

MEMORANDUM

TO: James J. Steele / Bill Coy
 FROM: Jorge Asensio A.
 DATE: February 26, 1993
 REF: Payments to the Sun King group.

To comply with the Sun King Group we basically have two options. One is to pay in Guatemala with local currency, and the other is to pay in dollars abroad. Both alternatives however, have local tax implications that have to be met in order to be able to account for these payments legally, and be able to deduct such a substantial expense for tax purposes in Guatemala.

I have very little information on the Sun King contract, but I do know that they can select their bank of preference. Please be aware that this does not mean that if they select a bank in the U.S. or in England we have to pay in Dollars or in Pounds. Above all, I understand that this provision means that we can not force that group over the use of one bank.

The commitment to pay such commission that was inherited from the Texas-Ohio contract should be seen as an obligation that arises out of the Guatemalan operation. It should not be taken as an obligation by Enron Power Development Corp. just for the fact that this was the company that originally took the contract. Whatever contract was accepted by Enron, it had as a main goal to develop a project in Guatemala, so the commission should always be linked to that project, and as such to its local earnings.

Of course, any company in Guatemala may have expenses and obligations payable abroad, and have the obligation to get the dollars to meet those obligations. Foreign contractual obligations are also tax deductible.

So, in order to establish a frame work of references I recommend the following:

- a) Not to obligate Puerto Quetzal Power Corp to pay in dollars;
- b) To allow payment in dollars provided that Puerto Quetzal Power Corp. can get dollars without limiting its own access to hard currency. In other words, Puerto Quetzal Power Corp. will leave any dollar obligation in last place, so if we are able to comply by getting the dollars we will, but if no sufficient dollars are available we will pay in Quetzales. This is strongly supported by two things: - We are paid in Quetzales and not in dollars; - The exchange mechanisms do not allow a free conversion to dollars, so it is obvious that Puerto Quetzal Power Corp. will apply its few dollars to pay for the

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elements that are needed to maintain the operation running. By the way, in David Haug's letter to the Sun King group dated march 12, 1992 he indicates that payments will be made to them at 6 av. 20-25 zona 10 in Guatemala City. There is no indication of payments abroad. The actual agreement between Enron and Texas-Ohio does not indicate anything with respect to form or place of payment.

- c) All payments are gross, including any taxes levied in Guatemala to either local or foreign obligations. Puerto Quetzal Power Corp. will not pay any taxes on behalf of Sun King. You must understand that guatemalan tax legislation levies withholding taxes on payments abroad where the payee is the taxpayer, even if the payor has the obligation to pay the withholding.
- d) Any charges or expenses, present or future that are charged in the exchange mechanism, and all fees involved in the Quetzal-Dollar conversion will also be discounted to the payee.
- e) Payments only cover the revenue obtained from the sale of electricity derived from the two barges. Any other revenue derived from future production is not part of the deal. By now Enron can promote itself in Guatemala.
- f) The term of the obligation in the original Texas-Ohio - Empresa Eléctrica de Guatemala, S.A. contract is 15 years. If the Sun King contract does not refer to any term, we should try to negotiate a more convenient term. I suggest 5 years. I understand that the 15 year term of the original contract was something requested by Empresa Eléctrica de Guatemala S.A. to Texas-Ohio and not a product of Sun King as a group pushing for that term.
- g) Given the fact that the Sun King payments do not represent any REAL service to Puerto Quetzal Power Corp. it is always possible that our tax authorities could disallow that deduction in the future. In this regard, I strongly recommend that we condition payments on the basis of their deductibility: payments will be made provided that they are deductible. I also recommend that the contract as such, and the invoicing be carefully drafted in order to avoid these problems. We should be very credible at the time of invoicing.
- h) It is also important to try to "lock-in" today's charges in the Empresa Eléctrica de Guatemala S.A. - Puerto Quetzal Power Corp. contract in order to avoid and endless increase in the 6% commission. If any increases for electricity charge have to be made to Empresa Eléctrica de Guatemala S.A. due to oil prices or otherwise, we should be able to invoice these increments as "overcharges" or "overcosts" in order to keep current prices permanently charged as our basic contractual stipulation, and only pay the 6% based on this basic price. Otherwise, any increment in cost is directly favorable to Sun King, an aspect of our relationship with Empresa Eléctrica de Guatemala, S.A. that doesn't help much.

After giving you these ideas, I now want to explain the difference between local and foreign payments regarding the tax issue.

I will use an example of a monthly gross income of Q20,000,000.00

LOCAL PAYMENTS:

Q20,000,000.00 = 6% = Q1,800,000.00 which should be INVOICED as follows:

Sun King invoice for	Q1,682,242.99
+ VAT tax of 7%	<u>Q 117,757.01</u>
TOTAL INVOICED AMOUNT	Q1,800,000.00
 This is paid as follows:	
VAT tax	Q1,682,242.99
	<u>Q 117,757.01</u>
	Q1,800,000.00
4% withholding on fees and commissions:	<u>Q 67,289.72-</u>
Actual payment:	Q1,732,710.28

The withholding tax is paid by us to the tax department on account of Sun King's income tax.

FOREIGN PAYMENTS:

Q20,000,000.00 6% =	Q1,800,000.00
Withholding of 25% =	<u>Q 432,000.00</u>
Balance due =	Q1,368,000.00

If we pay dollars at 5.30 x 1US\$ = US\$ 258,113.21 and this will be the amount paid.

If Sun King is an American company it should pay income tax in the US if they receive payment this way. In the event of local payments in Guatemala they will also be subject to income tax of 25% after expenses are deducted.

Another warning which I find very important in this case, is the one related to the definition of "Commissions", as we are considering periodical payments of commissions to Sun King. The Guatemalan Tax Authorities have always considered that a "commission" is a one shot deal, payable upon termination of a single transaction. A commission payable periodically is understood by them as being a "royalty". I recommend to define our payments to Sun King correctly as "royalties" in order to withhold 25% but, in the event of any adjustments or tax modifications, Sun King could petition Government for recognition of commission status and thus pay a 12.5% withholding due on commissions. The advantage of paying royalties is the

fact that these are basically justified by the contract. Commissions though, have to be justified by the nature of the transaction involved.

GROSSING UP ALL THE COMMISSION:

If it is preferred that Puerto Quetzal Power Corp. pay the "periodic commissions" rather than "Royalties", the following concept could accomplish that.

Another possibility, provided we maintain a 15 year contract with Sun King, is to determine a ceiling on the overall value of the 6% commission payable to SUN KING during the fifteen years of the contract, and establish a fixed amount to be paid every month for fifteen years. This payment would be attached to a provision that considers every monthly payment as a maximum, and that if a lesser amount is invoiced to Empresa Eléctrica de Guatemala, S.A. in a given month, the corresponding deduction would be applied.

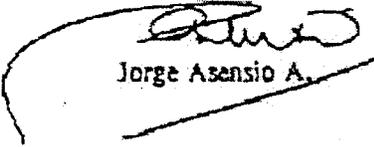
This alternative has the following advantages:

- a) We put a ceiling to the overall commission payments;
- b) If any costs go up in the future, the commission will stay the same. It would be variable in the sense that being subject to a lesser monthly charge, we still pay the commission for the amount invoiced, but never beyond current charges.
- c) The concept of a "commission" payable periodically, which is preferred to a "Royalty" for withholding purposes is much better founded this way, than an independent monthly payment of commissions.

The main disadvantage:

- a) A grossed up amount may be seen as very attractive, making future negotiations for a buy out more difficult and expensive.

If you need further information I will be delighted to extend this memo.


Jorge Asensio A.