technical assistance
• Set up and monitor the LRF

2.1.2 SHS Financing Program

The main elements of the financing structure proposed are consistent with the finance program developed by SSPC. These are as follows: SHS Financing Program, Vendor Finance Program, Loss Reserve Fund and Technical Assistance

The SHS Financing Program, is designed to involve a financial institution (FI) that would provide loans either (A) directly to households for acquiring the SHSs, or (B) to a community micro-finance intermediary (CFI), such as a local cooperative, which in turn would make loans to and collect loan payments from households.

The SHS financing offer to household customers is based on market assessments of what households can afford and what is acceptable. Financing terms are established and tested as part of the pilot financing program. All finance terms are subject to review and negotiation based on market conditions and negotiations with the Vendor, the Bank and CMFI and may vary between Banks. Key terms include the following.

2.1.2.1 Finance term

Finance term must be matched with the customer ability to pay; longer terms mean lower payments; at the same time, a longer term means longer/higher risk profile and a shorter term means shorter/lower risk profile; a finance term of 3-4 years has been anticipated; five years is acceptable in some instances. SSPC reports that some customers actually prefer shorter terms in order to pay off the systems more quickly. SSPC emphasizes in their marketing that the energy comes free from the sun and after the SHS is paid for, the SHS provides energy services for only the costs of maintenance, primarily battery replacement every 3-4 years.
2.1.2.2 Interest rate

The interest rate is established based on the market rates available from the Bank. Because of the small transaction size, the interest rate must be high enough to allow the Bank and other financial intermediaries to earn a reasonable return and cover transaction costs. Market rates for small/micro loans are in the range from 23-30% +/- per annum effective rates at present; these loans are typically for short terms for micro-enterprise working capital. Monthly amortization is typically computed using the “add-on method”, a local micro finance way of calculating monthly amortization schedule using the following formula: \[ \frac{\text{Principal} + (\text{Principal} \times \text{interest} \times \text{loan term})}{\text{loan term} \times 12} \]. The add-on method generates a higher effective interest rate for the lender, e.g., a quoted rate of 16% using the add-on method translates to an effective annual interest rate greater than 23%; thus it is important when working with micro-lenders and rural banks to clarify their amortization and payment calculation methodologies. Perhaps in the future some lower interest rate wholesale funding can be found to lower the effective rate to small borrowers; in general, rates to small borrowers are higher to cover the transaction costs associated with this market.

2.1.2.3 Customer down payment

The down payment is sized so as not to represent a barrier to participation. The down payment improves the loan-to-value ratio for the SHS loan financing, gives the customer a strong stake of ownership in the system and serves as a proxy to reflect the household’s ability to pay. A lower down payment in the range of 10% is considered if the higher down payment proves a barrier.

The down payment could also be expressed as two to three months of monthly payments, i.e., a security deposit. For example, the down payment could represent two monthly payments plus an additional month’s security deposit is anticipated. These advance payment would be applied to the last monthly payments. In default events, the customer would forfeit the security deposit.

2.1.2.4 Payment schedule

A payment schedule of equal monthly payments of principal and interest in arrears, reflecting a "mortgage-style" amortization, is applied. This is the industry practice in the local microfinance.

2.1.2.5 SHS Lending Pathways

There are two pathways for Banks to make SHS loans: "Option A" is direct lending to households; Option B is lending through a CMFI.
**Direst Lending**

Some rural banks, e.g., Cooperative Bank of Palawan and Rural Bank of Nara, can lend directly to households and can offer Option A but their service areas are quite limited. Whole sale lenders like DBP and Landbank could provide a source of refinancing for the rural banks, and thus also play the role of wholesale lender.

For the households, Option B may be slightly more expensive because the CMFI will need to also charge an interest rate margin for their role.

**Lending Through CMFIs**

Direct bank lending to households is limited in Palawan to a few areas served by rural banks. Therefore, lending through CMFIs will be needed frequently to assure broad geographic coverage of the market. The primary type of CMFI is the cooperative. Palawan, as across the Philippines, has a substantial number of local cooperatives organized for local economic agriculture and general purposes. Many cooperatives already conduct lending activities for their members, typically for short-term agricultural loans.

**Cooperatives as CMFIs.** In Palawan, the PGP has an established Cooperative Development Office (CDO). Further, PGP has an existing loan guarantee program for cooperatives to support agricultural loans. The PGP CDO registers, qualifies and keeps records concerning management quality of cooperatives in Palawan and is therefore a good source of information to identify qualified cooperatives to serve as CMFIs in their communities.

**BAPAs as CMFIs.** Another type of CMFI could be the "BAPA" or Barangay Power Association. BAPAs are currently in place in several communities performing collections functions for local power services. BAPAs have been started by Paleco in 17 communities; these BAPAs frequently perform power bill collections services. Other roles BAPAs could possibly play include technical support & maintenance, for both SHS and other NRE systems. Paleco has an existing BAPA service and technical assistance program conducted by its Membership Services Dept. The political nature of the BAPA has been cited as a factor of concern for assuring that its operation is done in a non-partisan and completely business like fashion. This concern could likely be addressed in the BAPA governance structure, and have the BAPA be more of a community cooperative with a specifically prescribed charter rather than an arm of the Barangay government. BAPAs could represent a type of community RESCO that would assume roles as required as the energy infrastructure of a community develops.

**Traditional MFIs.** IIEC has researched other types of micro-finance intermediaries and determined that traditional MFIs, typically doing micro-finance for small scale productive enterprises on a peer lending model, are active in Palawan only in a very limited degree. Further, traditional MFIs typically restrict
their lending activities to micro-scale productive enterprises and trades and would consider a SHS to be household consumption equipment and probably ineligible for financing.

2.1.3 Vendor finance program

A vendor finance program is a programmatic relationship between the equipment marketer, or "Vendor", and the Bank designed to support the Vendor's equipment marketing and provide financing to the customer at the point of sale. Vendor finance programs are an established commercial finance technique that offer experience, methods and precedents that can be applied to SHS direct sales financing and address some of the challenges of financing SHS equipment, including managing transactions costs, aggregation of financing demand, enhancement of the credit or security structure, and extending credit to more customers. Vendor finance programs are an essential element of an appropriate finance mechanism for direct sales of SHSs. In general, the Vendor must be sufficiently strong and well-established to provide the defined services and financial recourse in a reliable and financially creditworthy way to result in credit enhancement for the FI.

2.1.3.1 Vendor Finance Agreements

This agreement defines the financing terms offered to the customer, (including rates, terms, documentation requirements), the procedures used to originate individual transactions under the program, and the terms of the relationship between Vendor and financier, that is, the terms and structure by which the financier will purchase the customer finance paper generated by the program. The goals of the program design are to create a creditworthy program, enhance the security structure to allow credit to be extended to more customers, manage transaction costs, and create a volume of business for the Bank.

Offer to Customers.

The SHS finance program offer to household customers is agreed on between the Vendor and the Bank. Finance documentation is agreed to between the Vendor and the Bank and is based on standard Bank requirements for equipment financing, simplified for the household market.

There is certainly a connection between (a) the customers' willingness-to-pay, and (b) continued successful functioning of the SHS. If the SHS is broken, the customer is much less likely to pay, even if the customer is legally obligated to pay and has accepted the maintenance and parts replacement obligations. Hence, the Vendor's offer of an extended warranty and after-sale service on this SHS is an important support to the financing program.
Transaction Management.

A main goal of a vendor finance program is to manage transaction costs for the Bank by having the Vendor involved in marketing and originating the financing at the point of sale. Where a CMFI is involved, the CMFI will be involved in these functions. Standard financing terms, conditions and documentation will be used. Bank costs for running an SHS finance program are reduced by having the Vendor assume some responsibilities associated with originating financing. By creating an exclusive relationship between a Vendor and the financial intermediary, a deal pipeline is created which benefits the Bank. Business volume targets may be set and Bank fees and pricing may be reduced as targets are achieved.

In general, the steps involved in originating a financing with the customer include the following:

a) Customer education: description of SHS technology, services and benefits; description of the SHS finance program, offer, financial requirements, pricing and documentation.

b) Customer finance application: A standard application form will be used, which will solicit from the customer the information necessary for the Bank and CMFI, as applicable, to make a credit decision. Information gathering and customer interviews must be conducted.

c) SHS Loan Agreement: when the customer is approved for the loan, then the loan documentation can be presented to the customer for execution.

d) SHS Installation: after the loan is executed, the SHS can be installed.

e) Loan disbursements: occurs after installation of the SHS. Disbursements are made directly to the Vendor for payment to the Vendor of the net sales price.

When a CMFI is involved, one question concerns the timing of the payment to the Vendor; the CMFI will be grouping SHS loans monthly for refinancing by the Bank: will the CMFI pay the Vendor on installation or can the Vendor wait to be paid until the CMFI refinances the SHS loan with the Bank? In this case, the Vendor could accept delayed payment as the Vendor is financially strong and the Project wants to make the program as easy as possible for newly recruited CMFIs to participate.

f) Invoicing instructions & collections: customers must know clearly where and when to pay. The collections/payment location must be convenient.

g) Post-installation technical service and checks. The Vendor will perform routine checks on the SHS, to answer customer questions and check on customer satisfaction, during the first several months post-installation.

Vendor Repurchase of SHS Equipment.

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In event of default by the end-user/customer, the Bank will have the right to repossess the SHS equipment. The Bank will want to liquidate, i.e., sell the equipment to convert it to cash. To be sure that it has a method to do so, the Bank will obtain an agreement with the Vendor whereby the Vendor will either (a) remarket the equipment, on a best efforts basis, for no or low sales fees, on behalf of the Bank, or (b) better yet, commits to repurchase the equipment based on some firm price schedule. This agreement relieves the Bank from the expense and risk of reselling the equipment and allows the Bank to rely on some minimum value for the repossessed asset.

Collateral Value of SHS.

SHSs tend to have relatively high collateral value. The systems are virtually 100% repossessable. The useful life of the PV panels is 15-20 years and the controller approximately 7 years. All components, including the solar panel, pole mount, control panel, battery, wiring (which is exposed on the interior of the home), and lighting fixtures/lamps. Some wiring may be lost or not reusable but this cost is minor. The time required to remove a system is less than one to two hours, given access to the household. Other fee-for-service SHS companies have reported never having a case where a system could not be repossessed. The cost of a repossession varies with the location/distance of the customer but is relatively low, given low labor costs, and about estimated to average approximately one-half the cost of installation. Because SHSs have high and reliable asset value, a repurchase commitment from the Vendor is reasonable.

Pricing of Repurchase Commitment.

In a repurchase commitment, the vendor commits itself to repossess and repurchase the SHS equipment in the event of a customer default on its SHS loan. The repurchase price amount is negotiated with the vendor as a percentage of the remaining principal outstanding on the SHS loan. These monies would be applied to buy down the loan loss. Given the high collateral value of the SHS equipment, particularly the PV panel and controller, this value may have the potential to be increased. At the same time, the Vendor will incur costs for repossessing and remarketing the SHS. The pricing of the repurchase is negotiated.

The Vendor will execute its equipment repossession activities through its local service technicians and, where applicable, in coordination with the CMFI; decision to repossess equipment is not made by the Vendor but by the Bank and/or CMFI. The Vendor acts as the agent of the Bank/CMFI in conducting repossessions.

2.1.4 Loss Reserve Fund

The Loss Reserve Fund (LRF) is co-funded by the UNDP/GEF and the vendor, to provide additional cash security for the SHS lending program as a whole, sharing risk with the FI and CMFI. A more detailed discussion of the LRF is presented in the Chapter 3 of this report.
2.1.5 Technical assistance

This is the support and funding provided by UNDP/GEF for (i) FIs, helping cover their costs for managing the finance program, and, as applicable, for (ii) CFIs, to assist them to set up systems to perform their financial intermediary functions, i.e., management and payment collections for sub-loans to households in their community. A more detailed presentation of the technical assistance provided to the FI that took part in the pilot implementation is presented in Chapter 7 of this report.

3 RISK SHARING MECHANISM DESIGN

The Loss Reserve Fund (LRF) was created to assist in addressing end-user credit risk concerns. Because of lack of experience with lending to rural households, perceived credit risk was high and the Bank would likely need third-party credit enhancements to mobilize and secure their financing. Even if a bank was willing to do some lending in this market, an LRF would allow that bank to be more aggressive in its credit underwriting policies and extend credit to more households.

3.1 Portfolio Approach to Credit Structuring.

The LRF was designed to take advantage of the portfolio approach to credit structuring. The SHS market and equipment financings consist of large numbers of small projects. While this creates challenges due to relatively high transaction costs, the large number of small transactions, when pooled together in a portfolio, can become a virtue from a credit analysis point of view: If a portfolio approach is taken to credit structuring, then no single default can cause the lender to fail to recover principal.

The designed RSM has the capacity to generate more than 2,500 SHS installations and financings. This number, and expanded numbers resulting from replication of the program, was large enough to make valid a portfolio or statistical approach to credit structuring

3.2 Loss Reserve Fund Mechanism.

The following outlines the method used to structure the RSM by using a portion of UNDP/GEF funds as a loss reserve fund (LRF).

a) A loss reserve fund (LRF) was created with UNDP/GEF monies. The IIEC team sought to establish multiple parties sharing in the loss distribution formula.

b) The LRF funds was to be drawn to cover a portion of principal losses the Bank would incur in the event of customer default on the SHS financings, net of monies
recovered through liquidation/resale of subject SHS collateral. In effect, the LRF was to serve as cash collateral for the Bank’s SHS financings.

c) The LRF monies was placed on deposit with an escrow agent subject to a Loss Reserve & Escrow Agreement between the UNDP, the Bank and the escrow agent.

The Escrow Agreement defined the uses and disbursement of the funds and the loss sharing formula.

d) The LRF would be disbursed to cover a portion of first loss, up to a planned loss percentage. The planned loss percentage was sized to be greater than a reasonable worst case estimate of the Bank’s defaults.

e) The "planned loss rate" proposed initially was 30%. Some rural banks report non-performing loan (NPL) rates as high as 20-25%; this high NPL rate would not necessarily translate into ultimate losses at this rate. A NPL rate of 30% seemed conservatively high. Planning for a loss rate this high did not mean we estimated losses would be this high; it simply was a conservative method for credit structuring for the pilot program and was designed to induce the lending Bank to participate.

Losses up to the planned loss rate would be shared; all losses above the planned loss rate would be borne entirely by the Bank, and, as applicable, the CMFI. Therefore, it was appropriate to start the program with a conservatively high planned loss rate.

f) All monies realized from the repurchase of repossessed SHS would be applied to loan principal first, so the LRF would share in the loan losses net of realized collateral value of the SHSs.

g) When an SHS loan covered by the LRF would be in default and the SHS system repossessed, then the appropriate share of the loss, based on principal loss only, not accrued interest, would be withdrawn from the LRF. The definition of loss would be tied to the definition of event of default, loan acceleration and repossession of the SHS as defined in the underlying SHS loan agreement with the household.

3.3 Loss Sharing Formula.

Losses would be shared between:

- UNDP/GEF funds, deposited in the LRF
- The Vendor
- The Bank, who also, as applicable, would share losses with the CMFI
The loss sharing formula has two tiers: first losses, defined as losses up to the planned loss rate, were distributed according to the formula indicated below; all losses above the planned loss rate would be borne entirely by the Bank, and, as applicable, the CMFI. Table 1 below illustrates the formula presented and negotiated with the Vendor and Bank.

Table 1: Loss Sharing Formula

<table>
<thead>
<tr>
<th>Party</th>
<th>Share of Losses up to Planned Loss %</th>
<th>First Loss Liability as % of original principal</th>
</tr>
</thead>
<tbody>
<tr>
<td>4 UNDP/GEF Funding</td>
<td>65.00%</td>
<td>9.7500%</td>
</tr>
<tr>
<td>5 Vendor</td>
<td>25.00%</td>
<td>3.7500%</td>
</tr>
<tr>
<td>6 Bank Share</td>
<td>10.00%</td>
<td>1.5000%</td>
</tr>
</tbody>
</table>

An explanation of each line item follows.

Line 1, is the planned loss rate.; 30% is used, as explained above. This value is conservatively high.

Line 2, represents the estimated realized collateral value from repossession and resale of the SHSs. As indicated above, the Vendor is expected to provide a firm repurchase commitment equal to 50% of the loss amount (outstanding principal) on all defaulted SHS loans. Therefore, this value can be relied on as firm.

Line 3, is the planned net loss, net of the realized collateral value of the SHSs. As with the planned loss rate, this value is expressed as a percentage of the original principal value of the SHS loans in the portfolio.

Lines 4-6 indicate the proposed loss sharing percentage on the first losses of the portfolio between UNDP/GEF, the Vendor and the Bank. This is a sharing
which to our judgment will be fair and acceptable after consulting the parties concerned. The share provides enough incentive for banks and CMFI’s to get good quality loans

The UNDP/GEF share would be paid from the LRF. The UNDP/GEF share would also be subject to a maximum dollar or peso liability amount, set equal to the budgeted UNDP/GEF monies allocated for the LRF at $100,000.

The Vendor share would be incorporated into their price; the Vendor contributions could be paid in cash and deposited in the LRF as each SHS loan closes, or, they could be a contingent liability of the Vendor, with the Vendor paying only when and as loan losses occur.

The Bank share would be incurred by the Bank and paid. It was important that this share be positive even for losses within the planned loss rate to give incentives for good administration. In this sharing, the Bank and CMFI would also have incentives to minimize loan losses as all losses more than the planned loss rate would be borne entirely by the Bank, and, as applicable, the CMFI. This would give the Bank and the CMFI incentives for good finance origination and especially good recovery and finance administration practices, and avoids the moral hazard associated with guarantees.

This structure was expected to work both for Option A, where the lending Bank lends directly to the household, and Option B, where the Bank lends to a CMFI.

The second column, indicating the first loss liability as a percentage of the original loan principal, is the value in line 3 (15%) multiplied by each party's share of the first losses. This coefficient can be used to calculate the maximum dollar/peso liability exposure on a given portfolio of SHS loans. For the Bank, this value of 1.5% is easily accommodated as part of normal loss provisioning. In fact, the Bank would require the CMFI to be fully responsible for this amount, and the CMFI could budget for this by reserving a portion of their earned margin. For the Vendor, this value of 3.75% can easily be incorporated into their SHS sales price and budgeted. Note that for the Vendor, 3.75% of the SHS loan principal translates into less than 2% of the gross SHS sales price given the downpayment and the subsidy being applied.

### 3.4 Maximum Loans That Can Be Supported.

With $100,000 available for the UNDP/GEF contribution to the LRF, then, using the proposed loss sharing formula, the UNDP /GEF funds was estimated to support a loan portfolio of an estimated 35 million pesos (over $1,000,000) representing an estimated 2,564 SHS loans. See the following Table 2 for the calculation.
Table 2: Guarantee Program Sizing

1. UNDP/GEF funds for LRF, maximum liability $100,000
2. UNDP/GEF funds, pesos PHP 5,000,000
3. First Loss Liability as % original principal 9.75%
4. Maximum portfolio that can be supported PHP 51,282,051
5. Average loan size PHP 20,000
6. Total number of loans 2,564

While the majority of first losses would be borne by the UNDP/GEF LRF contributions for this first portfolio, this structure was designed to be commercially sustainable over time. First, there are multiple contributors in the loss sharing formula, including the principle commercial parties. Second, the LRF structure could be expanded with PGP NRE Fund monies and other concessional funds. Third, as experience is gained, the planned loss rate should decline significantly, allowing a given amount of concessional funding to support a larger SHS loan portfolio. The relatively high share of first losses borne by the UNDP/GEF funds was justified as this is a pilot program.

UNDP’s target for the PNRELSP was to install 1,000 systems. It was recommended that the pilot SHS finance program be made available outside the original five target communities, even while finance programs were being developed for these target communities. This financial leverage would allow SHS transactions outside the target communities to be funded while preserving financial capacity to meet the potential demand within the target communities. The demonstration value of the pilot program would be achieved even if a substantial number of SHS financings occur outside the target communities.

3.5 Loss Reserve Fund Management, Fiduciary & Documentation.

The LRF would be placed on deposit with and managed by a Bank fiduciary. The LRF would be governed by an LRF Escrow Agreement between the parties. The fiduciary could be the primary Bank SHS lender, or another institution. An LRF Escrow Agreement was written to establish clear unambiguous rules for management, reinvestment and disbursement of LRF funds. Recordkeeping on the SHS finance portfolio and LRF fund balances and disbursements was established. UNDP/CRREE or some other technical party was to be involved in the agreement to assure accountability of GEF funds. When a portfolio of sufficient size was created, it could be closed. Excess LRF funds could then be
freed to be distributed to a LRF for the next portfolios as they were created. At the end of the program life, any remaining LRF balances would be distributed to their contributors in defined proportions and priorities. How the GEF funds are contributed. It is proposed that all CRREE/GEF funds intended for the LRF be deposited with the fiduciary bank under the governance of the Escrow Agreement at the start of the LRF program. The Escrow Agreement would have two accounts established within it: (i) a Deposit Account, and (ii) a Loss Reserve Account. The Deposit Account would receive the initial deposit of UNDP/GEF funds intended for the LRF. These monies belong to UNDP/GEF. Subsequently, as SHS loans are made, the amount of the agreed UNDP/GEF first loss share, e.g., 65% as proposed in Table 1, multiplied by the SHS loan principal, would be transferred into the Loss Reserve Account. Monies in the Loss Reserve Account would be available to pay loan losses; monies in the Deposit Account would belong to UNDP/GEF. It was proposed that all interest earnings on the Deposit Account would accrue to this account. But all interest earnings of the Loss Reserve Account would accrue to the bank to serve as an incentive for the bank to maintain good quality loan portfolio.

3.6 Summary Rationale for LRF Concept

Rationale for the LRF concept could be summarized as follows.

- The LRF creates significant cash collateral for securing Bank SHS lending;
- The LRF supports aggressive credit approval in the beginning of the program and therefore access to credit for SHS financing for poorer households;
- The LRF takes advantage of a portfolio approach to credit structuring;
- The LRF as a percentage of the SHS loan portfolio, could decline overtime as the SHS portfolio builds and as customer payment performance dictates;
- The LRF involves contributions from multiple sources, including the commercial parties, thereby defining a pathway for commercial viability and creating positive incentives;
- The LRF creates leverage for UNDP/GEF and concessional funds; creates a vehicle and pattern that can be scaled up and replicated with PGP NRE Fund monies.
4 THE FINAL PLAYERS IN THE PILOT PROGRAM

4.1 The Vendor Supplier

Shell Solar Philippines Corporation ("Shell" or "SSPC") was the only main active vendor and installer of SHSs in Palawan when the design was being developed and piloted. SSPC was at that time the commercial hub and a primary entrepreneurial driver of the SHS market in Palawan. The Project enjoyed the cooperation of SSPC in developing the SHS finance program. The developed design was presented to other SHS vendors of the Philippines but since SSPC was the only SHS vendor at that time interested in developing its market in Palawan, SSPC became the major participant in the pilot SHS finance program as the primary Vendor. In the future, it is expected that other SHS vendors will be recruited to and become active in Palawan and can also use similar financing mechanisms supported with the PGP NRE Fund..

SSPC was investing considerable resources to establish its SHS business in Palawan, and elsewhere in the Philippines, including setting up a network of distributors/sales agents, SHS service centers, a network of local technicians providing after-sales and warranty services, and supporting equipment financing programs.

SSPC had experimented with other PV retail business models and technology configurations, including community hybrid mini-grids on a fee-for-service basis. But the operating and maintenance expense aggravated by the theft and pilferage on the ‘fee for service’ hybrid solar system operation they started in Aklan, Philippines proved too high too make the project a viable business concern. In late 2001, SSPC concluded that direct equipment sales was the most immediate practical delivery method for SHSs for rural villages in terms of economics, market/household acceptance and manageable business opportunity for SSPC at that time. All of SSPC’s SHS marketing efforts then focused on the direct sales approach. SSPC estimated that up to 70% of all SHS sales would be financed. Thus, development of a SHS finance program was a business priority for SSPC when the Project was developing the RSM.

Shell Grants. SSPC has arranged grant funding from (i) Shell Philippines Exploration B.V. (SPEX), and (ii) the Dutch government to support direct sales of SHSs. SSPC had used the Dutch government monies as an equipment cost subsidy to reduce the cost of the SHS equipment to customers. In SSPC's experience, even with this subsidy, the systems remain unaffordable without some financing mechanism that allowed the customers to pay for the systems over time. The SPEX monies was used as part of SSPC's SHS finance program.
4.2 The Finance Institution

For the pilot implementation, the FI who finally assumed the role of providing financing to the end user was the Cooperative Bank of Palawan, (CBP) a rural cooperative bank with head office in Puerto Princess City and branches in Bataraza, Espanola and Aborlan. These branches are mostly on the southern part of the Puerto Princessa City.

During the development of the RSM, the SHS vendor (SSPC) had already initiated talks with CBP for a vendor finance agreement. Initial agreement covered only 160 units. The introduction of the Project deliverables proved timely. Although the negotiation took almost a year, the piloting of the RSM facilitated the finalization of the vendor finance agreement to finance 1,400 units. The recommended RSM addressed the credit risk concerns of the bank in financing SHS to a market sector that is generally in far flung unelectrified poverty stricken areas. With the vendor finance agreement, the RSM and the technical assistance program provided to CBP, the bank agreed to lend to households who want to purchase SHS systems. CBP also agreed to expand its lending operation to areas that were not originally within the existing geographical target market and operation of CBP. It should be noted that expanding a bank operation to unelectrified far flung poverty stricken areas was a major step as far as any FI was concerned. Among the concerns that had to be addressed were, the distance from existing branches, the expected volume of loans to be generated, and the number of qualified potential loan borrowers in the area. Technology reliability and after sales service was not a concern because CBP acknowledged the technical and financial capability of the SSPC. By that time SSPC had already put up a number of service centers in strategic areas in Palawan. In a different situation, technical and financial capability of the SHS vendor would an important concern of an FI entering into a vendor finance agreement with an SHS vendor.

One major concern though that had to be addressed was the working capital needed for lending. CBP at that time was providing commercial and agricultural loans, salary loans. CBP had a relatively newly introduced livelihood micro finance program that was experiencing collection problems. This had a significant effect on the liquidity and financial ratios of the bank. This occurred when the negotiation was already in the middle stage. So even if the first few loans released proved that lending to SHS promises a profitable lending business, CBP could not commit to increase its SHS loan portfolio.

4.3 The Whole sale Financier

With funding form World Bank, the Development Bank of the Philippines (DBP), had financial products that could be tapped for funds for on-lending by CBP or any other potential FI or CMFI who intends to finance household SHS purchases. For the purposes of the pilot implementation, CBP could not avail
loans from DBP since it could not pass the required financial ratios set by DBP. This failure to meet required financial ratios was due to the collection problems of CBP with the microfinance loan portfolio.

To address the liquidity problem of CBP, SSPC deposited about P 7.0 M in CBP at commercial rates

4.4 The Escrow Agent

DBP served as escrow agent for the pilot implementation. The treasury department of the DBP handled the fiduciary services for the Loss Reserve Fund. Initially only 35% of the UNDP GEF monies were earmarked for CBP, so only the equivalent $ 35,000 in Peso denomination was deposited in the Deposit Account. The balance of 65% was deposited as a Trust Account which was to be withdrawn and converted to Peso and deposited to the Deposit Account as the financing of SHS picks up. CBP was required to submit a regular monthly report addressed to UNDP and the DBP treasury. The report served as the basis for escrow agent to transfer funds from the Deposit Account to the Reserve Account equal to 15% of the original principal amount of the loan released by CBP. The report also served as the basis for the escrow agent to releases the funds from the LGF to CBP in case of default. Payment on the defaulted loans would be triggered by the submission by CBP of an SSPC certificate stating that SSPC had dismantled the SHS system and paid CBP as per buy back agreement.
5 IMPLEMENTATION STEPS UNDERTAKEN

To set up and to start the operation of the RSM the following activities were undertaken.

**Drafting of the Escrow Agreement** – The IIEC team drafted the Escrow Agreement in consultation with UNDP and its lawyer to draw up a legal document acceptable to UNDP. The final copy of the Escrow Agreement is attached as Annex 1 of this report.

**Identification of the Escrow Agent** –The IIEC team presented the mechanism of the risk sharing and the required escrow fund management to support the mechanism to the different commercial and development banks. The banks approached were Global Bank and Metro Bank- two large private commercial banks that later on merged to form one bank; Land Bank- a semi- government development bank and Development Bank of the Philippines- the largest government development bank. One of the criteria in choosing the bank to approach is that it should have many branches across the country to facilitate the transaction. Most of the banks were initially interested but after conducting their own internal deliberations on the merits of participating in the scheme, they later on declined, not because of the intricacies of the fund management required but because of the amount of monies involved which is only $ 100,000 equivalent to about P 5.4 M then. For banks, that amount was too small to be considered/classified as corporate account requiring corporate management and supervision. Finally after several meetings, the Development Bank of the Philippines, a government development bank, agreed to manage the escrow fund due to the developmental objective of the project and the possibility that they would also be able to manage the other future renewable energy project funds of UNDP particularly the Guarantee Fund to be established under the CBRED Project. Being a party to the pilot fund would give them the experience on the risk sharing mechanism and thus an edge over the other banks.

**Negotiation with the Escrow Agent** – The IIEC team coordinated the negotiation of the escrow fees. The proposal had to get the approval of the bank’s trust committee.

**Finalization of the Escrow Agreement** – IIEC coordinated the review of the terms and conditions of the Escrow Agreement by the lawyers of the three parties involved. The three parties represented were the escrow agent, the financial institution and UNDP. Any single revision by another party on any of the provisions in the terms and conditions required another cycle of review by the two other parties.

**Selecting and Developing an Appropriate CMFI**. The two most basic selection criteria used in identifying the CMFI’s were: (i) management capability, as represented by good ratings from relevant agencies, including the PGP CDO, and
(ii) interest in SHSs and willingness to serve the CMFI roles. Prior borrowing and on-lending experience is also very good indicator. Some lenders, including Landbank, are active; lending to coops, usually for working capital loans.

Through the assistance of CRREE, community organizations operating within the vicinity of the pilot project sites were identified and consulted.

Identified as potential end user financial intermediaries and consulted were:

- Coron Employees Multipurpose Cooperative
- Coron School of Fisheries Multi-purpose Cooperative
- Coron Stevedoring Arrastre Service Cooperative (COSASCO)
- Caramay Coffee Planter’s Multipurpose Cooperative

Philacor Credit Corporation, a credit company providing financing for home appliance purchases was also identified as a possible CMFI. Ultimately, selection of CMFIs was made by the lending wholesale lender, who must be convinced in the CMFIs ability to perform and repay the loans.

Those who showed very strong interest in participating in the pilot program were Coron Stevedoring Arrastre Service Cooperative (COSSACO) and Philacor Credit Corporation. But all three entities could not pass the requirement of the wholesale lender.

**Drafting of the Memorandum of Agreement** – This was originally a document to be called the Vendor Finance Agreement between the SHS vendor and the FI or the CMFI that will provide the financing. But since the decision of the FI or the CMFI to enter into the agreement was also due to the technical assistance to be provided by UNDP, a memorandum of agreement was drawn to be signed by the SHS vendor, the FI and UNDP. The technical assistance was critical since this would enhance the ability of the FI / CMFI to go into the business of SHS financing and ensure an effective and successful SHS financing program.

**Identification of the possible SHS wholesale lender.** To generate a substantial portfolio for the financing of SHS, the FI would need additional liquidity. IIEC coordinated the meetings with the wholesale lender who will provide the refinancing needs of the FI. Three possible wholesale lenders were approached:

- Land Bank (LB),
- Land Bank Leasing (LB Leasing)
- Development Bank of the Philippines (DBP)
The IIEC team found LB to be too rigid since at that time LB would only consider loan projects that have livelihood components.

While LB Leasing and DBP seriously evaluated the proposal to be a wholesale lender of the CMFI’s. IIEC saw the disadvantage that LB Leasing’s interest rates were high and that would translate to high interest rate for the rural end borrowers. The proposal was presented to the Board of Directors of LB Leasing, but the Board felt that this type of development financing should be handled by the mother company.

Negotiations with PEF were not pursued since further follow up did not reach any conclusive meetings with them. PEF was a large non-government organization with substantial funds for poverty alleviation. PEF was also giving out loan financing to community organizations in poverty stricken areas. PEF would have been a good partner in the scheme but the timing of the negotiations were not conducive to a serious talk since PEF was undergoing some management organizations and new appointment to critical positions. IIEC team deemed it would take a long time before a productive meeting could be set with PEF, the vendor and the FI and would not fit in the project timetable. Also it would still be best to deal with the commercial sector so as to facilitate the commercialization of the scheme.

With funding form World Bank, the Development Bank of the Philippines (DBP), had financial products that could be tapped for funds for on-lending by CBP or any other potential FI or CMFI who intends to finance household SHS purchases. For the purposes of the pilot implementation, CBP, a rural cooperative bank willing to lend directly to households could not avail loans from DBP since it could not pass the required financial ratios set by DBP. This failure to meet required financial ratios was due to the collection problems of CBP with the microfinance loan portfolio.

Eventually the negotiation with DBP progressed. But in the middle of the negotiation the CBP encountered collection problems in its existing livelihood loan portfolio. This resulted to the CBP not being able to meet the required financial past due ratios of the wholesale lender (DBP). Past due ratio is the ratio of the past due accounts to the total loan portfolio balance. The wholesale lender was interested in providing refinancing services to the FI/CMFI provided the FI improves its financial past due ratios. The SHS vendor then offered to solve the liquidity problem by placing cash deposits to the FI at a rate lower than the existing cost of money of the FI. This would enable the FI/CMFI to start its SHS loan portfolio. And since the SHS loans are expected to have a good collection rate, it will then have a positive impact to the FI’s past due ratios. Eventually during the course of the pilot implementation, the FI’s would improve its financial ratios to eventually qualify for the refinancing window of the wholesale lender. All through out this negotiation period with the vendor and the wholesale lender, IIEC was coordinating the meetings and exchange of terms and conditions.
Assistance during the MOA negotiation. Among the issues that had to be settled during the negotiation was the interest rate of the SHS vendor’s money to be deposited with the FI. This was not originally an issue not until there was a need to assist the FI with its liquidity problem. Another bone of contention during the MOA negotiation was the number of units to be committed for lending by the FI. The FI was hesitant to commit to more than 400 SHS units but the vendor’s position was that anything less than 1,200 units per year will not be a profitable business for the vendor. IIEC was well aware of the fact the due to the limited size of the fund for pilot implementation, it maybe prudent to concentrate program resources with one main lending FI. Considering that this is a portfolio approach to risks sharing, then a small loan portfolio might not give the project enough basis for evaluation if the transactions were fragmented. The only negative side to this was that the program would be limited to essentially one vendor during the first cycle. Again due to the limited project timeframe of 6 months, IIEC found it not practical to expect the other vendors to come in at this point within the project implementation timeframe unless the other vendors are already in operation in Palawan doing direct sales. Nevertheless the designed risk sharing mechanism does not preclude the other vendor’s participation in the future. At the end of the first portfolio cycle, UNDP could chose to use the remaining loss reserve fund for the next portfolios whether with another FI or with another vendor.

Signing of the MOA and Escrow Fund Agreement. Eventually both the MOA and Escrow Agreement were signed in September 2004.

Attached as Annex 1 and 2 are copies of the finalized Escrow Fund Agreement and the MOA.

Development and implementation of the technical assistance A technical assistance program was developed. This was an essential component in piloting the RSM. Assessment of the technical assistance requirement of CBP was conducted. From the result of the assessment a technical assistance plan was drawn.

This is discussed in detail in Chapter 7 of this report.
6 FINAL TERMS APPLIED TO THE AGREEMENTS

After almost a year of negotiation meetings with the final key player, the following were the final terms agreed upon.

6.1 Escrow Agreement

<table>
<thead>
<tr>
<th>Total Escrow Fund Size</th>
<th>Equivalent to $100,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Escrow Accounts to be established</td>
<td>Initially only $35,000 is earmarked for CBP. The balance of $65,000 will be deposited as Trust Account until such time that CBP agrees to a higher SHS units to be targeted.</td>
</tr>
<tr>
<td></td>
<td>A Peso Deposit Account is created using the $35,000 as initial deposit. Interest income realized accrues back to the Peso Deposit Account</td>
</tr>
<tr>
<td></td>
<td>A Peso Reserve Account is created depending on the number of SHS loans generated by CBP. An amount equal to 15% of the original principal loan amount is transferred from the Peso Deposit Account to the Peso Reserve Account.</td>
</tr>
<tr>
<td></td>
<td>Interest income realized accrues to the account of CBP. Doing so encourages the CBP to maintain good portfolio quality.</td>
</tr>
<tr>
<td></td>
<td>Interest rate for all Accounts will depend on prevailing market rates.</td>
</tr>
<tr>
<td>Escrow Management Fee</td>
<td>10% of interest earnings from Permitted Investments of Deposit Account and Reserve Account or P 5,000 per month plus VAT whichever is greater.</td>
</tr>
</tbody>
</table>

Details of the Escrow Agreement are attached as Annex 1

6.2 Memorandum of Agreement
### Targeted Number of SHS units
Initially CBP wanted to finance only 400 units but finally agreed to sign for 1,400 units

<table>
<thead>
<tr>
<th>Offer to customers</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Interest rate</td>
<td>Market rate</td>
</tr>
<tr>
<td>Loan Term</td>
<td>1-5 years</td>
</tr>
<tr>
<td>Down Payment</td>
<td>Minimum 10% of the SHS price net of subsidy from the Dutch government</td>
</tr>
<tr>
<td>Monthly Amortization Payment</td>
<td>Fixed amount based on “add-on” amortization computation. Principal ([1 + \text{Interest rate per year} \times \text{number of years}] / \text{Total number of months})</td>
</tr>
<tr>
<td>Documentation</td>
<td>Regular loan documentation requirement of the CBP will be followed</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Lending Pathway</th>
<th>Direct lending to end users</th>
</tr>
</thead>
<tbody>
<tr>
<td>Vendor SHS Pricing repurchase commitment</td>
<td>50% of the remaining balance of the outstanding balance of the loan in default</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Loss Sharing</th>
<th>Planned loss rate- 30%</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Estimated SHS Collateral value-50%</td>
</tr>
<tr>
<td></td>
<td>Net planned loss rate- 15%</td>
</tr>
<tr>
<td></td>
<td>1st loss liability -UNDP/GEF- 15%, Vendor-0%, Bank-0%</td>
</tr>
<tr>
<td></td>
<td>Vendor did not agree to share in the 1st loss liability. Their argument is that vendor is already sharing risk since vendor will deposit P 7.0 M in CBP at prevailing market rates to address CBP’s working capital requirement for this lending operation. Vendor will also pay salary of two credit investigators hired by CBP.</td>
</tr>
</tbody>
</table>

Details of the MOA are attached as Annex 2.

The final arrangement with the key players are summarized in Figure 2 below. The dashed lines indicate possible future arrangements.

September 2005
Figure 2

UNDP/GEF → Fund LRF → DBP Escrow Agent → Loss Reserve Fund → 1st Loss Liability

Vendor Finance Agreement → Buy Back P 7M Deposit → SHS loans & collections → Repay loans → Monthly Report

Vendor → SHS

Local SHS Technicians → SHS Maintenance → SHS

CBP Bank → SHS loans & collections

WHolesale Lender e.g., DBP

Technical Assistance to all parties, incl. program design & start-up

RSM Piloted

Households...
7 TECHNICAL ASSISTANCE PROGRAM

Providing technical assistance to the FI/CMFI was essential for an effective pilot implementation of the risk sharing mechanism. A successful implementation of the pilot program could facilitate an eventual commercialization of SHS financing by the finance sector.

7.1 Technical Support

UNDP/GEF earmarked $4,000 to provide technical support to the FI. It was agreed that the technical support will have two tranche. The first tranche of $2,000 would be provided upon MOA signing. The balance would be released after 700 SHS units had been financed.

Upon loan signing two motorcycles were provided by UNDP to the FI. At the start of the pilot RSM pilot implementation CBP had already generated about 160 SHS loan accounts. One of the difficulties encountered by the FI was the distance of the client / borrowers from the branches of the FI. And since credit investigation had to be conducted in the immediate vicinity/ location where the client/borrower resides, it was important that facilities be made available to facilitate the access to these rural areas. The most suitable motor vehicles for this type of operation are motorcycles, which could negotiate narrow rough roads common in the rural poor areas in Palawan. The motorcycles would also be used in collecting the amortization payments of the borrowers during the term of the loans.

The second tranche is earmarked to support the maintenance of SHS loan records and the preparation of monthly reports for submission to UNDP and the escrow agent.

7.2 Training Needs

The results of the training needs analysis and consultations with the FI revealed that the most relevant training for the CFI was on Remedial Management. The training should just cover 2 to 3 days, to minimize disruption of work on the bank’s operation.

Remedial Management involved the management of the risks and uncertainties associated with problem loan accounts, the recognition of early warning signals for potential problem accounts and the management of the problem accounts. A specific example would be the ways or the options in which the FI establishes an achievable repayment plan with client-borrowers having payment problems. Training on remedial management would help ensure that loan defaults will be managed well. Among the topics recommended for training were as follows:
• Determining causes and costs of delinquency
• Measuring and controlling arrears
• Measuring portfolio quality, effectiveness and profitability
• Formatting financial statements for decision making

7.3 Selection of Training Institutions

The training was delivered by an institution specialized in providing financial training. A list of potential training institutions considered were follows:

1. Association of Development Finance Institution in Asia and the Pacific (ADFIAP) - This is an institution focused on providing training to development banks. Lately ADFIAP is providing training to rural banks on macro issues such as good governance, environmental issues etc.

2. Rural Bankers Research and Development Foundation (RBRDF) - This is a foundation affiliated with the Rural Bankers Association of the Philippines (RBAP). The foundation provides training to the rural bank members of the association. CBP is a member of the association. The foundation has delivered Remedial management training courses in the past. The contact persons are

3. Punla Sa Tao Foundation (Punla) - This institution was launched in 1995 to provide training to micro finance institutions and entrepreneurial poor. It is focused on setting up grassroots banking services. Among the institutions or entities that Punla has provided training to, are NGO’s giving credit services, micro finance institutions, rural cooperatives and rural banks. Punla has already delivered remedial management training courses in the past.

4. Ahon Sa Hirap Inc. (ASHI) – was organized in 1989 to replicate the Grameen Lending Scheme, a rural based credit scheme providing loans with no collateral and no guarantee to very poor but very enterprising rural women. ASHI’s lending operation is mainly in the rural and semi-urban areas around Laguna de Bay in Luzon. ASHI started as a social research project of the University of the Philippines. It started giving micro finance loans to 50 mothers. Now ASHI has about 2,500 borrowers. When ASHI experienced serious default problems in 1992-1994, the organization undertook an extensive internal restructuring, re training and re education of its branch managers and staff. By 1995 ASHI repayment rate substantially improved and has since maintained an average repayment rate of 98%. ASHI continues to provide training on remedial management.

September 2005
Among the four entities presented, the Punla Sa Tao Foundation has experience in both training and micro finance. The financing of solar home systems is basically micro financing. It would therefore be best if the training were to be delivered by a trainer specialized in micro financing.

ADFIAP and RBRDF are also knowledgeable in remedial management training, but financing and loan management of development projects and rural bank loan accounts are different from that of micro financing. The latter involves dealing with small accounts and with clients who are not familiar with the banking transactions or do not have previous bank dealings. Most of the clients do not have current nor savings accounts with banks nor any formal bank support documents. This therefore requires a different loan management or loan collection strategy. It also requires a different lender – borrower approach when it comes to problem accounts. ASHI has the expertise in actual remedial management and would probably have a more in-depth experience on managing micro loan delinquencies and defaults compared to the ADFIAP, RBRDF and Punla. But ASHI has limited experience in training other entities. It is only now that ASHI has started negotiation for a training delivery with another micro finance entity.

Punla was eventually chosen to conduct the training.

7.4 The Training Workshop

Punla conducted a training to CBP in December 2004 on Portfolio Management. There was total of about 20 participants.

Participants consisted of branch managers, loan officers and credit investigators of SSPC. The details of the training topics and agenda are shown in Annex 3.
8 RESULTS OF THE FINANCING PROGRAM

As of June 2005, a total of 788 loans have been generated. One borrower bought two units so a total of 789 SHS units have been financed. Attached is a copy of the first monthly report submitted by CBP. This is ten (10) months after the finalization of the MOA between UNDP, SSPC and CBP in September 2004. It should be noted though that prior to the finalization of the MOA some 160 loans have already been generated.

The succeeding portfolio analysis is based on the June 2005 report of CBP to UNDP ten months after the Loss Reserve Fund was established.

8.1 Financing Terms Applied to Household Borrowers

The interest rates applied to borrowers were basically 16% and 24% per annum. The 16% rate was the original rate used. Eventually it was adjusted to market rates of 24% per annum. Approximately 8% of the loans generated carried an interest rate of 16% p.a. while 92% of the loans generated had a 24% interest rate.

Number of Loans Accounts According to Interest Rate Used

<table>
<thead>
<tr>
<th>Location</th>
<th>16%</th>
<th>24%</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>CBP-Head Office</td>
<td>5</td>
<td>227</td>
<td>232</td>
</tr>
<tr>
<td>CBP-Bataraza Branch</td>
<td>18</td>
<td>236</td>
<td>254</td>
</tr>
<tr>
<td>CBP-Espanola Branch</td>
<td>36</td>
<td>256</td>
<td>292</td>
</tr>
<tr>
<td>CBP-Aboran Branch</td>
<td>6</td>
<td>4</td>
<td>10</td>
</tr>
<tr>
<td>Total</td>
<td></td>
<td></td>
<td>788</td>
</tr>
<tr>
<td>Percent to Total</td>
<td>8%</td>
<td>92%</td>
<td>100%</td>
</tr>
</tbody>
</table>

Number of Loans Accounts According to Selling Price and Down Payment

September 2005
During the early stages of the negotiation of SSPC with CBP under a vendor finance program, the net selling price to the borrower was PhP 19,360 for a 50Wp unit. This was already net of the Dutch Government Subsidy. But by 2004 SSPC requested for a price increase by PhP 600 due to Peso depreciation. Subsequently by the time the MOA was finalized the net selling price of a 50Wp SHS unit was increased to PhP 19,960. To make the financing package more affordable the down payment required was lowered from 20% of the net selling price to 10%. However if there are borrowers who would opt for a higher down payment then this was allowed. As of June 2005 out of the total 788 loans 21% was based on the original price of which 76% opted for 10% down payment. While 79% of the 788 loans generated was based on the new price of which 98% opted for a 10% down payment. As expected, generally end borrowers prefer to give 10% down payment. The table below shows the details of this analysis.

<table>
<thead>
<tr>
<th>Selling Price</th>
<th>PhP 19,360</th>
<th>PhP 19,960</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>% Down Payment</td>
<td>20%</td>
<td>10%</td>
<td>30%</td>
</tr>
<tr>
<td>Original Principal Amount (Php)</td>
<td>15,488</td>
<td>17,424</td>
<td>13,972</td>
</tr>
<tr>
<td>Number of Loans</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>CBP-Head Office</td>
<td>2</td>
<td>13</td>
<td>-</td>
</tr>
<tr>
<td>CBP-Bataraza Branch</td>
<td>17</td>
<td>49</td>
<td>-</td>
</tr>
<tr>
<td>CBP-Espanola Brancj</td>
<td>20</td>
<td>62</td>
<td>2</td>
</tr>
<tr>
<td>CBP-Aborlan Branch</td>
<td>1</td>
<td>5</td>
<td>-</td>
</tr>
<tr>
<td>Total</td>
<td>40</td>
<td>129</td>
<td>2</td>
</tr>
<tr>
<td>Percent to Total</td>
<td>5%</td>
<td>16%</td>
<td>0%</td>
</tr>
</tbody>
</table>

**Number of Loans Accounts According to Loan Term**

Loans generated were had a term between 1 to 5 years depending on the negotiation between CBP and the loan borrower and the paying capability of the latter. Almost 95% of the loans had a term of 3 years or less, more than half of which opted for a two year term. Details of this are shown on the following table.
There were borrowers who opted for a 5 year loan term. Most of this type of borrowers came from Bataraza.

<table>
<thead>
<tr>
<th></th>
<th>1 Year</th>
<th>2 Years</th>
<th>3 Years</th>
<th>4 Years</th>
<th>5 Years</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>CBP-Head Office</td>
<td>71</td>
<td>112</td>
<td>47</td>
<td>1</td>
<td>1</td>
<td>232</td>
</tr>
<tr>
<td>CBP-Bataraza Branch</td>
<td>60</td>
<td>43</td>
<td>113</td>
<td>1</td>
<td>37</td>
<td>254</td>
</tr>
<tr>
<td>CBP-Espanola Branch</td>
<td>47</td>
<td>245</td>
<td></td>
<td></td>
<td></td>
<td>292</td>
</tr>
<tr>
<td>CBP-Aborlan Branch</td>
<td>4</td>
<td>6</td>
<td></td>
<td></td>
<td></td>
<td>10</td>
</tr>
<tr>
<td>Total</td>
<td>182</td>
<td>406</td>
<td>160</td>
<td>2</td>
<td>38</td>
<td>788</td>
</tr>
<tr>
<td>Percent to Total</td>
<td>23%</td>
<td>52%</td>
<td>20%</td>
<td>-</td>
<td>5%</td>
<td>100%</td>
</tr>
</tbody>
</table>

8.2 Loan Portfolio Profile and Preliminary Performance

Figures indicate that after the MOA was signed and the LRF was established in September 2004, the portfolio of CBP’s SHS Loans had increased substantially. This can be partly attributed to LRF which was created to assist in addressing end-user credit risk concerns. The LRF allowed the bank to be more aggressive in its credit underwriting policies and extend credit to more households.

Number of Loan Accounts Generated per Year

<table>
<thead>
<tr>
<th></th>
<th>Jan-Dec 2002</th>
<th>Jan-Dec 2003</th>
<th>Jan-Dec 2004</th>
<th>Jan–June 2005</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>CBP-Head Office</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>232</td>
</tr>
<tr>
<td>CBP-Bataraza Branch</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>254</td>
</tr>
<tr>
<td>CBP-Espanola Branch</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>292</td>
</tr>
<tr>
<td>CBP-Aborlan Branch</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>10</td>
</tr>
</tbody>
</table>
From a total of 788 loans, 73 accounts have fully paid while 14 accounts are past due. Of these accounts only 1 has been considered on default necessitating the pull out of the SHS system.

**Portfolio Performance in terms of number of accounts**

<table>
<thead>
<tr>
<th></th>
<th>Current</th>
<th>Past Due</th>
<th>Fully Paid</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>CBP-Head Office</td>
<td>217</td>
<td>3</td>
<td>12</td>
<td>232</td>
</tr>
<tr>
<td>CBP-Bataraza Branch</td>
<td>224</td>
<td>8</td>
<td>22</td>
<td>254</td>
</tr>
<tr>
<td>CBP-Espanola Branch</td>
<td>252</td>
<td>1</td>
<td>39</td>
<td>292</td>
</tr>
<tr>
<td>CBP-Aborlan Branch</td>
<td>8</td>
<td>2</td>
<td></td>
<td>10</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>701</td>
<td>14</td>
<td>73</td>
<td>788</td>
</tr>
<tr>
<td><strong>Percent to Total</strong></td>
<td>89 %</td>
<td>2 %</td>
<td>9 %</td>
<td>100%</td>
</tr>
</tbody>
</table>

**Portfolio Quality based on outstanding balance as of June 2005**

Based on outstanding balance, past due loans account for only about 1% of the total outstanding loan portfolio. This represents a very healthy portfolio compared to the planned loss rate of 30%.
The one account with its SHS systems pulled out had a loan outstanding balance of P 7,736.70 at the time of default. This is roughly 40% of its original loan principal amount of P 19,360 indicating that the loan was past halfway its amortization payment when it defaulted.

<table>
<thead>
<tr>
<th></th>
<th>Current</th>
<th>Past Due</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>CBP-Head Office</td>
<td>99 %</td>
<td>1 %</td>
<td>100%</td>
</tr>
<tr>
<td>CBP-Bataraza Branch</td>
<td>98 %</td>
<td>2 %</td>
<td>100%</td>
</tr>
<tr>
<td>CBP-Espanola Branch</td>
<td>99 %</td>
<td>1 %</td>
<td>100%</td>
</tr>
<tr>
<td>CBP-Aborlan Branch</td>
<td>83 %</td>
<td>17 %</td>
<td>100%</td>
</tr>
<tr>
<td>Total</td>
<td>99 %</td>
<td>1 %</td>
<td>100%</td>
</tr>
</tbody>
</table>

**Portfolio Generated from the previously identified pilot sites.**

Out of the total 788 loans generated 97 accounts or roughly 12.3% were generated from the Project’s previously identified pilot sites. The table below shows that most of the accounts generated from the Project pilot sites are recorded and managed in the head office of CBP except for Coron/Bulalacao which is managed at the Bataraza Branch of CBP.

<table>
<thead>
<tr>
<th></th>
<th>El Nido</th>
<th>Napsan</th>
<th>Coron/ Bulalacao</th>
<th>Caramay/ Roxas</th>
<th>New ibajay</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>CBP-Head Office</td>
<td>45</td>
<td>15</td>
<td>16</td>
<td></td>
<td></td>
<td>76</td>
</tr>
<tr>
<td>CBP-Bataraza Branch</td>
<td></td>
<td></td>
<td>21</td>
<td></td>
<td></td>
<td>21</td>
</tr>
<tr>
<td>Total</td>
<td>45</td>
<td>15</td>
<td>21</td>
<td>16</td>
<td>0</td>
<td>97</td>
</tr>
</tbody>
</table>
9 Lessons Learned

The key lessons learned in the pilot implementation are as follows:

Without a local facilitator, implementation of fund mechanisms in far flung areas will require longer time to establish. The CRREE project ended when the identification and negotiation with possible key players had just commenced. The absence of CRREE to facilitate the pilot testing hampered the negotiation with the local bank and local micro finance intermediaries. Most of the micro finance entities are based closed to their target market. So naturally, the MFI’s who could possibly on lend to the targeted areas are in far flung areas where communication facilities remain scarce and backward.

The pilot implementation determined the terms acceptable to the stakeholders in the RSM. For the banks, terms that are lower than market rates may be acceptable initially but eventually it becomes obvious that commercial level will not be achieved unless market rates are used. Interventions done to initially prop the requested terms cannot be sustained once the intervention is removed.

Pilot testing provided an SHS loan portfolio risk profile which could be utilized as a very important data to encourage private financing sector to support the direct sales of SHS. The pilot testing showed that SHS borrowers even in far flung areas can be good credit risks. It proved that SHS financing is viable business but it should be noted that a close and committed partnership with an SHS vendor cannot be underestimated.

With the results of the pilot implementation, the planned loss rate can be reduced further in future negotiations.
ANNEXES

1. Escrow Fund Agreement
2. Memorandum of Agreement
3. Portfolio Management Training Topics and Agenda
4. Summary of Loan Portfolio Generated as of June 2005
   10 months of Pilot Testing
Annex 1

Palawan New and Renewable Energy and Livelihood Support Project

Solar Home Systems Finance
Loss Reserve Fund Escrow Agreement

among

United Nations Development Program (UNDP)

Cooperative Bank of Palawan (CBP)

and

Development Bank of the Philippines (DBP)

2004
LOSS RESERVE FUND
ESCROW ACCOUNT AGREEMENT

This LOSS RESERVE FUND ESCROW ACCOUNT AGREEMENT (this "Agreement"), dated ______________2004 is undertaken into by:

United Nations Development Program (hereinafter UNDP) an international organization having its principal Philippines place of business at 7th Floor, NEDA sa Makati Building, 106 Amorsolo St. Legaspi Village, Makati City, Philippines;

Cooperative Bank of Palawan (hereinafter CBP) a rural banking company organized and existing under the laws of the Republic of Philippines, having its principal place of business at Fernandez St. Puerto Princesa City, Palawan, Philippines; and

Development Bank of the Philippines (hereinafter referred as Escrow Agent), a government financial institution duly organized and existing pursuant to the provisions of Executive Order No. 81 dated December 3, 1986, otherwise known as the 1986 Revised Charter of the Development Bank of the Philippines, as amended by Republic Act No. 8523 dated February 14, 1998, duly authorized to perform trust and other fiduciary business, having its principal place of business at Sen. Gil J. Puyat Avenue corner Makati Avenue, Makati City, Philippines.

WHEREAS:

(A) UNDP is acting as the Implementing Agency of the Global Environment Facility (GEF) to support a medium size project (PHI/99/G35 Palawan New and Renewable Energy Livelihood Support Project) aimed primarily at reducing the long-term growth of greenhouse gas (GHG) emissions through removing barriers to commercial utilization of renewable energy power systems to substitute for use of diesel generators in Palawan.

(B) Part of this UNDP-GEF project is a component for supporting the development and finance of renewable energy projects serving rural areas of Palawan, which has specifically targeted support for financing direct sales of solar home systems (SHSs);

(C) Cooperative Bank of Palawan can provide loan financing direct to individual customers (“Loans”) for SHSs and wishes to expand its SHS finance activity both geographically and in volume and wishes to obtain the financial support for its SHS financing activities available from UNDP and as provided herein;

(D) Escrow Agent can provide fiduciary services to manage the receipt, disbursement and investment of UNDP/GEF funds as provided herein;

NOW, THEREFORE, in consideration of the premises and the agreements set forth herein, the parties have agreed to enter into this Loss Reserve Fund Escrow Account Agreement and to establish a Deposit Account and a Reserve Account (such terms as defined below) with the Escrow Agent, to be funded and administered in accordance with the terms as provided herein.

ARTICLE I
Definitions

Section 1.01: Definitions. The following terms shall have meanings defined below when used herein.

"Deposit Account" has the meaning given in Section 2.01 hereof.

“Defaulted Loans” shall be those Loans which are (i) in default, and, having remained uncured, proceeded to loan acceleration, as defined in the Loan Agreement, (ii) for which the subject SHS or other energy equipment has been repossessed, and (iii) for which CBP has obtained the Realized Value pursuant to the Memorandum of Agreement entered into by CBP, Shell Solar

“Loans” shall be loans made by CBP for the purposes of financing SHSs or other energy services equipment approved by UNDP using a form Loan Agreement approved by UNDP; all Loans eligible for coverage under this Agreement must be closed and funded by CBP no later than June 30, 2006.

"Initial Deposit" means an initial deposit by UNDP of GEF funds in the amount of thirty-five thousand Dollars ($35,000.00) to be deposited into the Deposit Account.

“Memorandum of Agreement” means the Memorandum of Agreement between CBP, Shell Solar Philippines Corporation (SSPC) and UNDP dated _______, 2004, hereinafter “SSPC MOA”.

“Monthly Report” means the monthly reports on new Loans and Loan repayment and loss status as defined in Section 3.02, below; a form Monthly Report is attached hereto as Annex A.

“Net Loss Amount” shall equal (A) the outstanding principal balance on a Defaulted Loan plus, as applicable, accrued interest for no more than two months, minus (B) the Realized Value for the given subject SHS.

"Permitted Investments” shall mean, for both the Deposit Account and the Reserve Account, which are Peso-denominated current accounts of the Escrow Agent, any of the following investment opportunities: demand deposits, call account deposit (48 hours notice before draw downs), or 1, 3, 6, 9 or 12 month Philippine Government securities.

“Portfolio” refers to the portfolio of Loans scheduled to this Agreement via the Monthly Reports.

"Reserve Account" has the meaning given in Section 3.01 hereof.

"Subsequent Deposit" means any subsequent deposit by UNDP to be deposited into the Deposit Account.

“Realized Value” means the net amount realized by CBP from a repossessed SHS either by (i) resale of the SHS by SSPC, or (ii) purchase of the SHS by SSPC as per the terms of the SSPC MOA.

“Realized Value Date” means the date when the Realized Value is received by CBP.

ARTICLE II
Deposit Account

Section 2.01: Deposit Account. The Escrow Agent, on behalf of UNDP and at the request of and for the benefit of the CBP and UNDP, hereby establishes a segregated Peso-denominated special account, named the LRF DEPOSIT ACCOUNT, account number _________ (the "Deposit Account") to be funded and administered as provided in this Agreement. The escrow arrangement hereby established does not create a debtor-creditor relationship between the parties, and all monies, funds, or assets of the Deposit Account shall not be insured with the Philippine Deposit Insurance Corporation (PDIC). Losses, if any, shall be for the sole account and risk of the UNDP.

Section 2.02: Funding of the Deposit Account.

(a) On the date hereof UNDP has agreed to make an Initial Deposit into the Deposit Account in the amount of USD $35,000 (thirty-five thousand US Dollars), and the Escrow Agent shall acknowledge receipt of such funds upon deposit. Escrow Agent shall convert this deposit into Pesos upon receipt.

(b) UNDP may, at its option, make a Subsequent Deposit to the Deposit Account, provided that the Subsequent Deposit shall not be made after December 31, 2005.
Section 2.03: Interest on Deposit Account. Any interest earned on the Deposit Account shall accrue to the Deposit Account and may be used for the purposes defined herein, including payment of Escrow Agent fees, as per Section 7.02, below.

Section 2.04: Disbursements from Deposit Account. Disbursements from the Deposit Account will be made by Escrow Agent as follows:

(a) to the Reserve Account, as provided for in Section 3.02, below; and

(b) to UNDP, as provided for in Section 2.05, below.

(c) In no event, except as provided in subsections (a) and (b) immediately above, shall funds to be disbursed or withdrawn from the Deposit Account.

Section 2.05: Termination of Deposit Account. The Deposit Account shall terminate on July 31, 2006 at which time Escrow Agent shall notify UNDP of any remaining balance including interest and remit such balance to UNDP at such bank as UNDP may be instruct at that time.

ARTICLE III
Reserve Account

Section 3.01: Reserve Account. The Escrow Agent, on behalf of the CBP and at the request of and for the benefit of the CBP and UNDP, hereby establishes a segregated Peso-denominated special account, named the LRF RESERVE ACCOUNT, account number (the "Reserve Account") to be funded and administered as provided in this Agreement. The escrow arrangement hereby established does not create a debtor-creditor relationship between the parties, and all monies, funds or assets of the Reserve Account shall not be insured with the Philippine Deposit Insurance Corporation (PDIC). Losses, if any, shall be for the sole account and risk of the UNDP.

Section 3.02: Funding of Reserve Account. The Reserve Account will be funded by funds from the Deposit Account on a monthly basis according to the following procedure.

(a) CBP will provide UNDP and Escrow Agent the Monthly Reports by the fifteenth day of each month. The Monthly Report shall, amongst other information, list all new SHS Loans financed by CBP for the preceding month, give each Loan a unique identification number, and indicate the original principal amount of each Loan. A full form Monthly Report is attached hereto as Annex A.

(b) Within ten (10) calendar days (or next day if it were a banking holiday) of receipt by UNDP and the Escrow Agent of each Monthly Report, if UNDP does not communicate its disapproval of the Monthly Report, in whole or in part as to an individual Loans in the Portfolio, the Escrow Agent shall transfer funds from the Deposit Account to the Reserve Account in an amount equal to 15% (fifteen percent) of the principal amount of all new Loans added to the Portfolio indicated in the Monthly Report.

(c) Each Monthly Report and all Loan Agreements corresponding to Loans listed on the Monthly Reports will be scheduled to this Agreement.

Section 3.03: Interest on Reserve Account. Interest earned on the Reserve Account shall be disbursed to CBP. The amount to be disbursed shall be equal to the monthly interest earned net of the monthly Escrow Agent Fee referred to in Section 7.02 that cannot be sufficiently covered by the interest earnings of the Deposit Account referred to in Section 2.03. Disbursement to CBP of the interest earnings on the Reserve Account shall be done on a monthly basis.

Section 3.04: Use & Disbursement of Funds from the Reserve Account.

(a) CBP will utilize Reserve Account funds as additional security for it SHS Loans. Defaulted Loans, Realized Value for SHSs which are the subject of Defaulted Loans, and Net Loss Amounts for Defaulted Loans shall be reported in the Monthly Reports. For each Defaulted Loan, CBP shall include in the respective Monthly Reports a completed calculation of the
Realized Value and Net Loss, a form for which is included in Annex A. Certification by SSPC of the Realized Value calculation for each SHS which is subject of a Defaulted Loan shall be attached to each Monthly Report.

(b) Within ten (10) calendar (or next day if it were a banking holiday) of receipt by Escrow Agent of each Monthly Report, if UNDP does not communicate its disapproval of the Monthly Report, in whole or in part as to an individual Loans in the Portfolio, Escrow Agent will disburse to CBP from the Reserve Account funds equal to 100% (one hundred percent) of CBP’s Net Loss Amounts on the Defaulted Loans newly reported on the Monthly Report.

(c) All funds in the Reserve Account shall be available to CBP for the purposes defined herein. When and if the Reserve Account has zero balance (no funds), (i) CBP will have no further financial support pursuant to this Agreement, the Escrow Agent shall not be obligated to pay any Net Loss Amounts to CBP, UNDP shall not be obligated to pay any Net Loss Amounts to CBP, and all further Net Losses will be to CBP’s own account.

Section 3.05: Resolution of Monthly Reports. If, for the purposes of sections 3.02(b) and 3.04(b), above, UNDP should disapprove of a Monthly Report within the 10 day period following its receipt of a Monthly Report, then:

(a) UNDP shall immediately so notify CBP and Escrow Agent in writing;

(b) Escrow Agent shall temporarily suspend its actions with respect to that Monthly Report;

(c) UNDP shall immediately state to CBP its reasonable cause for such disapproval and request from CBP such additional information as needed to resolve the matter in question;

(d) CBP shall provide additional information as requested by UNDP to support and document its Monthly Report; and

(e) CBP and UNDP shall immediately use their best efforts to complete the mutually acceptable corrected Monthly Report.

(f) When the Monthly Report is accepted by UNDP, UNDP and CBP will forward the approved Monthly Report to Escrow Agent to take its actions as defined herein.

Section 3.06: Use of Monthly Reports. UNDP may use aggregated information, not specific individual loan information, contained in the Monthly Reports to report to its management and stakeholders on the success of this LRF and SHS loan program.

Section 3.07: Termination of Reserve Account. The Reserve Account shall terminate on the date when the CBP notifies the Escrow Agent that the last Loan in the Portfolio has matured; this date shall be no later than July 31, 2010. At such time the Escrow Agent shall notify UNDP of any remaining balance (including interest) and remit such balance to UNDP at such bank as UNDP may be instruct at that time.

ARTICLE IV
Assignment & Assurances

Section 4.01: Negative Pledge. Neither the CBP nor the Escrow Agent shall grant, assign, or otherwise create, or permit to exist, any assignment, lien, encumbrance, security interest, pledge, charge, privilege or priority of any kind in or to the Deposit Account or the Reserve Account or any of the funds at any time or from time to time deposited therein in favor of any person or entity other than UNDP.

Section 4.02: Assignment by CBP. Notwithstanding the foregoing in Section 4.01, CBP may assign its rights under this Agreement with the prior approval of UNDP. CBP assignment for the purposes of refinancing its SHS Loan portfolio is contemplated and UNDP will support and cooperate with this effort. In event of such assignment, UNDP will direct Escrow Agent to effect and document such assignment and Escrow Agent will do so as directed by UNDP.
Section 4.03: Further Assurances. At the request of UNDP, the Escrow Agent and the CBP shall cooperate in executing one or more financing or other supplemental statements, instruments or other documents in form reasonably satisfactory to UNDP in all public offices where filing is reasonably deemed by UNDP to be necessary or desirable. All cost of filing incurred in the Philippines shall be paid by the Escrow Agent and CBP while the cost of filing incurred outside Philippines shall be paid by UNDP. UNDP hereby grants to the Escrow Agent the right to do all acts and things which UNDP may reasonably deem necessary or desirable to maintain and operate the Deposit Account and the Reserve Account provided by this Agreement, including without limitation the filing of financing continuation or termination statements, any cost of which shall be funded from the earnings of the Deposit Account from Permitted Investments, and the UNDP hereby irrevocably appoints the Escrow Agent as its attorney-in-fact to do all acts and things to accomplish the foregoing as long as this Agreement is in effect.

Section 4.04: Escrow Agent Notice. Neither the Escrow Agent nor the CBP has actual knowledge of any other assignment, lien, encumbrance, pledge, security interest, charge, privilege or other priority of any kind related to the Deposit Account and the Reserve Account other than that created pursuant to this Agreement, and the Escrow Agent shall give UNDP prompt notice of any such interest other than that created pursuant to this Agreement of which a Responsible Officer of the Escrow Agent obtains actual knowledge after the date hereof. For the purpose of this Agreement, a "Responsible Officer" of the Escrow Agent means any officer of the Escrow Agent with responsibility for the administration of this Agreement, the Deposit Account or the Reserve Account.

ARTICLE V
Administration of Account

Section 5.01: Investment of Funds. The Escrow Agent shall invest and re-invest all funds in such Permitted Investments as the Escrow Agent shall, in its discretion, select. The exercise of the investment powers by the Escrow Agent under the terms of this Agreement does not guarantee a yield, return or income, as such performance of the investment of the Deposit Account and Reserve Account is not a guaranty of future performance and the income of the investment can fall as well as rise depending on prevailing market conditions.

Section 5.02: Earnings; Statements.

(a) All income or interest earned on the balance from time to time standing to the credit of the Deposit Account and/or the Reserve Account, as the case may be, including income or interest earned on Permitted Investments, shall be deposited in the Deposit Account and/or the Reserve Account, respectively, and added to the funds therein. Interest earnings on the Deposit Account and Reserve Account shall be available for payment of Escrow Agent Fees, as defined in Section 7.02, below.

(b) The Escrow Agent shall provide to UNDP on a monthly basis and from time to time upon request a statement with respect to the Deposit Account and the Reserve Account of (i) the balance of funds as of the beginning and the end of, (ii) all deposits, income and interest received and all withdrawals made, and all transactions in Permitted Investments and payment of Escrow Agent Fees during, and (iii) the Permitted Investments held as of the beginning and the end of, the month or period covered by such statement. Except in the case of manifest error, each such statement shall be deemed correct and final upon receipt thereof by UNDP unless the Escrow Agent is notified in writing to the contrary within thirty (30) days after the date of such statement.

ARTICLE VI
Representations, and Warranties and Covenants; Indemnification

Section 6.01: Representations of the Escrow Agent and CBP. The Companies individually and jointly represent and warrant to UNDP as follows:
(a) Each has the requisite corporate power to own its assets, conduct its business as presently conducted, and enter into, and perform its obligations under, this Agreement.

(b) Neither the making of this Agreement nor the compliance with its terms will conflict with or result in a breach of any of the terms, conditions or provisions of, or constitute a default or require any consent under, any indenture, lien, mortgage, pledge, charge, conditional assignment, hypothecation, security interest, title retention, preferential right, trust arrangement, privilege or priority of any kind, agreement or other instrument or arrangement to which either the Escrow Agent or the CBP is a party or by which it is bound, or violate any of the terms or provisions of either the Escrow Agent or the CBP’s charter or any judgment, decree or order or any statute, rule or regulation applicable to either CBP.

(c) This Agreement has been duly authorized and executed by each of the Escrow Agent and the CBP and constitutes the valid and legally binding obligation of each, enforceable against each in accordance with its terms.

(d) There is not any consent, authorization or approval of, or any registration or filing with, any government or governmental, administrative, fiscal, judicial or government-owned body, department, commission, tribunal, agency, entity or authority required under any law, regulation, order, decree or judgment applicable to each of the Escrow Agent and the CBP in connection with the making and performance of this Agreement.

(e) The Deposit Account and all funds from time to time deposited therein are and shall be lawfully owned by UNDP, free and clear of any assignment, pledge, lien, charge, encumbrance or security interest, other than those granted hereby to UNDP.

(f) The Reserve Account and all funds from time to time deposited therein are and shall be lawfully owned by UNDP, free and clear of any assignment, pledge, lien, charge, encumbrance or security interest, other than those granted hereby to UNDP and CBP.

Section 6.02: Indemnification. CBP shall indemnify, hold and save harmless, and defend, at their own expense, UNDP and the Escrow Agent, their officials, agents, and employees from and against all suits, claims, demands and liability of any nature or kind, including their costs and expenses, arising out of acts or omissions of CBP’s employees, officers, agents or sub-contractors, in the execution and implementation of this Escrow Agreement. This provision shall extend, inter alia, to claims and liability in the nature of workmen's compensation, products liability and liability arising out of the use of patented inventions or devices, copyrighted materials or other intellectual property by CBP and SSPC, its employees, officers, agents or sub-contractors. The obligations under this Article do not lapse upon termination of this Escrow Agreement.

Section 6.03: UNDP Immunity. Nothing in or relating to this Escrow Agreement shall be deemed a waiver, express or implied, of any privileges and immunities of UNDP, including its subsidiary organs.

Section 6.04. Covenants of UNDP and CBP. UNDP and CBP shall each submit to the Escrow Agent a certification under oath by its Corporate secretary or other equivalent officer attesting to the authority of the officer duly designated each by UNDP and CBP to issue instructions for purposes of this Agreement and setting forth their full names, their respective positions and specimen signatures. All orders, instructions, requests or certifications of such duly designated officers shall be in writing and the Escrow Agent may rely upon, and shall be fully protected and discharged from any responsibility, or accountability in acting in accordance with such orders, instructions, requests or certifications which UNDP and CBP hereby warrant to be valid, binding and duly authorized by its Board of directors.

ARTICLE VII

The Escrow Agent

Section 7.01: General.

(a) The Escrow Agent shall not deal with the Deposit Account, the Reserve Account and the funds in each respective account, except in accordance with (i) this Agreement, (ii) written instructions given in conformity with this Agreement, or (iii) instructions agreed to in
writing by UNDP. It is understood that this Agreement expressly sets forth all of the duties and obligations of the Escrow Agent with respect to the Deposit Account, the Reserve Account, and the funds in each respective account. In the event that any of the terms and provisions of any other agreement between or among any of the parties hereto conflict or are inconsistent with any of the terms and provisions hereof for purposes of determining the duties and obligations of the Escrow Agent under this Agreement, the terms and provisions of this Agreement shall govern and control in all respects.

(b) The Escrow Agent shall not have any liability with respect to any action taken by it arising out of or in connection with this Agreement except for its own gross negligence, fraud, or willful misconduct. Without limiting the generality of the foregoing, the Escrow Agent shall not be liable in connection with its investment or re-investment of any cash held by it hereunder in good faith, in accordance with the terms hereof, including without limitation any liability for any delay not resulting from its own gross negligence or willful misconduct in the investment or re-investment of the funds or any loss of interest incident to any such delays.

(c) The Escrow Agent may rely and shall be protected in relying upon any notice, instruction, instrument or other writing in good faith believed by it to be genuine and to be signed and presented by the proper party or parties. The Escrow Agent may act in reliance upon the advice of counsel with respect to any matter relating to this Agreement, and shall not incur any liability for any action taken or not taken in good faith in accordance with such advice.

(d) This Agreement is for the exclusive benefit of the parties hereto and their respective successors and permitted assigns hereunder, and shall not be deemed to give, either express or implied, any legal or equitable right, remedy, or claim to any other entity or person whatsoever.

(e) If at any time the Escrow Agent is served with any judicial or administrative order, judgment, decree, writ or other form of judicial or administrative process which in any way affects the Deposit Account, the Reserve Account or any of the funds in the accounts (including but not limited to order of attachment or garnishment or other forms of levies or injunctions or stays relating to the transfer of any of the funds), the Escrow Agent is authorized to comply therewith in any manner as it or its legal counsel deems appropriate, and if the Escrow Agent complies with any such judicial or administrative order, judgment, decree, writ or other form of judicial or administrative process, the Escrow Agent (except in the case of the Escrow Agent's gross negligence or willful misconduct) shall not be liable to any of the parties hereto or to any other person or entity even though such order, judgment, decree, writ or process may be subsequently modified or vacated or otherwise determined to have been without legal force or affect.

(f) In no event (except in the case of the Escrow Agent's gross negligence or willful misconduct or fraud) shall the Escrow Agent be liable (i) for any consequential, punitive or special damages, (ii) for the acts or omissions of its nominees, correspondents, designees, subagents or sub-custodians, or (iii) for an amount in excess of the value of the funds, valued as of the date of deposit.

(g) The Escrow Agent shall not incur any liability for not performing any act or fulfilling any duty, obligation or responsibility hereunder by reason of any occurrence beyond the control of the Escrow Agent (including but not limited to any act or provision of any present or future law or regulation or governmental authority, any act of God or war, or the unavailability of the Bangko Sentral wire or telex or other wire or communication facility).

(h) The Escrow Agent shall not be responsible in any respect for the form, execution, validity, value or genuineness of documents or securities deposited hereunder, or for any description therein, or for the identity, authority or rights of persons executing or delivering or purporting to execute or deliver any such document, security or endorsement.

(i) The Escrow Agent is authorized to comply with and rely upon any notices, instructions or other communications believed by it to have been sent or given by a person or persons authorized by any other party hereto. Whenever under the terms hereof the time for giving a notice or performing an act falls upon a Saturday, Sunday, or banking holiday, such time shall be extended to the next day on which the Escrow Agent is open for business.
Section 7.02: Escrow Agent Fees.

(a) Escrow Agent fees for its services provided hereunder shall be paid monthly and shall be the greater of (i) 10% of interest earnings from Permitted Investments of Deposit Account and Reserve Account monies, or (ii) P5,000 per month plus 10% VAT. Additionally, all out of pocket expenses shall be for the account of UNDP which is subject to prior approval of UNDP; such expenses shall also be payable from interest earnings on the Deposit Account. If the interest earnings on the Deposit Account are not sufficient to cover the amount due to the Escrow agent, then the balance will be funded by the interest earned on the Reserve Account.

Section 7.03: Replacement and Resignation. The Escrow Agent or any successor Escrow Agent hereunder may be replaced by UNDP at any time or may resign upon the giving or at least sixty (60) days’ prior written notice of resignation to the CBP and UNDP, and such resignation shall be effective from the date specified in such notice. If the office of Escrow Agent shall be vacant for any reason, UNDP may, upon consultation with the CBP, appoint a successor Escrow Agent hereunder by an instrument or instruments of appointment in writing delivered to such successor Escrow Agent, the retiring Escrow Agent, the CBP, together with (in the case of such successor Escrow Agent) a copy of this Agreement, and upon written acceptance by such Escrow Agent of such appointment such successor Escrow Agent shall succeed to all the rights and obligations of the retiring Escrow Agent as if this Agreement were originally executed by such successor Escrow Agent, and the retiring Escrow Agent shall duly transfer and deliver to such successor Escrow Agent the Funds in the form held by it hereunder at such time.

Section 7.04: Waiver of Set-off. The Escrow Agent shall not have, and hereby expressly waives, any right of bankers’ lien, setoff or counterclaim in respect of the Deposit Account, the Reserve Account, or any of the funds.

ARTICLE VIII
Miscellaneous

Section 8.01: Termination of Agreement.

(a) This Agreement shall terminate upon the payment in full by the Escrow Agent of all amounts that may be or become due and owing to the CBP and UNDP under Sections 2.05 and 3.06 and payment to Escrow Agent of all fees due under Section 7.02.

(b) In addition to the termination provisions provided in subsection (a) above, this Agreement shall terminate upon agreement of all of the parties hereto regardless of cause.

If the Parties are in breach of any provision of this Escrow Agreement, such breach shall be remedied within thirty (30) days of written notice by the concerned party. The initiation of arbitral proceedings in accordance with the herein prescribed procedure for Arbitration shall not be deemed a termination of this MOA/Escrow Agreement.

(c) Should CBP be adjudged bankrupt, or be liquidated or become insolvent, or should CBP make an assignment for the benefit of its creditors, or should a Receiver be appointed on account of the insolvency, UNDP may, without prejudice to any other right or remedy it may have, terminate this Escrow Agreement forthwith. CBP shall immediately inform UNDP of the occurrence of any of the above events.

(d) In the event of misrepresentation, or any other just cause for the termination of this Escrow Agreement, CBP shall be temporarily disqualified from future participation in UNDP contracting for a period of two (2) successive years for the first offense and perpetual disqualification for the second offense.

Section 8.02: Settlement of Disputes and Arbitration.

(a) The parties shall use their best efforts to settle amicably any dispute, controversy or claim arising out of, or relating to this Escrow Agreement or the breach, termination or invalidity thereof. Where the parties wish to seek such an amicable settlement through
conciliation, the conciliation shall take place in accordance with UN Commission on International Trade Law (UNCITRAL) Conciliation Rules then obtaining, or according to such other procedures as may be agreed between the parties.

(b) Unless any such dispute, controversy or claim between the parties arising out of or relating to this MOA/Escrow Agreement or the breach, termination or invalidity thereof is settle amicably under the preceding paragraph of this Article within sixty (60) days after receipt by one party of the other party's request for such amicable settlement, such dispute, controversy or claim shall be referred by either party to arbitration in accordance with the UNCITRAL Arbitration Rules then obtaining, including its provisions on applicable law. The arbitral tribunal shall have no authority to award punitive damages. The parties shall be bound by any arbitration award rendered as a result of such arbitration as the final adjudication of any such controversy, claim or dispute. Any arbitration award rendered as a result of such arbitration shall bind the parties as the final adjudication of any such controversy, claim or dispute.

(c) During the dispute or arbitration, the performance of the obligations of the Parties shall not be stopped or put on hold except for such work as may be the subject matter of the dispute or arbitration, or is directly affected thereby.

Section 8.03: Use of UNDP Name, Observance of UN Conventions and Other Laws

(a) CBP shall not advertise or otherwise make public in any manner whatsoever, use the name, emblem or official seal of the UNDP or UN, or any abbreviations of the name of UNDP or UN in connection with its business or otherwise.

(b) CBP represent and warrant that neither it, nor any of their suppliers, personnel, agents or sub-contractors is engaged in any practice inconsistent with the rights set forth in the Convention on the Rights of the Child, including Article 32 thereof, which, inter alia, requires that a child shall be protected from performing any work that is likely to be hazardous or to interfere with the child's education, or to be harmful to the child's health or physical, mental, spiritual, moral or social development. Any breach of this representation and warranty shall entitle UNDP to terminate this Escrow Agreement immediately upon notice to the Parties, without any liability for termination charges or any other liability of any kind to UNDP.

(c) CBP represent and warrant that neither their, nor any of their suppliers, personnel, agents or sub-contractors is actively and directly engaged in patent activities, development, assembly, production, trade or manufacture of mines, or in such activities in respect of components primarily utilized in the manufacture of mines. The term "mines" shall herein refer to those devices defined in Article 2, Paragraphs 1, 4 and 5 of Protocol II annexed to the Convention on Prohibitions and Restrictions on the Use of Certain Conventional Weapons Which May Be Deemed to be Excessively Injurious or to Have Indiscriminate Effects of 1980. Any breach of this representation and warranty shall entitle UNDP to terminate this Escrow Agreement immediately upon notice to the Parties, without any liability for termination charges or any other liability of any kind to UNDP.

(d) CBP shall comply with all laws, ordinances, rules and regulations bearing upon the performance of its obligations under the terms of this Escrow Agreement.

(e) Nothing in this Escrow Agreement shall constitute a partnership among the parties nor constitute one party the agent of the other party and vice versa. Except as set out in this Escrow Agreement, no party shall have express or implied authority to bind or represent any other party for any purpose whatsoever unless expressly agreed in writing by the party concerned.

(f) This Escrow Agreement may not be released, discharged, supplemented, interpreted, amended, varied or modified in any manner except in writing signed by a duly authorized officer or representative of each of the parties hereto.

(g) The Parties shall notify the other party of any material changes in the production process, nature and quality of supplies, mode of operation, delivery schedule, change of premises, change in the financial position as well as any litigation or proceedings involving the other party before any court or administrative agency which may adversely affect the ability of the other party to fulfill its contractual obligations to each other.
Section 8.04: Taxes

(a) The Parties recognize that Section 7 of the Convention on Privileges and Immunities of UNDP provides, inter-alia, that the UN, including its subsidiary organs, is exempt from all direct taxes, except charges for public utility services, and is exempt from customs duties and charges of similar nature in respect of articles imported or exported for its official use. In the event any Governmental authority refuses to recognize the UN exemptions from such taxes, duties or charges, the Parties shall immediately consult with UNDP to determine a mutually acceptable procedure to address any issues arising from or as a result of the non-recognition of the UN tax exemption privilege.

(b) CBP shall not be exempted from the payment of taxes, if any, which they shall incur in the process of undertaking their respective obligations under this Escrow Agreement, such as, but not limited to, taxes due to the Government on the gross income, among others.

Section 8.05: Notices. All notices, instructions and other communications hereunder shall be in writing and shall be given personally or sent by cable, telex, telecopy or by registered airmail, to the parties hereto at the following addresses or for any party at such other address as shall be specified by such party to each other party by like notice:

For CBP:
Manager
Cooperative Bank of Palawan
Fernandez St. Puerto Princesa
Palawan, Philippines
facsimile: +63 48 434 4492

For DBP (Escrow Agent):
Mr. Danilo L. Javilinar
Assistant Vice President
Trust Services Department
Development Bank of the Philippines
Sen. Gil J. Puyat Avenue corner Makati Avenue
Makati City, Philippines
facsimile: +632 893 0942

For UNDP:
339 Ms. Imee I. Manal
Programme Manager
UNDP-Environment Unit
106 Amorsolo St. Legaspi Village 1229
Makati City, Philippines
facsimile: +632 816 4061

All such notices and communications shall be deemed to have been given on the date of delivery if personally delivered, the date of sending if sent by cable (with proof of receipt from the cable office) or if telexed (with proper answerback received), or the date of receipt if telecopied or mailed.

Section 8.06: Successors and Assigns. This Agreement shall bind and inure to the benefit of the parties hereto and the respective successors and assigns, but shall not be assignable by the CBP or the Escrow Agent without the prior written consent of UNDP. Any purported assignment in violation of this Section shall be void.

Section 8.07: Entire Agreement; Waiver and Modification. This Agreement constitutes the entire agreement between the parties hereto with respect to the subject matter hereof and supersedes any and all prior agreements and undertakings, written or oral, with respect to the subject matter hereof. Any waiver, amendment or modification of the provisions hereof shall not be effective unless in writing and signed by all the parties hereto. Any waiver or consent shall be effective only in the specific instance and for the specific purpose for which given, and shall not
be construed to affect any other or future waiver or consent.

Section 8.08: **Headings**. Headings and Articles and Sections of this Agreement are for convenience of reference only, and shall not be used in the interpretation or construction of this Agreement.

Section 8.09: **Severability**. If any one or more of the provisions of this Agreement shall be found to be invalid, illegal or unenforceable in any respect or to any extent, such finding shall not affect the validity, legality or enforceability of such provisions in any other jurisdiction, and the validity, legality and enforce-ability of the remaining provisions hereof shall not in any way be affected, impaired or restricted thereby.

Section 8.10: **Counterparts**. This Agreement may be executed in any number of counterparts, each of which shall be deemed to be an original and all of which together shall be deemed to be a single agreement.

Section 8.11: **No Waiver; Remedies**. No failure on the part of UNDP or the Escrow Agent to exercise, and no delay in exercising, and no course of dealing with respect to, any right, power or privilege under this Agreement shall operate as a waiver thereof, nor shall any single or partial exercise of any right, power or remedy under this Agreement preclude any other or further exercise thereof or the exercise of any other right, power or remedy. The remedies provided herein are cumulative and not exclusive of any remedies provided by law.

Section 8.12. **Governing Laws**. Except as provided for Section 8.02 hereof, the terms and conditions, as well as the form and solemnities of this Agreement, shall be governed by and construed in accordance with the laws of the Republic of the Philippines.
IN WITNESS WHEREOF, the parties to this Agreement have caused this Agreement to be duly executed as of the date first written above.

COOPERATIVE BANK OF PALAWAN

By: Epifanio C. Magbanua
Title: Chairman of the Board

DEVELOPMENT BANK OF THE PHILIPPINES

By: Mr. Manuel S. Banayad
Title: First Vice President

UNITED NATIONS DEVELOPMENT PROGRAM

By: Ms. Deborah Landey
Title: Resident Representative

Signed in the Presence of:
ACKNOWLEDGMENT

Republic of the Philippines)
City of Makati ) S.S.

BEFORE ME, this _______ day of _____________, 2004, personally appeared:

<table>
<thead>
<tr>
<th>Name</th>
<th>Community Tax Cert. No.</th>
<th>Place/Date Issued</th>
</tr>
</thead>
<tbody>
<tr>
<td>Epifanio C. Magbanua</td>
<td>02657938</td>
<td>Manila/ 02-04-2004</td>
</tr>
<tr>
<td>Coop. Bank of Palawan</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Manuel S. Banayad</td>
<td>0036221</td>
<td>Makati/ 01-06-2004</td>
</tr>
<tr>
<td>Dev. Bank of the Phil.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Deborah Landey</td>
<td></td>
<td></td>
</tr>
<tr>
<td>UNDP</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

all known to me to be the same persons who executed the foregoing instrument and they acknowledged to me that the same is their free and voluntary act and deed as well as the free and voluntary act and deed of the entities they represent.

Said instrument refers to a loss Reserve Fund Escrow Agreement and consists of thirteen (13) pages, including this page where this acknowledgment is written, signed by the parties and the witnesses on each and every page hereof and sealed with my notarial seal.

NOTARY PUBLIC

Doc. No. ________ ;
Page No. ________ ;
Book No. ________ ;
Series of 2004.

Annexes
Annex A -- Monthly Report Form
Cooperative Bank of Palawan, Solar Home Systems Finance Program

**Annex A**

**MONTHLY REPORT to UNDP and Escrow Agent**
pursuant to Loss reserve Fund Escrow Agreement dated ____________, 2004

**Reporting Period:** 15-Jun-04 to 6/31/2004

**New Loans Added to Portfolio during Period**

<table>
<thead>
<tr>
<th>Loan #</th>
<th>Borrower</th>
<th>Location</th>
<th>Equipment Description</th>
<th>Equipment Net Sales Price</th>
<th>Customer Downpayment</th>
<th>Loan Principal</th>
<th>Loan Closing date</th>
<th>Loan Maturity date</th>
<th>Loan Interest Rate</th>
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<tr>
<td>1</td>
<td>00214</td>
<td>Reyes, Joel</td>
<td>El Nido</td>
<td>50Wp SHS</td>
<td>PHP 20,000</td>
<td>PHP 2,000</td>
<td>PHP 18,000</td>
<td>15-Mar-04</td>
<td>14-Mar-08</td>
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<tr>
<td>2</td>
<td>etc.</td>
<td>etc.</td>
<td>etc.</td>
<td>etc.</td>
<td>etc.</td>
<td>etc.</td>
<td>etc.</td>
<td>etc.</td>
<td>etc.</td>
</tr>
<tr>
<td>3</td>
<td>etc.</td>
<td>etc.</td>
<td>etc.</td>
<td>etc.</td>
<td>etc.</td>
<td>etc.</td>
<td>etc.</td>
<td>etc.</td>
<td>etc.</td>
</tr>
</tbody>
</table>

Total: PHP 18,000

**Funds to be Transferred from Deposit Account to Reserve Account for these new Loans as per Escrow Agreement Section 3.02(b)**

- 15.00% of PHP 2,700
- Funds Transferred from Deposit Account to Reserve Account, per all prior Monthly Reports: PHP 200,000
- Funds Transferred from Deposit Account to Reserve Account, with this Monthly Report: PHP 2,700
- Total Funds transferred from Deposit Account to Reserve Account, as of this Monthly Report: PHP 202,700

**Defaulted Loans During Period**

<table>
<thead>
<tr>
<th>Loan #</th>
<th>Borrower</th>
<th>Location</th>
<th>Outstanding Loan Principal</th>
<th>Accrued Interest*</th>
<th>Realized Value</th>
<th>Net Loss Amount</th>
<th>Calculation</th>
<th>Realized Value Date</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>00306</td>
<td>Lopez, Manual</td>
<td>El Nido</td>
<td>PHP 12,000</td>
<td>PHP 240</td>
<td>PHP 6,000</td>
<td>yes</td>
<td></td>
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<tr>
<td>2</td>
<td>etc.</td>
<td>etc.</td>
<td>etc.</td>
<td>etc.</td>
<td>etc.</td>
<td>etc.</td>
<td>etc.</td>
<td>etc.</td>
</tr>
<tr>
<td>3</td>
<td>etc.</td>
<td>etc.</td>
<td>etc.</td>
<td>etc.</td>
<td>etc.</td>
<td>etc.</td>
<td>etc.</td>
<td>etc.</td>
</tr>
</tbody>
</table>

Total: PHP 6,240

*not greater than two months accrued interest

**Funds to be Disbursed to CBP from Reserve Account for total Net Loss Amount**
per this Monthly Report, as per Escrow Agreement Section 3.02(b) 100.00%  PHP 6,240

Funds Disbursed to CBP from Reserve Account, per all prior Monthly Reports
Funds to be Disbursed to CBP from Reserve Account, with this Monthly Report  PHP 6,240
Total Funds Disbursed to CBP from Reserve Account, as of this Monthly Report  PHP 6,240

Portfolio Data

1. Total Loans in Portfolio, prior Monthly Report
2. Total # New Loans Added, this Monthly Report
3. Total # Loans as of this Monthly Report
4. Total Original Loan Principal, all Loans in Portfolio, with prior Monthly Report
5. Total Original Principal, all New Loans, this Monthly Report
6. Total Original Principal, all Loans in Portfolio, this Monthly Report
7. Total Outstanding Principal, all Loans in Portfolio, as of 6/31/2004
8. # Loans current
9. # Loans past due 30 days
10. # Loans past due 60 days
11. Total Outstanding Principal, all Loans in Portfolio past due 60 days
12. Total outstanding principal of Loans in default, but prior to Realized Value Date

Prepared By:

Approved By: Engr. Herudito A. Hista, Jr.
Manager
Cooperative Bank of Palawan
Annex 2

MEMORANDUM OF AGREEMENT

KNOW ALL MEN BY THESE PRESENTS:

This Memorandum of Agreement ("MOA") is entered into by and among:

UNITED NATIONS DEVELOPMENT PROGRAMME ("UNDP") an international organization having its principal Philippines place of business at 7th Floor, NEDA sa Makati Building, 106 Amorsolo St. Legaspi Village, Makati City, Philippines, represented by its Resident Representative Deborah Landey;

SHELL SOLAR PHILIPPINES CORP. ("SSPC"), a Philippine corporation with offices at 156 Valero Street, Makati City, Metro Manila, represented by its General Manager, Ramin Nadimi

- and -

COOPERATIVE BANK OF PALAWAN, INC. ("CBP"), a Philippine corporation duly licensed to operate as a rural bank with offices at Fernandez St., Puerto Princesa City, Palawan, represented by its Chairman, Epifanio C. Magbanua

WITNESSETH: That –

WHEREAS:

(A) UNDP is acting as implementing agency of the Global Environment Facility ("GEF") to support a medium size project (PHI/99/G35 Palawan New and Renewable Energy and Livelihood Support Project) aimed primarily at reducing the long-term growth of greenhouse gas (GHG) emissions by removing barriers to commercial utilization of renewable energy power systems to substitute for use of diesel generators in Palawan.

(B) Part of this UNDP-GEF project is support for the development and finance of renewable energy projects serving rural areas of Palawan, which has specifically targeted support for financing sales of solar home systems;

(C) SSPC is engaged in developing the rural market for solar photovoltaic systems which it markets and sells, through franchisees, to rural households under the brand name “Solarmax Solar Home Systems” ("SHS"), a sustainable and renewable energy technology suited for basic electrification of rural households;

(D) CBP can provide loan financing direct to individual customers for the purchase of SHSs, subject to availability of funds;

(E) The parties have agreed to establish a consumer finance system to assist Palawan rural households in acquiring SHSs.

NOW, THEREFORE, the parties have agreed as follows:

1.0. Purpose and Scope

1.1. This MOA sets forth the basic understanding of the parties on the establishment of a consumer finance system geared towards assisting Palawan rural households in acquiring SHSs. The parties acknowledge that in the course of implementing the
consumer finance system, other agreements (e.g., Loss Reserve Fund Escrow Agreement, Loan Agreement, Chattel Mortgage, Deed of Sale, etc.) will need to be executed. Moreover, the parties will be guided by an Operating Manual which shall be prepared by the parties, on such matters as loan approval, payment of proceeds of the loan to the franchisees, loan collections and procedures in case of default, including claims on the Loss Reserve Fund and the Buy-Back Guarantee.

1.2. The total number of SHS units to be covered by this MOA and which shall be financed by CBP through loans to the consumers is one thousand four hundred (1,400). CBP’s loss in case of default on up to thirty percent (30%) of the SHS loans and a maximum of four hundred twenty (420) loans, to be extended by CBP pursuant to this MOA shall be covered via (i) the Buy-Back Guarantee of SSPC under Clause 3.0 below, and (ii) the Loss Reserve Fund to be established by the UNDP pursuant to the Loss Reserve Fund Escrow Agreement and described in Clause 4.0 below.

2.0. Extension of SHS Loans by CBP to Prospective Customers

2.1. In the event that a prospective buyer of an SHS intends to finance such acquisition, SSPC, by itself or through its franchisee, shall inform CBP. CBP shall then undertake its usual credit investigation process to determine whether or not to extend a loan to the prospective SHS buyer.

A timeline schedule of actions for the processing and grant of SHS loans is attached as Annex “A”.

2.2. In the event that CBP decides to extend a loan to the prospective SHS buyer, it shall so inform SSPC and UNDP (through the Escrow Agent, identified in Clause 3.1 below). The terms of the loan shall be as follows:

| Loan Amount: | Maximum of ninety percent (90%) of the net selling price of the SHS |
| Purpose: | To acquire SHS |
| Drawdown Date: | Payment due date appearing on invoice of franchisee selling the SHS; loan proceeds to be released directly to franchisee for the account of the prospective SHS buyer |
| Term: | Maximum of three (3) years |
| Interest Rate: | Fixed at 24% p.a. (subject to adjustment as may be necessary) |
| Payments: | Interest payments and principal repayments every thirty (30) days commencing from Drawdown Date |
| Security: | Chattel Mortgage on the SHS to be purchased |
| Taxation: | All payments by the prospective SHS buyer to CBP, whether of principal, interest, fees, penalties or otherwise, shall be made without set-off or counterclaim, and fee and clear and without any deduction or withholding on account of any taxes. DST shall be for the account of the prospective SHS buyer |
| Representations, Warranties and Customary |
Covenants:

<table>
<thead>
<tr>
<th>Events of Default</th>
<th>Customary</th>
</tr>
</thead>
<tbody>
<tr>
<td>Remedies in Case of Default</td>
<td>In addition to legal and equitable remedies of a lender and mortgagee, CBP may repossess the SHS from the defaulting borrower. CBP may use the services of an agent or SSPC to effect the repossession.</td>
</tr>
</tbody>
</table>

| Fees and Expenses | For the account of the prospective SHS buyer. This includes registration fees for the chattel mortgage and insurance. |

As stated above, as additional security for the SHS loans to be granted by CBP, SSPC shall provide a Buy-Back Guarantee and UNDP shall establish a Loss Reserve Fund, to cover losses of CBP in case of default on the financing of up to thirty percent (30%) of the SHS loans and a maximum of 420 loans, made by CBP pursuant to this MOA.

CBP shall assign a unique identification number to all SHS loans (covering up to a maximum of 1,400 SHS units) which CBP wants covered with the Buy-Back Guarantee and the Loss Reserve Fund security under this MOA, and shall identify such loans in its Monthly Reports to UNDP and the Escrow Agent, as required under the Escrow Agreement. CBP shall also furnish SSPC with a copy of such Monthly Reports. To be eligible for coverage under this MOA, the SHS loan must be drawn no later than 31 July 2006. All SHS loans provided by CBP are covered by this MOA, including those systems already installed at the time of signing of this MOA.

3.0. Buy-Back Guarantee

3.1. SSPC commits to buy from CBP up to a price equivalent to fifty percent (50%) of the outstanding balance of the principal of the defaulted loan previously identified by CBP as covered by the guarantee. The Buy-Back Guarantee shall not cover earned income or any future income.

3.2. The maximum amount committed by SSPC for the Buy-back Guarantee is Three Million Seven Hundred Seventy One Thousand and Six Hundred Pesos (₱3,771,600) which is equivalent to 50% (SSPC’s share) of 90% (loan amount) of the selling price (₱19,960) of 420 SHS units.

3.3. Upon foreclosure by CBP of the chattel mortgage on the defaulted loan, and upon request and supervision of CBP, SSPC shall (a) direct its contractor to repossess the SHS, and (b) within six (6) months from receipt by SSPC of the written request from CBP, cause its franchisee who sold the relevant SHS to sell or dispose of the repossessed SHS on a best-efforts basis. The Selling Price shall be mutually agreed upon by CBP and the franchisee.

3.4. If upon expiration of the 6-month period the SHS remains unsold, then SSPC shall purchase the repossessed SHS from CBP at a price equivalent to fifty percent (50%) of the outstanding balance of the principal of the defaulted loan.

3.5. Costs of sale of the foreclosed and repossessed SHS, including but not limited to costs of de-installation, refurbishment and re-installation shall be for the account of CBP. Cost of storage shall be for the account of SSPC.

4.0. Loss Reserve Fund
4.1. UNDP shall establish a Loss Reserve Fund, consisting of (i) a Deposit Account and (ii) a Reserve Account, with the Development Bank of the Philippines (the "Escrow Agent") pursuant to an Escrow Agreement among UNDP, CBP and the Escrow Agent substantially in the form of Annex "B".

The principal amount of the Loss Reserve Fund shall be Three Million Seven Hundred Seventy One Thousand and Six Hundred Pesos (₱3,771,600). This is equivalent to 50% (UNDP’s share) of 90% (loan amount) of the selling price (₱19,960) of 1,400 SHS units. At its option, UNDP may make the deposit in equivalent foreign exchange. Investment of and disbursements from, the Loss Reserve Fund shall be governed by the Escrow Agreement.

4.2. In case of default on a loan previously identified by CBP as covered by the Loss Reserve Fund, and provided SSPC has paid its corresponding obligation under the Buy-Back Guarantee, CBP may formally request the Escrow Agent for immediate disbursement of the appropriate amount from the Loss Reserve Fund.

4.3. The Loss Reserve Fund shall only answer for (i) the outstanding principal amount of the defaulted loan, plus (ii) up to two (2) months accrued interest, minus (iii) CBP’s realized value for the SHS.

5.0. Other Conditions for the SSPC Buy-Back Guarantee and UNDP Loss Reserve Fund

The commitments of SSPC and UNDP under Clauses 3.0 and 4.0, respectively, are further subject to the following conditions:

5.1. The SHS buyer shall be required to purchase insurance policies, such as a life insurance policy on his life and a property insurance on the SHS, and to include CBP as additional insured. The Loss Reserve Fund and the Buy-Back Guarantee shall not cover insurance-covered incidents. Thus, in the event CBP recovers from, say, the life insurance policy on the life of the SHS buyer, or the property insurance on the SHS, then the amount recovered shall be deducted from the amount that CBP may draw from the Loss Reserve Fund and the buy-back price under the Buy-Back Guarantee.

5.2. CBP shall commit its resources to finance 1,400 SHS units. Thereafter, CBP shall continue lending to qualified SHS buyers even after the Loss Reserve Fund and Buy-Back Guarantee amounts have been fully committed, provided that:

   a. Collection rate does not fall below 80%; and
   b. Demand for solar credit facility exists.

5.3. Except for a chattel mortgage on the SHS, no other security shall be required by CBP from the borrower.

6.0. Intellectual Property Rights

6.1. Each of the parties acknowledges that the ownership of all rights, title and interest to the "Shell", "Solarmax Solar Home Systems", “SSPC” and other similar trademarks (collectively, "Intellectual Property") is and shall remain vested solely in SSPC and its affiliates and related entities, and the other parties disclaim any right or interest therein or the goodwill derived therefrom.

6.2. Each of the parties shall use the Intellectual Property in accordance with the requirements prescribed by SSPC.
6.3. Each of the parties will not directly or indirectly do or cause to be done any act or thing disputing, attacking or in any way impairing or tending to impair the validity of SSPC’s right, title or interest in the Intellectual Property. Any use by a party of the Intellectual Property shall inure to the benefit of SSPC.

6.4. It is understood and agreed that any license under this MOA for the use of the Intellectual Property is solely in connection with the consumer finance system established hereunder. Use of the Intellectual Property shall not create in favor of any party any right, title or interest on or to the Intellectual Property, but that all of such use shall inure to the benefit of SSPC. All goodwill associated with the Intellectual Property, including any goodwill which might be deemed to have arisen through any party’s activities, inures directly and exclusively to the benefit of SSPC.

7.0 Shell Business Principles

SSPC observes honesty, integrity and fairness in all aspects of its business and expects the same from CBP. Accordingly, CBP shall abide by the Statement of General Business Principles of the Shell Group of Companies (copy of which is attached as Annex “C”), to the extent that it applies to CBP.

8.0. Technical Assistance Funding

UNDP will provide direct cash support of Four Thousand US Dollars (US$4,000) to CBP for CBP’s new staffing costs, start up costs and other mobilization costs for administrative and geographic expansion of its SHS loan program. UNDP’s cash support will be released as follows:

- US$ 2,000 upon signing of the MOA and submission to UNDP of operating plan for the application of the US$2,000 cash support
- $ 2,000 after CBP completes the financing of the first 700 units of SHS and submission to UNDP of operating plan for the application of the US$2,000 cash support

Selected CBP personnel shall undergo training on developing solar market awareness and CBP shall proactively assist SSPC franchisees in offering SHS through a SHS loan.

9.0. Effectivity and Termination

9.1. This MOA shall become effective upon execution hereof. It shall terminate on the date when CBP notifies UNDP, the Escrow Agent and SSPC that the last SHS loan covered by this MOA has been repaid in full; this date shall be no later than 31 July 2010.

9.2. Upon termination of this MOA as stipulated in the immediately preceding paragraph, UNDP may withdraw any remaining funds in the Loss Reserve Fund, and the parties shall have no further rights and obligations to each other under this MOA.

10.0. Force Majeure

Neither party shall be liable to the other for any delay or non-performance of its obligations under this MOA arising from any cause or causes beyond its reasonable control including but not limited to acts of God, governmental act, war, fire, flood, explosion or civil unrest (“Force Majeure”) except that the party affected by the Force Majeure shall promptly notify in writing the other party of the cause constituting Force Majeure and the likely duration of the delay. In the event that the Force Majeure continues for at least three (3) months, this MOA may be terminated by either party.
11.0. Notices

All notices or other communication under this MOA or in connection herewith shall be given in writing and, unless otherwise stated, may be made by letter or facsimile. Any such notice or communication will be deemed given as follows: (a) if by letter, when delivered personally or on actual receipt, or (b) if by facsimile, when sent out (provided that the person sending the fax shall have received a transmission receipt).

However, a notice given in accordance with the above but received on a non-working day or after business hours will only be deemed to be given on the next working day in that place.

The address, telephone and facsimile number of the parties are as follows:

United Nations Development Program
106 Amorsolo St., Legaspi Village
Makati City
Tel. No.: 02 892 0611
Fax No.: 02 816 4061
Attention: Ms. Imee I. Manal
Programme Manager

Shell Solar Philippines Corp.
156 Valero St., Makati City
Tel. No.: 02 816 6069
Fax No.: 02 816 6226
Attention: Mr. R. Nadimi
General Manager

Cooperative Bank of Palawan, Inc.
Fernandez St., Puerto Princesa, Palawan
Tel. No.: 048 434 4493
Fax No.: 048 434 4492
Attention: Mr. E.C. Magbanua
Chairman

12.0. Non-exclusivity

The consumer financing system established under this MOA shall be on a non-exclusive basis. UNDP and SSPC shall be at liberty to enter into similar agreements with other financial institutions.

13.0. Confidentiality

Each of the parties shall keep confidential, and shall procure that its directors, officers, employees, agents and representatives keep confidential, any and all information of a confidential nature which it or they may acquire in relation to the other party and shall not
use or disclose such information except with the consent of the other party or in accordance with the order of a court of competent jurisdiction or governmental order.

14.0. Assignment

Neither party may assign any of its rights under this MOA without the prior written consent of the other parties. CBP assignment for the purposes of refinancing its SHS loan portfolio is contemplated and UNDP and SSPC will support and cooperate with this effort.

15.0. Amendments

This MOA may be amended only by written consent of all parties.

16.0 Waiver

Any waiver by a party or failure by a party to assert a breach of any provision of this MOA shall not be considered a permanent waiver of such provision or of other provisions by the non-breaching parties.

17.0 Required UNDP Provisions

17.1. Taxes. CBP and SSPC shall not be exempted from the payment of taxes, if any, they shall incur in the process of undertaking their respective obligations under this MOA, such as, but not limited to, taxes due to the government on their respective gross income, among others.

17.2. UNDP Tax Exemption. The parties recognize that Section 7 of the Convention on Privileges and Immunities of UNDP provides, inter-alia, that the UN, including its subsidiary organs, is exempt from all direct taxes, except charges for public utility services, and is exempt from customs duties and charges of similar nature in respect of articles imported or exported for its official use. In the event any governmental authority refuses to recognize the UN exemption from such taxes, duties or charges, the parties shall immediately consult with one another to determine a mutually acceptable procedure to address any issues arising from or as a result of the non-recognition of the UN tax exemption privilege.

17.3. Indemnification. Each of CBP and SSPC shall indemnify, hold and save harmless, and defend, at its own expense, UNDP, its officials, agents, and employees from and against all suits, claims, demands and liability of any nature or kind, including their costs and expenses, arising out of acts or omissions of CBP's or SSPC's respective employees, officers, agents or sub-contractors, in the execution and implementation of this MOA. This provision shall extend, inter alia, to claims and liability in the nature of workmen's compensation, products liability and liability arising out of the use of patented inventions or devices, copyrighted materials or other intellectual property by CBP or SSPC, its employees, officers, agents or sub-contractors. The obligations under this Clause 17.3 do not lapse upon termination of this MOA.

17.4. UNDP Immunity. Nothing in, or relating to this MOA shall be deemed a waiver, express or implied, of any privileges and immunities of UNDP, including its subsidiary organs.

17.5. Use of UNDP Name, Emblem or Official Seal. CBP and SSPC shall not use, advertise or otherwise make public in any manner whatsoever, the name, emblem or official seal of the UNDP or UN, or any abbreviations of the name of UNDP or UN in connection with their respective businesses or otherwise.
17.6. **Child Labor.** Each of CBP and SSPC respectively represents and warrants that neither it, nor any of its suppliers, personnel, agents or sub-contractors is engaged in any practice inconsistent with the rights set forth in the Convention on the Rights of the Child, including Article 32 thereof, which, inter alia, requires that a child shall be protected from performing any work that is likely to be hazardous or to interfere with the child's education, or to be harmful to the child's health or physical, mental, spiritual, moral or social development. Any breach of this representation and warranty shall entitle UNDP to terminate this MOA immediately upon notice to the other parties, without any liability for termination charges or any other liability of any kind to UNDP.

17.7. **Mines.** Each of CBP and SSPC respectively represents and warrants that neither it, nor any of its suppliers, personnel, agents or sub-contractors is actively and directly engaged in patent activities, development, assembly, production, trade or manufacture of mines, or in such activities in respect of components primarily utilized in the manufacture of mines. The term "mines" shall herein refer to those devices defined in Article 2, Paragraphs 1, 4 and 5 of Protocol II annexed to the Convention on Prohibitions and Restrictions on the Use of Certain Conventional Weapons Which May Be Deemed to be Excessively Injurious or to Have Indiscriminate Effects of 1980. Any breach of this representation and warranty shall entitle UNDP to terminate this MOA immediately upon notice to the other parties, without any liability for termination charges or any other liability of any kind to UNDP.

17.8. **Observance of the Law.** Each of CBP and SSPC shall comply with all laws, ordinances, rules and regulations bearing upon the performance of its obligations under the terms of this MOA.

17.9. **Parties not Partners.** Nothing in this MOA shall constitute a partnership among the parties nor constitute one party the agent of the other party and vice versa. Except as set out in this MOA, no party shall have express or implied authority to bind or represent any other party for any purpose whatsoever unless expressly agreed in writing by the party concerned.

17.10. **Material Changes.** A party shall notify the other parties of any material changes in the production process, nature and quality of supplies, mode of operation, delivery schedule, change of premises, change in the financial position as well as any litigation or proceedings involving that party before any court or administrative agency which may materially and adversely affect its ability to fulfill its contractual obligations under this MOA.

17.11. **Right to Termination.** In addition to the termination provisions in Clause 9.0, this MOA shall terminate upon agreement of all of the parties hereto regardless of cause.

If a party is in breach of any provision of this MOA, such breach shall be remedied within thirty (30) days of written notice by either of the other parties. The initiation of arbitral proceedings in accordance with the herein prescribed procedure for arbitration shall not be deemed a termination of this MOA.

17.12. **Termination Due to Bankruptcy or Insolvency.** Should CBP or SSPC be adjudged bankrupt, or be liquidated or become insolvent, or make an assignment for the benefit of its creditors, or should a receiver be appointed on account of the insolvency, UNDP may, without prejudice to any other right or remedy it may have, terminate this MOA forthwith. CBP and SSPC shall immediately inform UNDP of the occurrence of any of the above events.
17.13. **Temporary or Perpetual Disqualification.** In the event of material misrepresentation, or any other breach justifying termination of this MOA, the breaching party shall be temporarily disqualified from future participation in UNDP contracting for a period of two (2) successive years for the first offense and perpetual disqualification for the second offense.

17.14. **Amicable Settlement.** The parties shall use their best efforts to settle amicably any dispute, controversy or claim arising out of, or relating to this MOA or the breach, termination or invalidity thereof. Where the parties wish to seek such an amicable settlement through conciliation, the conciliation shall take place in accordance with UN Commission on International Trade Law (UNCITRAL) Conciliation Rules then obtaining, or according to such other procedures as may be agreed between the parties.

17.15. **Arbitration.** Unless any such dispute, controversy or claim between the parties arising out of or relating to this MOA or the breach, termination or invalidity thereof is settled amicably under Clause 17.14 within sixty (60) days after receipt by one party of the other party's request for such amicable settlement, such dispute, controversy or claim shall be referred by either party to arbitration in accordance with the UNCITRAL Arbitration Rules then obtaining, including its provisions on applicable law. The arbitral tribunal shall have no authority to award punitive damages. The parties shall be bound by any arbitration award rendered as a result of such arbitration as the final adjudication of any such controversy, claim or dispute. Any arbitration award rendered as a result of such arbitration shall bind the parties as the final adjudication of any such controversy, claim or dispute.

17.16. **Continuation of Work During Arbitration.** During the dispute or arbitration, the performance of the obligations of the parties shall not be stopped or put on hold except for such work as may be the subject matter of the dispute or arbitration, or is directly affected thereby.

IN WITNESS WHEREOF, the duly authorized representatives of the parties have signed these presents on __________ at __________.

**UNITED NATIONS DEVELOPMENT PROGRAM**

By:

DEBORAH LANDEY
Resident Representative

**SHELL SOLAR PHILIPPINES CORP.**

By:

RAMIN NADIMI
General Manager

**COOPERATIVE BANK OF PALAWAN, INC.**

By:

EPIFANIO C. MAGBANUA
Chairman

Signed in the Presence of:
ACKNOWLEDGMENT

Republic of the Philippines )
________________________) Ss.

BEFORE ME, a Notary Public for and in the above jurisdiction, this __________, personally appeared the following:

<table>
<thead>
<tr>
<th>Name</th>
<th>Comm. Tax Cert. No.</th>
<th>Date/Place Issued</th>
</tr>
</thead>
<tbody>
<tr>
<td>United Nations Development Program</td>
<td></td>
<td></td>
</tr>
<tr>
<td>By: Ms. Deborah Landey</td>
<td></td>
<td></td>
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<tr>
<td>Shell Solar Philippines Corp.</td>
<td></td>
<td></td>
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<tr>
<td>By: Mr. Ramin Nadimi</td>
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<tr>
<td>Cooperative Bank of Palawan, Inc.</td>
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<td></td>
</tr>
<tr>
<td>By: Mr. Epifanio C. Magbanua</td>
<td></td>
<td></td>
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</tbody>
</table>

who are known to me and to me known to be the persons who executed the foregoing instrument and they acknowledged to me that the same is their free and voluntary act and deed, and the free and voluntary act and deed of the entity/corporations represented.

WITNESS MY HAND AND SEAL.

Doc. No. _____;
Page No. _____;
Book No. _____;
Series of 2004.
1. Within three (3) working days from the date of receipt of the accomplished loan application, Coop Bank shall inform the concerned franchisee if applicant has passed the assessment of the Coop Bank and is considered qualified to avail of the loan accommodation to finance the acquisition of the SHS. Similarly, the Coop Bank shall also inform the franchisee if the applicant has failed the assessment without giving any reasons for denying the application to maintain confidentiality of information it has collated on applicant.

2. Within four (4) working days from date of Coop Bank notification as mentioned under 1 hereof, the Coop Bank shall process the required loan documentation, in coordination with the franchisee who hereby undertakes to help in the completion of requirements needed by the Coop Bank from the applicant.

3. Once the documentation and registration procedures have been completed, the Coop Bank shall release the proceeds of loan within three (3) working days. The loan proceeds shall be credited to the franchisee’s savings account maintained in the Coop Bank.
Annex B - Escrow Agreement
STATEMENT OF GENERAL BUSINESS PRINCIPLES

INTRODUCTION

This document reaffirms the general business principles that govern how each of the Shell companies which make up the Royal Dutch Shell Group of Companies conducts its affairs.

The Group is a decentralised, diversified group of companies with widespread activities, and each Shell company has wide freedom of action. However what we have in common is the Shell reputation. Upholding the Shell reputation is paramount. We are judged by how we act. Our reputation will be upheld if we act with honesty and integrity in all our dealings and we do what we think is right at all times within the legitimate role of business.

Shell companies have as their core values honesty, integrity and respect for people. Shell companies also firmly believe in the fundamental importance of the promotion of trust, openness, teamwork and professionalism, and in pride in what they do.

Our underlying corporate values determine our principles. These principles apply to all transactions, large or small, and describe the behaviour expected of every employee in every Shell company in the conduct of its business.

In turn, the application of these principles is underpinned by procedures within each Shell company which are designed to make sure that its employees understand the principles and that they act in accordance with them. We recognise that it is vital that our behaviour matches our intentions.

All the elements of this structure - values, principles and the accompanying procedures - are necessary.

Shell companies recognise that maintaining the trust and confidence of shareholders, employees, customers and other people with whom they do business, as well as the communities in which they work, is crucial to the Group's continued growth and success.

We intend to merit this trust by conducting ourselves according to the standards set out in our principles. These principles have served Shell companies well for many years. It is the responsibility of management to ensure that all employees are aware of these principles, and behave in accordance with the spirit as well as the letter of this statement.

1. OBJECTIVES

The objectives of Shell companies are to engage efficiently, responsibly and profitably in the oil, gas, chemicals and other selected businesses and to participate in the search for and development of other sources of energy. Shell companies seek a high standard of performance and aim to maintain a long-term position in their respective competitive environments.

2. RESPONSIBILITIES

Shell companies recognise five areas of responsibility:

a. To shareholders To protect shareholders' investment, and provide an acceptable return.

b. To customers To win and maintain customers by developing and providing products and services which offer value in terms of price, quality, safety and
environmental impact, which are supported by the requisite technological, environmental and commercial expertise.

c. To employees To respect the human rights of their employees, to provide their employees with good and safe conditions of work, and good and competitive terms and conditions of service, to promote the development and best use of human talent and equal opportunity employment, and to encourage the involvement of employees in the planning and direction of their work, and in the application of these principles within their company. It is recognised that commercial success depends on the full commitment of all employees.

d. To those with whom they do business To seek mutually beneficial relationships with contractors, suppliers and in joint ventures and to promote the application of these principles in so doing. The ability to promote these principles effectively will be an important factor in the decision to enter into or remain in such relationships.

e. To society To conduct business as responsible corporate members of, to observe the laws of the countries in which they operate, to express support for fundamental human rights in line with the legitimate role of business and to give proper regard to health, safety and the environment consistent with their commitment to contribute to sustainable development.

These five areas of responsibility are seen as inseparable. Therefore it is the duty of management continuously to assess the priorities and discharge its responsibilities as best it can on the basis of that assessment.

3. ECONOMIC PRINCIPLES

Profitability is essential to discharging these responsibilities and staying in business. It is a measure both of efficiency and of the value that customers place on Shell products and services. It is essential to the allocation of the necessary corporate resources and to support the continuing investment required to develop and produce future energy supplies to meet consumer needs. Without profits and a strong financial foundation it would not be possible to fulfil the responsibilities outlined above. Shell companies work in a wide variety of changing social, political and economic environments, but in general they believe that the interests of the community can be served most efficiently by a market economy.

Criteria for investment decisions are not exclusively economic in nature but also take into account social and environmental considerations and an appraisal of the security of the investment.

4. BUSINESS INTEGRITY

Shell companies insist on honesty, integrity and fairness in all aspects of their business and expect the same in their relationships with all those with whom they do business. The direct or indirect offer, payment, soliciting and acceptance of bribes in any form are unacceptable practices. Employees must avoid conflicts of interest between their private financial activities and their part in the conduct of company business. All business transactions on behalf of a Shell company must be reflected accurately and fairly in the accounts of the company in accordance with established procedures and be subject to audit.

5. POLITICAL ACTIVITIES

a. Of companies Shell companies act in a socially responsible manner within the laws of the countries in which they operate in pursuit of their legitimate commercial objectives. Shell companies do not make payments to political parties, organisations or their representatives or take any part in party politics. However, when dealing with
governments, Shell companies have the right and the responsibility to make their position known on any matter which affects themselves, their employees, their customers, or their shareholders. They also have the right to make their position known on matters affecting the community, where they have a contribution to make.

b. Of employees Where individuals wish to engage in activities in the community, including standing for election to public office, they will be given the opportunity to do so where this is appropriate in the light of local circumstances.

6. HEALTH, SAFETY AND THE ENVIRONMENT

Consistent with their commitment to contribute to sustainable development, Shell companies have a systematic approach to health, safety and environmental management in order to achieve continuous performance improvement. To this end Shell companies manage these matters as any other critical business activity, set targets for improvement, and measure, appraise and report performance.

7. THE COMMUNITY

The most important contribution that companies can make to the social and material progress of the countries in which they operate is in performing their basic activities as effectively as possible. In addition Shell companies take a constructive interest in societal matters which may not be directly related to the business.

Opportunities for involvement - for example through community, educational or donations programmes - will vary depending upon the size of the company concerned, the nature of the local society, and the scope for useful private initiatives.

8. COMPETITION

Shell companies support free enterprise. They seek to compete fairly and ethically and within the framework of applicable competition laws; they will not prevent others from competing freely with them.

9. COMMUNICATION

Shell companies recognise that in view of the importance of the activities in which they are engaged and their impact on national economies and individuals, open communication is essential. To this end, Shell companies have comprehensive corporate information programmes and provide full relevant information about their activities to legitimately interested parties, subject to any overriding considerations of business confidentiality and cost.
**Schedule of Activities**

<table>
<thead>
<tr>
<th>Time</th>
<th>Topic</th>
</tr>
</thead>
<tbody>
<tr>
<td>November 25</td>
<td></td>
</tr>
<tr>
<td>9:30 – 10:00 a.m.</td>
<td>Registration</td>
</tr>
<tr>
<td>10:00 – 11:00 a.m.</td>
<td>Welcome and Introduction</td>
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# PORTFOLIO MANAGEMENT COURSE
Legend Hotel, Puerto Princesa City, Palawan
November 25-27, 2004

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## Portfolio Data:

### Accounts

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<tr>
<th>Accounts</th>
<th>Current</th>
<th>Past Due</th>
<th>Fully Paid</th>
<th>TOTAL</th>
<th>Current</th>
<th>Past Due</th>
<th>Fully Paid</th>
<th>TOTAL</th>
<th>Current</th>
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<th>TOTAL</th>
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</thead>
<tbody>
<tr>
<td>Head Office_1/</td>
<td>217</td>
<td>3</td>
<td>12</td>
<td>232</td>
<td>PHP 3,895,488.00</td>
<td>PHP 52,272.00</td>
<td>PHP 207,200.00</td>
<td>PHP 4,154,960.00</td>
<td>PHP 3,134,549.78</td>
<td>PHP 35,406.08</td>
<td>PHP 3,169,955.86</td>
</tr>
<tr>
<td>Bataraza (Branch)_2/</td>
<td>224</td>
<td>8</td>
<td>22</td>
<td>254</td>
<td>3,962,796.00</td>
<td>139,392.00</td>
<td>386,128.00</td>
<td>4,488,316.00</td>
<td>3,473,966.99</td>
<td>72,437.28</td>
<td>3,546,404.27</td>
</tr>
<tr>
<td>Espanola (Branch)_3/</td>
<td>252</td>
<td>1</td>
<td>39</td>
<td>292</td>
<td>4,469,988.00</td>
<td>15,488.00</td>
<td>661,480.00</td>
<td>5,146,956.00</td>
<td>3,601,632.77</td>
<td>5,977.34</td>
<td>3,607,610.11</td>
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<tr>
<td>Aborlan (Branch)_4/</td>
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<td>2</td>
<td>0</td>
<td>10</td>
<td>141,552.00</td>
<td>32,912.00</td>
<td>-</td>
<td>174,464.00</td>
<td>95,048.49</td>
<td>19,887.69</td>
<td>114,936.18</td>
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<tr>
<td>Total</td>
<td>701</td>
<td>14</td>
<td>73</td>
<td>788</td>
<td>PHP 12,489,824.00</td>
<td>PHP 240,064.00</td>
<td>PHP 1,234,808.00</td>
<td>PHP 13,964,696.00</td>
<td>PHP 10,305,198.03</td>
<td>PHP 133,708.39</td>
<td>PHP 10,438,906.42</td>
</tr>
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_Funds to be Transferred from Deposit Account to Reserve Account as per Escrow Agreement Section 3.02(b)___

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### Defaulted Loans During Period

**Loan # | Borrower | Location | Outstanding Loan Principal | Accrued Interest* | Realized Value | Net Loss Calculation | Realized Value Date | Realized Value**
---
1 | Baga, Leonilla | Roxas Pal | Php 7,736.70 | Php 154.73 | Php 3,868.35 | Php 4,023.08 | NO | Php 4,023.08 |
---
Total | | | **Php 7,736.70** | | | **Php 4,023.08** | | |

*not greater than two months accrued interest