

PROJECT FINANCING IN THE CARIBBEAN



Caribbean Commercial Law Workshop
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PROJECT FINANCE:

- The financing of the development or exploitation of a right, natural resource or other asset where the bulk of the financing is to be provided by way of debt and is to be repaid principally out of the asset being financed and its revenues.

Why Choose Project Finance

- Insulation of sponsors
- Non-consolidation of project debt onto sponsor's balance sheets
- Sharing of risk with others
- Sponsor's ability to borrow limited by covenants – negative pledge

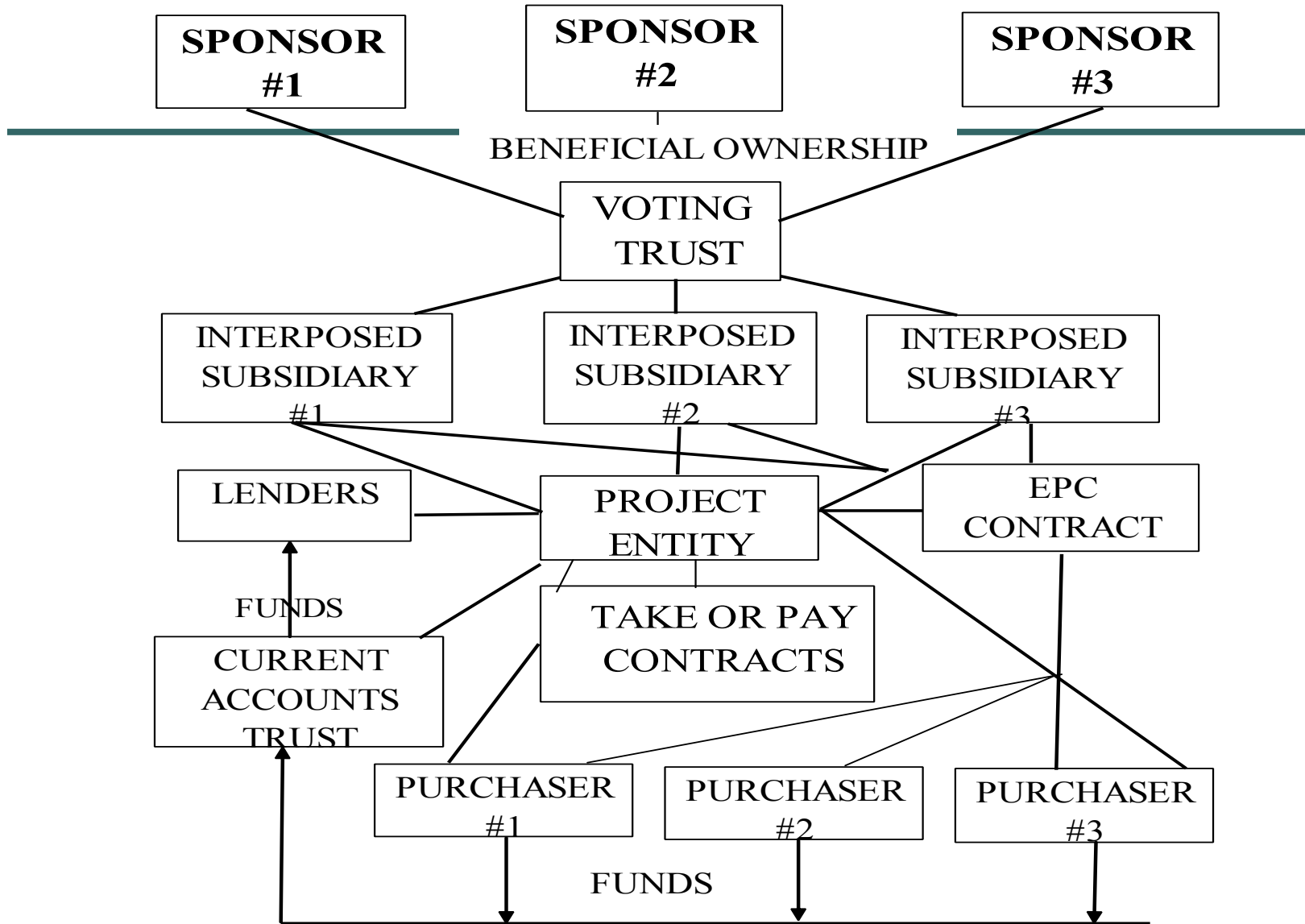
Why Choose Project Finance

- Sponsor engaging in multiple projects compelling need for external financing
- Multiple sponsors make sharing of risks extremely difficult, therefore SPV is an attractive option
- Tax advantages in some jurisdictions
- Jurisdiction may compel use of locally incorporated vehicle.

Key Sponsor Issues

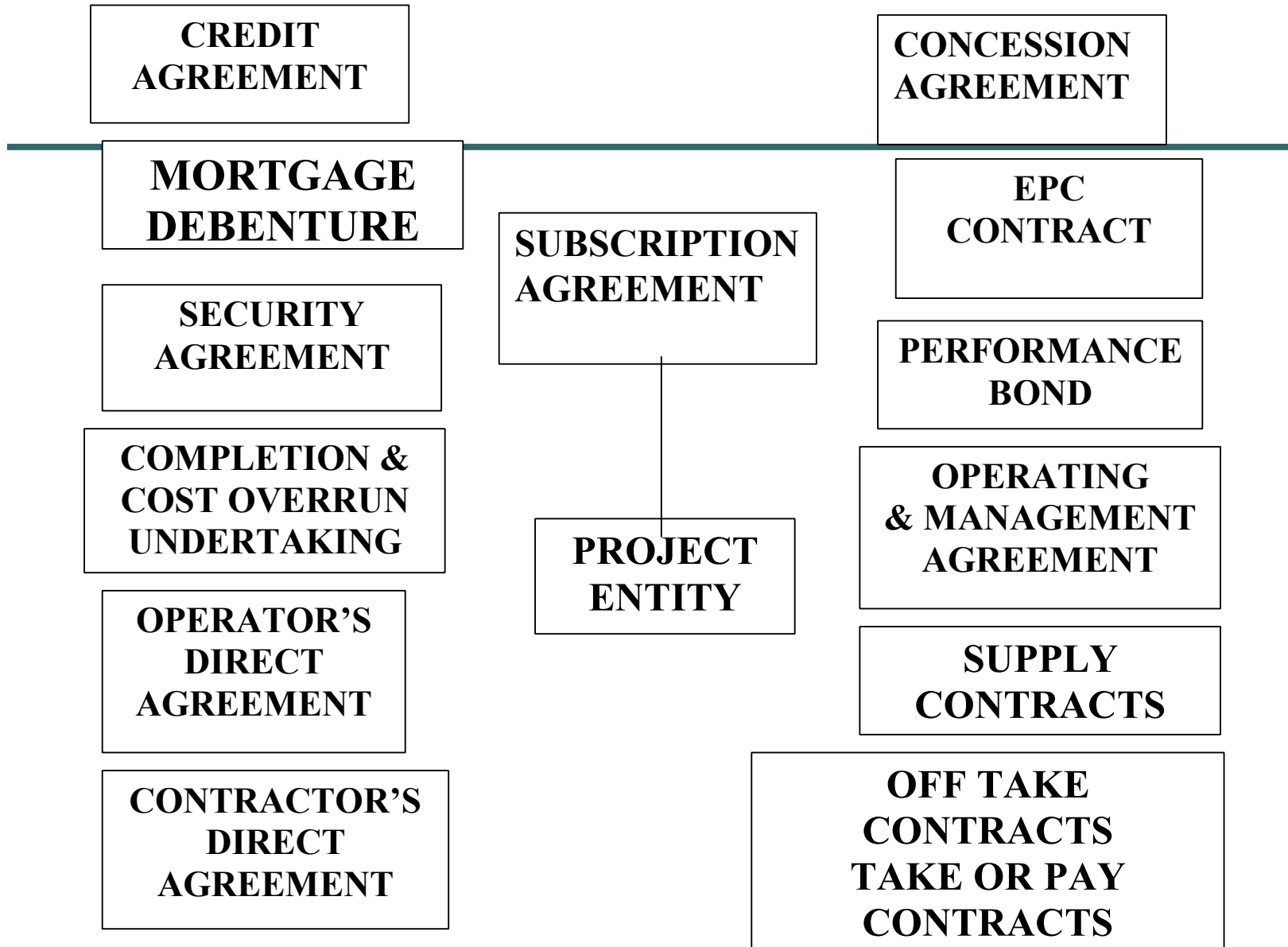
- Respective roles of each sponsor
- Appointment of advisers to the project
- Capitalization of project (Debt/Equity Ratio)
- Dividend distribution policy
- Management of project vehicle
- Sales of shares and pre-emption rights

PROJECT STRUCTURE



October 6, 2011

PROJECT FINANCE OUTLINE



Parties to Project Financing

- **Project Company not to (Negative Covenants):**
- Incur incur further financial indebtedness
- Create further security interests
- enter agreements unconnected to project
- lend money or make investments

Parties to Project Financing

- **change accounting period**
- **pay dividends**
- **change its constitutional documents**
- **create subsidiaries**

Sponsors

- often involved in aspects of project, including:
 - Construction
 - Operation/Maintenance
 - Purchases of services or output
 - Ownership of land

Banks

- Arranging banks
- Syndication
- Facility agent
- Technical bank
- Insurance bank
- Account bank

Banks

- **Multilateral & Export Credit Agencies**
- political risk insurance
- commercial risk insurance
- insurance against adverse currency movements
- interest rate support
- direct lending

Construction Company

- Turnkey contract
- Engineering design, procurement and construction
- Track record
- Project management

Experts

- **Consultants/Professional Firms**
- Insurance
- Environment
- Technical/Engineering

Documentation

1. Shareholder/Sponsor Arrangements
2. Loan & Security Documents
3. Project Documents

1. Sponsor Documentation

- Pre-development agreements
 - Feasibility study
 - Appointment of advisers
 - Scope of arrangements
 - Confidentiality
 - Competition restrictions

Sponsor Documentation

- Shareholders' Agreement/Joint Venture Agreement
 - Equity injection
 - Funding
 - Voting
 - Dispute Resolution
 - Dividend Policy
 - Management
 - Share transfer/pre-emption rights

Sponsor Documentation

- Lender Concerns
 - Identity/credit worthiness sponsors
 - Management resources/expertise
 - Triggers for further equity injection
 - Direct commitment to lender re-equity **vs** assignment

Sponsor Documentation

- Lender Concerns (cont'd)
 - Assignment limitations:
 - limited to loss of assignor
 - set-off/counter-claim by sponsor
 - not survive winding-up project company

Sponsor Documentation

- Lender Concerns (cont'd)
 - damages based claim weakness:
 - causation
 - remoteness
 - mitigation

Sponsor Documentation

- Shareholders Support Agreement
 - Management/Technical assistance
 - Funding
 - Equity/Subordinated loan
 - Share transfer limitation
 - Completion guarantees
 - Security requirements

2.

Loan & Security Documentation

- Project Loan Agreement
 - Drawdown requirements
 - Interest (capitalization construction period)
 - Principal repayment
 - Warranties, covenants, events of default

Loan & Security Documentation

- Project bank accounts:
 - sales proceeds
 - insurance receipts
 - liquidated damages
 - Sponsor payments

Loan & Security Documentation

- **Project Loan Agreement (cont'd)**
 - Waterfall arrangements
 - Appointment of experts
 - Information and access (annual accounts, etc.)
 - Cover ratios (software model)
 - Governing law

Loan & Security Documentation

- **Project Loan Agreement (cont'd)**
- Completion tests:
 - Physical completion certificate
 - Performance criteria certificate
 - Operational reliability

Loan & Security Documentation

- Security Document
 - Universal Security Interest (common law)
 - Enforcement without court intervention
 - Priority for fixed charges
 - Security over all types of assets (present and future)
 - Floating charge
 - Non-possessory security interest

Loan & Security Documentation

- Security Document (cont'd)
 - No requirement for specific identification of assets
 - Central registration system
 - No liability on security holders (but shadow director concerns)
 - Trust concept (permit transfer security/ underlying loan)

Loan & Security Documentation

- Security Interest on Key Assets of SPV
 - Concession agreement
 - Plant and machinery
 - Real property (including leasehold)
 - Construction contract (EPC)
 - Performance bonds/guarantees

Loan & Security Documentation

- Security Interest on Key Assets of SPV
 - Project agreements
 - Project insurances
 - Project Bank accounts
 - Product
 - Other project assets

WATERFALL ARRANGEMENTS PROJECT ACCOUNTS

PROJECT REVENUES ACCOUNT

OPERATING ACCOUNT

DEBT SERVICE ACCOUNT

DEBT RESERVE ACCOUNT

TAXES ACCOUNT

MAJOR MAINTENANCE ACCOUNT

F F & E REPLACEMENT ACCOUNT

INSURANCE ACCOUNT

DISTRIBUTION ACCOUNT

Loan & Security Documentation

- **Third-Party Security**
 - Shares in SPV
 - Completion guarantees
 - Cost overrun guarantees
 - Management agreements
 - Equity contribution agreements
 - Collateral warranties (professionals)

Loan & Security Documentation

- Third-Party Security (cont'd)
 - Direct agreements (government/
contractor/supplier/off taker/operator
 - notice to third party
 - third party notice to lender of default
 - suspension termination
 - step-in rights by lender as its SPV
 - step-out rights

Loan & Security Documentation

- **Third-Party Security** (cont'd)
 - Direct agreements (government/
contractor/supplier/off taker/operator
 - acceleration step-in right
 - waiver set-off or counter claim
 - no amendment
 - payments direct to lenders

Loan & Security Documentation

- **Host Government Support**
 - No change of law (non-discrimination)
 - Foreign exchange guarantee
 - No expropriation/nationalisation without compensation
 - Taxation levels (non-discrimination)
 - Exchange controls
 - Consents and permits

Loan & Security Documentation

- Comfort Letters
 - Binding
 - Non-binding

Loan & Security Documentation

- Governing Law

- **Asset**

- Land and buildings
- Registered assets
- Physical chattels/
negotiable
instruments
Benefit of contract/
receivables

Applicable Law

Location of asset
Country of
registration
Location at
mortgage date
Governing law of
contract

Loan & Security Documentation

- Security Trusts
- Advantages
 - Trading of loans
 - Risk of collateral agent insolvency eliminated
 - Transfer security

Loan & Security Documentation

- **Intercreditor Arrangements**
 - Order of drawdowns
 - Maturities of different classes
 - Priority distribution project revenues
 - Restrictions on amendment to finance documents
 - Acceleration and enforcement rights
 - Priority of enforcement proceeds

3. Project Documents

- **Concession Agreement**
 - Duration
 - Project company/duties with respect to project
 - Concession grantor duties
 - non-competition
 - utilities
 - change of law

Project Documents

(cont'd)

- **Concession Agreement (cont'd)**
 - Concession fees (where applicable)
 - Default and forfeiture terms
 - Assignments and transfers
 - Termination expiration (education and training)

Project Documents

- **Construction Contracts**
 - Turnkey EPC Contract
 - on-time completion
 - guaranteed performance standards
 - design, supply, construction
 - testing and commissioning
 - guarantee of performance of all components – sub-contractors

Project Documents

- **Project Company/Sponsor Project Management**
 - experience in management design and construction
 - cost or time saving
 - lender verify technical capacity and resources
 - lender require added sponsor support

Project Documents

- **Construction Contracts (cont'd)**
 - Project Management Structure
 - Project Management Company
 - individual contractors
 - lender concerns:
 - unallocated responsibilities
 - greater contract and risk analysis
 - claims between different contractors

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- Construction Contracts (cont'd)
 - Key Provisions Construction Contracts
 - Price and payment terms:
 - deposit/advice on equipment
 - stage payments
 - unforeseen inflation risk – who bears?
 - consent for variations
 - risk of contract breach

Project Documents

- Completion
 - postponement in limited specified circumstances
 - impact of postponement on other Project Documents (e.g. Concession Agreement)

Project Documents

- **Construction Contracts (cont'd)**
 - Liquidated damages for delay
 - cover interest and operating costs during delay
 - independent consultant to certify:
 - physical completion
 - commissioning
 - performance tests

Project Documents

- **Construction Contracts (cont'd)**
 - Force Majeure
 - performance impossible
 - be irresistible
 - be external – no fault or negligence of party affected
 - Done everything in its power to perform

Project Documents

- **Construction Contracts (cont'd)**
 - Warranties
 - quality and fitness for purpose
 - match any given to Concession Grantor
 - Insurance
 - contractors' All Risk

Project Documents

- **Construction Contracts (cont'd)**
 - Consents
 - planning approvals
 - health safety & environment
 - fire and building regulations

Project Documents

(cont'd)

- **Construction Contracts (cont'd)**
 - Limitations on Liability
 - Lender's preference - no limit or high limit
 - Sponsors consider impact on pricing
 - Contractor desire for upper limit

Project Documents

(cont'd)

- **Operating & Maintenance Agreements**
 - Skillful operator – crucial to success
 - Proven track record
 - If Project Company, lender to be satisfied by experienced and necessary staffing

Project Documents

- **Operating & Maintenance Agreements**
(cont'd)
 - **Objectives**
 - allocating risk to operator (insulating Project Company)
 - maximum revenue earning capacity
 - quality of operation and maintenance
 - achievement of targets
 - within budget

Project Documents

- **Operating & Maintenance Agreements**
(cont'd)
 - Fixed Price Structure
 - cost over-runs borne by operator
 - cost savings - greater profit to operator
 - Cost Plus Structure
 - fixed fee
 - cost of operating
 - termination of budget exceeded

Project Documents

- **Operating & Maintenance Agreement (cont'd)**
 - Incentive/Penalty Structure (Lender preferred)
 - strict performance targets
 - bonus achievements
 - reduced compensation non-achievement
 - Bonus and penalty cops

Project Documents

- **Fuel Supply Agreements**
 - Take or Pay Contracts
 - agreed volume
 - agreed price (may be widened)
 - pay for supplies not taken subject to make-up provision
 - obligation to supply

Project Documents

- **Fuel Supply Agreements (cont'd)**
- Sole Supplier Contracts
- Single source for all project requirements
- volume and price not specified
- payment for actual use
- no obligation to supply

Project Documents

- **Sales/Off-take Agreements**
- Pass through agreement (charges based on production cost)
 - raw material cost
 - operating and maintenance costs
 - administrative costs

Project Documents

- **Sales/Off-take Agreements (cont'd)**
 - Insurance
 - principal repayments to costs
 - interest payments to lenders
 - sponsor's return on lenders' capital

Project Documents

- Take or Pay Agreement
- buyer pays of available for delivery
- 'hell or high water'
- price indexed (may be subject floor and ceiling)
- consider enforceability
 - is it a penalty?
 - adequacy of consideration in some jurisdictions

Project Documents

- **Other Project Documents**
- Throughput Agreements
- Tolling Agreements
- Technology/operating licenses
- Consultancy Contracts
- Utility Agreements
- Refining Agreements
- Transportation Agreements

Project Documents

- **Lender Concerns**
- Assignability of project agreements
- Negative pledge
- Termination rights of counter-party
- Expiry revocation rights licenses or concessions
- Force Majeure commonality
- Liquidated damages enforceability
- Forfeiture/withering rights
- Third party pre-emption rights
- Non-performance set-off by third parties

Project Documents

- Conditional effectiveness of concession
- Payment terms, currency, payment to lender's agent, no reduction for withholding taxes, grossing up
- Credit rating of bonding company or bank
- Subordination of sponsor security
- Take-out provisions to replace exiting sponsor

Project Documents

- Governing law
- Arbitration clauses not favoured unless judicial system not equipped for sophisticated international disputes

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THANK YOU

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