



Guidance on PPP Contractual Provisions

2019 EDITION

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This current edition of the Guidance on PPP Contractual Provisions, 2019 Edition (“Guidance”) is largely based upon work done by the international law firm of Allen & Overy LLP, under a team led by David Lee, Helga Van Peer, Tim Conduit, Fleur Clegg and Sarah Garvey, with input from across Allen & Overy’s global PPP practice. It builds on the Guidance’s 2017 edition on which Allen & Overy LLP also worked and which expanded the Guidance’s first edition, known as “Report on Recommended PPP Contractual Provisions, 2015 Edition”, as developed by a Paris-based team of the international law firm of Gide Loyrette Nouel. The work done by both Allen & Overy LLP on this 2019 and on the 2017 edition and Gide Loyrette Nouel on the 2015 Report was generously funded by the Public-private Infrastructure Advisory Facility (PPIAF). PPIAF, a multi-donor trust fund housed in the World Bank Group, provides technical assistance to governments in developing countries. PPIAF’s main goal is to create enabling environments through high-impact partnerships that facilitate private investment in infrastructure. For more information, visit www.ppiaf.org

The Guidance received expert technical support from various World Bank Group staff, including from the World Bank’s Legal Vice Presidency, the International Finance Corporation (IFC), the Multilateral Investment Guarantee Agency (MIGA) and the International Centre for Settlement of Investor Disputes (ICSID). In addition, special thanks is due to the Global Infrastructure Hub (GIH), the African Legal Support Facility (ALSF), the Inter-American Development Bank (IDB) as well as all those organizations, entities and firms that participated in the public consultations conducted on the contents of both the 2017 and the 2019 edition of the Guidance.

With the support of Allen & Overy LLP, the various comments and suggestions from all of the above sources were edited by Christina Paul and Susanne Foerster, lawyers within the World Bank’s Infrastructure Finance, PPPs & Guarantees Group.

INTRODUCTION

This Guidance contains guidance and example drafting in relation to a number of core PPP contractual clauses and is intended to aid Contracting Authorities who have decided to use PPP as the procurement method for a project. The Guidance is not a recommendation to use PPP or an analysis of its advantages or disadvantages. The merits of opting for a PPP model need to be assessed on a case-by-case basis, taking into account the relevant sector, project and other actual circumstances. Given the variety of PPP transactions carried out globally; the different legal systems existing in various countries; and the need to have ‘tailor-made’ provisions to deal with the individual characteristics of specific projects, the development of complete PPP Contracts on an international basis is likely an unrealistic goal. Nevertheless, there is merit in focusing on certain contractual provisions dealing with particular legal issues encountered in virtually every PPP Contract/structure, such as, for example, the issues of Force Majeure, termination rights or dispute resolution. For a project to be successful, the contractual format (for example, PPP) is important, however other factors – such as a country’s legal regime, the management of the procurement process and the quality of the bidders – will be even more important.

Public-Private Partnerships (“PPPs”) are now being used in many countries to develop infrastructure projects. While PPP transactions in this context are typically based on a network of complex legal agreements, at the center of each such transaction there is normally a form of contract between a public authority (the “Contracting Authority”) and a private company (the “Private Partner”). This may be a contract for particular works and services or a form of a concession agreement through which the Contracting Authority effectively gives the Private Partner the right to carry out a particular service. For the purposes of this Guidance, the form of contract is generically referred to as the “PPP Contract”.

The complexity and sophistication of PPP transactions, and the fact that they are often heavily negotiated to reflect the characteristics of a given infrastructure project, frequently means that considerable time and expense is involved in preparing and finalizing PPP Contracts. This has led many commentators to ask if it is possible to reduce costs, and shorten the time involved in such processes, by standardizing the provisions found in PPP Contracts between the Contracting Authority and the Private Partner. In a number of countries efforts have been made to develop complete standardized PPP Contracts for different types of infrastructure projects, such as roads, railways, ports or power generation. To date, however, there is no universally accepted language for such agreements on an international basis.

Against this background, the World Bank Group developed the Report on Recommended PPP Contractual Provisions, 2015 Edition (the “2015 Report”) which presented the first attempt by a Multilateral Development Bank to prepare a compilation of “recommended” language in respect of a selection of these typically encountered provisions. Following internal and external consultations on the contents of the 2015 Report, it was in response to the industry feedback received then that the 2017 edition was developed. This version built on the contractual provisions outlined in the 2015 Report and complemented these with detailed commentaries concerning key considerations relevant for Contracting Authorities due to different levels of PPP transactional experience or due to the characteristics of different legal systems. With

the support of the Global Infrastructure Facility (GIF), the 2017 edition also entailed two additional chapters that address contractual considerations related specifically to bond financed and corporately financed PPP transactions.

The 2019 edition of the Guidance expands on this previous edition by updating the existing eleven chapters in accordance with further stakeholder feedback received, including the consideration of themes such as climate change and environmental/social issues in the context of PPP Contracts. It also includes three additional chapters on contracting authority step-in rights, termination events, and handback of assets at the end of the PPP Contract. The overall objective of the Guidance remains to assist its target audience, namely Contracting Authorities – and particularly those in Emerging Markets – with obtaining a more comprehensive understanding of essential clauses in a PPP Contract and to help them to carefully assess the issues specific to their own PPP Project and jurisdiction when developing contractual provisions.

In regard to the sample drafting contained in this document, the authors would like to emphasize that it is not intended to be exhaustive or prescriptive – specifically, it is not meant to be mandatory for use in all PPP transactions which the World Bank Group financially supports. Instead, the objective of the Guidance is to set out and analyze contractual language that has formed the basis of many successfully procured PPP transactions, and to describe the rationale for these provisions. In doing so, the authors of the Guidance hope to foster discussion and consensus-building around these provisions and of appropriate contractual language in PPP transactions generally, with a view to helping to reduce the aforementioned time and expense associated with PPP Contract development.

As in any document of this type, some cautionary notes should be emphasized. As indicated, PPP transactions are usually very complex, and extensive due diligence – with the assistance of qualified legal, financial and technical specialists – needs to be undertaken by both Contracting Authorities and private parties before concluding a PPP Contract and related agreements. In this regard, the contents of this Guidance should simply be regarded as a suggested starting point and one of many inputs for the contracting parties to consider.

Also, many of the provisions set out in the Guidance will affect the allocation of risks in a PPP transaction – and the fairness of the overall risk allocation in a transaction can only be assessed by consideration of the entirety of the PPP Contract and related agreements. Where appropriate, suggested contractual language has been linked to the sample matrices showing the allocation of risks between public and private sectors in typical PPP transactions as contained in the PPP Risk Allocation Tool 2019 Edition developed by the Global Infrastructure Hub. It should likewise be noted that this Guidance primarily focuses on PPP transactions on a project finance basis, as reflected by the attention given to the involvement of third party lenders and the sharing of the benefits of refinancing, although other financing approaches are contemplated as reflected by the section on Corporate Financing.

This being the third edition, the authors would finally like to stress that this publication is seen as an evolving process. The intention is to develop further iterations of the Guidance once further industry feedback has been collected and as and when new consensus develops around the provisions considered in the document or in connection with an analysis of other contractual language typical of successful PPP transactions.

DEFINED TERMS

Capitalized terms in this Guidance have the meanings set out below and additional capitalized terms used in the Sample Drafting sections are defined in those sections.

Base Case Equity IRR	has the meaning set out in Section 5, Refinancing .
Contracting Authority	means the public authority that enters into the PPP Contract with the Private Partner.
Developed Market	means a jurisdiction or sector that has experienced successful financial close and operation of PPP projects, typically with a stable political and economic system and a fair and predictable legal system. A jurisdiction or sector which is stable in these terms may not be a Developed Market in a PPP context or may only be a Developed Market in certain sectors or contexts, but an Emerging Market in others.
Direct Agreement	means an agreement entered into by the Contracting Authority and the Lenders (and the Private Partner) in connection with the PPP Contract, as described in Section 7, Lenders' Step-in Rights .
Dutch Model	means Version 5.0 of the Netherlands Standard PPP Contract published in June (accommodation) and July (infrastructure) 2018. See links in Appendix A, Additional PPP Resources .
Emerging Market	means a jurisdiction or sector in which few PPP projects have been commenced, sometimes (but not necessarily) with a legal, political or economic system which may entail a degree of unpredictability. A jurisdiction or sector which is less stable in these terms may not be an Emerging Market in a PPP context or may only be an Emerging Market in certain sectors or contexts, but a Developed Market in others.
Equity Investors	means, at any time, the Shareholders and/or their parent companies, as the context requires.
Estimated Change in Project Costs	has the meaning set out in Section 3, Change in Law .
Infra Australia PPP Guidelines	means the <i>National Public-private Partnership Guidelines, Volume 3: National Commercial Principles for Social Infrastructure (December 2008)</i> and/or the <i>National Public-private Partnership Guidelines, Volume 7: National Commercial Principles for Economic Infrastructure (February 2017)</i> published by the Australian Government Department of Infrastructure and Regional Development. See links in Appendix A, Additional PPP Resources .

Lenders	means the finance parties under the Senior Finance Documents providing senior debt to the Private Partner [and/or the Issuer – see Section 9, Bond Financing] for the purpose of the PPP Project (excluding the Shareholders and their affiliates, as providers of equity or subordinated debt).
MAGA	means Material Adverse Government Action as further described in Section 2, Material Adverse Government Action .
Original Base Case	has the meaning set out in Section 8, Termination Payments in Section 8.7, Sample Drafting 8 .
Party or Parties	means the Contracting Authority and/or the Private Partner, as the context requires.
PPP	means Public-Private Partnership. See also definition of "PPP Contract" .
PPP Contract	means the long-term agreement between the Contracting Authority and the Private Partner, for providing a public asset or service, in which the Private Partner bears significant risk and management responsibility, and remuneration is linked to performance. ¹
PPP Project	means the underlying project which is the subject of the PPP Contract.
Private Partner	means the private company that enters into the PPP Contract with the Contracting Authority. The Private Partner often takes the form of a special purpose company.
Project Agreements	means the [Sub-contracts (the construction contract, the operating and maintenance agreement), any offtake agreement, the land lease agreement] ² .
Senior Finance Documents	has the meaning set out in Section 8, Termination Payments in Section 8.7, Sample Drafting 8 .
Shareholders	means, at any time, any person holding share capital in the Private Partner [adapt as appropriate to reflect financing and holding structure].
South Africa PPP Guidelines	means South Africa's National Treasury Standardized PPP Provisions: First Issue, published 11 March 2004. See link in Appendix A, Additional PPP Resources .
Sponsors	has the same meaning as Equity Investors.
Sub-contracts	means the main Sub-contracts entered into by the Private Partner in connection with the construction and operation of the PPP Project (e.g. the construction contract and the operation and maintenance contract).
Sub-contractor	means [the Private Partner's counterparty to a Sub-contract (e.g. the construction Sub-contractor and the operation and maintenance Sub-contractor)].
UK PF2 Guidance	means the <i>Standardisation of PF2 Contracts (Draft)</i> guidance issued by HM Treasury in the United Kingdom, launched on 5 December 2012 (withdrawn as regards new government projects on 28 November 2018). See link in Appendix A, Additional PPP Resources .

¹ There is no single, internationally accepted, definition of Public-Private Partnership. This definition is the definition provided in the *PPP Reference Guide Version 3.0*, dated April 2017. [See link in Appendix A, Additional PPP Resources](#).

² To be tailored on a project-by-project basis to refer to the material contracts entered into by the Private Partner in connection with and relevant for the PPP Project.

PPP CONTRACTS IN CONTEXT

AIM OF GUIDANCE

This Guidance is intended to provide Contracting Authorities who have decided to use PPP as the procurement method for a project with an analysis of, and drafting guidance for, certain specific provisions that are typically included in a PPP Contract and/or its related agreements in order to achieve a successfully financed PPP Project that will deliver the service or asset desired by the Contracting Authority. The Guidance should be seen as a starting point – a signpost for how to approach key issues which will be influenced and determined according to the specific circumstances of the PPP Project or project as a whole and as part of the whole contractual arrangements. The Guidance does not cover all the provisions which are typically seen in a PPP Contract. Recognising that there can be no “one size fits all” approach given the ranges of sectors, jurisdictions and projects in the PPP market, the Guidance focuses on certain contractual provisions dealing with particular legal issues encountered in virtually every PPP Contract/structure, such as, for example, the issues of Force Majeure, termination rights or dispute resolution. Appendix B sets out an overarching list of the provisions usually seen in a PPP Contract.³

The Guidance is not a recommendation to use PPP or an analysis of its pros and cons as a procurement model; the merits of opting for a PPP model need to be assessed on a case-by-case basis, taking into account the relevant sector, project and other actual circumstances. While the contractual format (for example, PPP) is important, other factors – such as a country’s legal regime, the management of the procurement process and the quality of the bidders – will be even more important to achieve a successful project.

The Guidance draws on over 20 years’ PPP market practice internationally, including guidance published by governmental bodies for Contracting Authorities, as well as the extensive experience of legal advisers supporting Contracting Authorities, Private Partners and different types of funders on PPP Projects, in both Developed and Emerging Markets. This unique and comprehensive perspective enables the Guidance to present a real-world view of contractual issues and outcomes to help Contracting Authorities manage the private sector’s expectations, as well as their own, after they have selected PPP as a method of infrastructure procurement.

PPP AS CHOSEN PROCUREMENT METHOD

PPP is just one of the procurement methods in a Contracting Authority’s toolkit to procure infrastructure assets and related service provision. Most methods available to governments typically involve some level of private sector involvement, whether through traditional procurement of the construction of an asset or the outsourcing of the operation of an asset or service, or through joint venture, privatization or the establishment of regulated utilities and businesses. This Guidance assumes that the Contracting Authority has carried out a

³ For resources which contain guidance on other contractual provisions in PPP Contracts, see the resources in [Appendix A, Additional PPP Resources](#).

thorough analysis in relation to how best to procure its infrastructure and has concluded that a PPP procurement is the right method for the project in question, taking into account all relevant aspects including its feasibility, value for money and affordability for the Contracting Authority, as well as wider governmental factors such as fiscal policy and, for example, upholding the G20 Principles for Quality Infrastructure Investment⁴. In coming to this conclusion, the Contracting Authority may have its own government procurement guidance to follow and can also draw on guidance published by various bodies, including the World Bank and its partners.⁵

As highlighted below in *Section K*, the foundations for a successful PPP Contract include a clear and transparent procurement process. This is because the design of the procurement process itself affects the ability of governments to identify which projects are best done as PPPs and to manage contracts in a transparent and effective way.⁶

It is also important to bear in mind that many of the issues applicable to other forms of infrastructure procurement are equally, and often particularly, relevant to procuring PPP Contracts – issues such as sustainable development, inclusivity, climate change and social and environmental impact (discussed further below). PPP is typically a small proportion of a government’s infrastructure procurement plan, yet the challenges and opportunities involved tend to receive more focus in a PPP context due to the long-term nature and high value of the contracts. These types of important matters are not unique to PPP, but PPP can offer an opportunity to find innovative solutions in a competitive environment.

The procurement process will serve to determine the contractual rights and obligations of the Parties throughout the lifespan of the PPP Project, and, ultimately, the impact the PPP Project has on the environment, the wider economy (including employment) and society. This is why it is so important to set the right minimum requirements and criteria when designing the tender process for the award of a PPP Project. Choosing the right tender process and setting the right standards and criteria will also define the quality of the competition. It will drive the nature and engagement of the bidders (who will only want to invest time and resources in the bid process if they feel that it is fair and transparent and that the PPP Contract is balanced). It is crucial for the Contracting Authority to ensure that bidders’ offers are of a sufficient quality (e.g. by setting high minimum requirements). The Contracting Authority will also need to decide how to appropriately weight evaluation criteria between price, degree of risk transfer to the Private Partner and quality, according to its overarching aims for the PPP Project. In doing so, the Contracting Authority should bear in mind that its choices will have knock on effects on how the PPP Project affects and is perceived by the public and on its own reputation, even where the Private Partner is contractually responsible for delivering the relevant works and services – particularly in sectors which have traditionally been

4 See https://www.mof.go.jp/english/international_policy/convention/g20/annex6_1.pdf.

5 See *PPP Knowledge Lab: Tools to assess whether to implement a project as PPP*. This includes, for example, the PPP Fiscal Risks Assessment Model (PFRAM) developed by the International Monetary Fund and the World Bank in 2016, which is a tool aimed at assessing fiscal costs and risks associated with an envisioned PPP Project, and therefore designed to help governments to make informed decisions as to whether to procure a project as a PPP or not. *See link in Appendix A, Additional PPP Resources.*

6 See *Procuring Infrastructure Public-private Partnerships* 2018. *See link in Appendix A, Additional PPP Resources.*

expected to be public sector-delivered. Effective contract management by both Parties during the life of the PPP Project is an important means of ensuring delivery standards, together with appropriate expert advisory support, particularly where this may help stabilize delivery of the PPP Project in its early years.⁷⁸

UNDERSTANDING PPP CONTRACTS

Prior to reviewing the detailed analysis and contractual provisions provided in this Guidance, it is key for Contracting Authorities to first understand the overall context in which a PPP Project is being developed. This is because the circumstances of each individual PPP Project will shape and determine the drafting of its PPP Contract and related agreements.

To that end, set out below is a brief overview of why governments establish PPP programs, what a PPP involves, key aspects of risk allocation between the Parties and approaches to ensure “bankability”, as well as an overview of variations in approach that may be encountered in different legal systems, sectors and countries. It is important to take these factors into account in formulating and negotiating the terms of a PPP Contract.

Also included in this Guidance are links to more detailed sources of information on these areas, all of which will inform the Contracting Authority’s approach towards developing the specific terms of a PPP Contract for its particular PPP Project. See [Appendix A, Additional PPP Resources](#).

A. Overview of infrastructure development utilizing PPPs

PPP programs are being established by governments across the world as a means to deliver and maintain infrastructure, as well as to deliver other assets and services. Common themes encountered include:

- the need for the public sector to maximize the efficiency of building and maintaining infrastructure assets without negatively impacting on the quality of public sector services;
- the need to accelerate delivery of both greenfield and rehabilitation infrastructure and the expansion of brownfield infrastructure; and
- the ability to benefit from private sector expertise in delivering innovative technologies and services.

⁷ The World Bank is currently developing a PPP Contract Management Tool which is envisaged to be released by June 2020. See also the Global Infrastructure Hub’s PPP Contract Management Tool. [See link in Appendix A, Additional PPP Resources](#).

⁸ See also Benchmarking PPP Procurement 2017. See link in [Appendix A, Additional PPP Resources](#).

B. *What does a PPP involve?*

While there is no single, internationally accepted, definition of PPP, the essentials of a PPP arrangement which are encapsulated in a PPP Contract are:

- a long-term contract between a private party (the Private Partner) and a government entity (the Contracting Authority);
- for providing a new or existing public asset or service;
- under which the Private Partner bears significant risk and management responsibility; and
- where payments received by the Private Partner are linked to performance.⁹

The PPP Project functions transferred to the Private Partner – such as design, construction, financing, operation and maintenance – may vary from PPP Contract to PPP Contract¹⁰ but the inclusion of privately raised finance is key to ensuring that the Private Partner is financially exposed and therefore incentivized to perform.

C. *Finance structures for PPPs*

This Guidance primarily focuses on PPP transactions structured on a project finance basis, involving third party lenders through bank debt or bond finance. Other financing approaches are possible, as reflected by [Section 13, Corporate Financing](#).

The Private Partner in most project-financed PPP Contracts is a project company specifically formed for that purpose – often called a “special purpose company” or “special purpose vehicle” (abbreviated to “SPV”). The SPV commonly finances the cost of a PPP Project through a combination of equity – provided by its Shareholders – and third party debt provided by its Lenders (who may be commercial banks, bond investors or other finance providers). The choice of third party funder and the cost of such funds will be carefully considered by the Private Partner in its bid preparation.

Any PPP Project losses suffered by the Private Partner are borne first by its Shareholders, and Lenders are adversely affected only if the equity investment is lost. This means Equity Investors accept a higher risk than debt providers and require a higher return on their investment. As equity is typically more expensive than debt, the aim in reducing the overall weighted average cost of capital of a PPP Project is to use as high a proportion of debt as possible to finance the PPP Project (typically 70% to 95% of total project cost in Developed

⁹ See “PPP Contract” definition in [Defined Terms Section](#) and associated footnote.

¹⁰ In this Guidance, for example, a PPP Contract for a hospital may involve the Private Partner designing, building, financing and maintaining the hospital, but only providing certain operational services (such as cleaning, catering etc.) and not clinical services which may continue to be provided by the Contracting Authority. Other types of PPP Contract (e.g. the design, construction, management and financing of a university accommodation block or a tolled highway) may involve more comprehensive operational services.

Markets), which in turn should result in a lower priced asset and service for the Contracting Authority. The level of expected equity return will depend on the particular PPP Project's circumstances, but one of the advantages of a competitive bidding process is that bidders will be aiming to find a funding solution which delivers the best value for money for the Contracting Authority. Some jurisdictions may have laws regulating the establishment of SPVs and matters such as the level of permitted debt they are allowed to carry.

From the Equity Investors' perspective, limiting their exposure to a single PPP Project in this way makes it possible to undertake much larger (and potentially more) projects than would otherwise be the case. This contributes towards a larger pool of bidders and greater competition, to the benefit of Contracting Authorities.

PPP Project financings are typically structured as “non recourse” or “limited recourse” financings. In non recourse PPP Projects, Lenders can be paid only from the Private Partner's revenues, without recourse to the Equity Investors. In the context of limited recourse PPP Projects, Lenders rely primarily on the Private Partner's revenues to repay their loans but have certain additional limited recourse to the Equity Investors.¹¹

There have been examples of state/procuring entities taking equity stakes in project vehicles, for example, the Building Schools for the Future programme in the UK, the Non-Profit Distributing programme in Scotland and certain Belgian PPPs. In some jurisdictions (e.g. Poland), a PPP Contract may provide that, for the purpose of performing it, the Contracting Authority and the Private Partner will jointly form a limited liability company or a joint-stock company. Equity interests held by public and private sectors can serve to align incentives and promote cooperation at an operational level, while also giving the public sector a direct stake in the financial success of the PPP Project. However, it is important to design the framework to avoid conflicts of interest and to ensure that decisions necessary for the implementation of the PPP Project can be taken effectively and quickly and free from political influence. A public-private equity structure is therefore likely to be less suitable for PPP Projects in Emerging Markets, particularly where there is a less stable legal and political environment, as Equity Investors may feel the structure holds too much uncertainty for them.

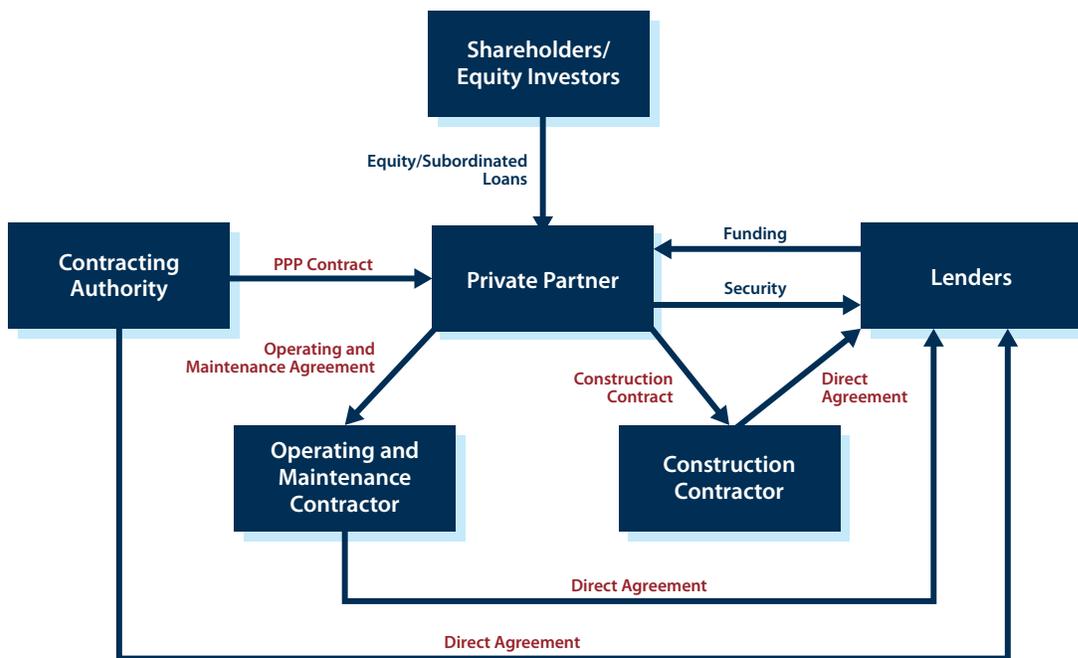
D. Structure diagram

This diagram shows the key parties and contracts involved in a typical PPP Project. The Contracting Authority contracts with the Private Partner through the PPP Contract and also enters into a separate “Direct Agreement” with the Lenders (*see Section 7, Lenders' Step-in Rights*). The Lenders provide funding to the Private Partner and take security over the Private Partner's assets for the repayment of such funding. The Lenders also enter into Direct Agreements with the Construction Contractor and Operating and Maintenance Contractor typically retained by the Private Partner to build and operate

¹¹ See *Section 13, Corporate Financing* for alternative mode of financing for a PPP Project and its implications for the considerations for Contracting Authorities as detailed in *Sections 1 to 11* of this Guidance.

the project as required under the PPP Contract. The Shareholders/Equity Investors own the Private Partner, providing funding to it by means of equity and shareholder loans (the repayment of which is subordinated to the Lenders' funding).

TYPICAL PPP STRUCTURE



The Contracting Authority will evaluate the technical and financial capabilities of the key parties in each bid (i.e. the Private Partner and its proposed key Sub-contractors and Equity Investors) as part of the procurement process. Where it is essential that the key parties it has contracted with remain in the PPP Project or where, for example, national law or procurement rules require the initial tenderers to remain involved, the Contracting Authority may want to place certain restrictions in the PPP Contract to prevent parties being replaced or changes in ownership occurring, at least for a certain period. Often, replacement and other changes in ownership will require approval by the Contracting Authority, to ensure that the Private Partner continues to have the expertise and financial strength which led to the Contracting Authority selecting that particular bidder for the PPP Project.

E. “Bankability” considerations for Contracting Authorities

Due to the high proportion of debt and the limited recourse available outside the PPP Project for debt repayment, third party Lenders undertake rigorous due diligence prior to funding, to assess whether a PPP Project is “bankable”. For a PPP Project to be bankable, Lenders need to be confident that the Private Partner can service the debt raised to carry out the PPP Project.

In practice, this means that the Private Partner’s operating cash flows need to be high enough to cover debt service plus an acceptable margin to cover the risk of variation to the cash flows. Lenders will therefore focus on the payment mechanic and any risks which could adversely affect the expected revenue stream. In doing so, they will assess the technical and financial viability of the PPP Project, taking into account all material project risks and how these are allocated between, and managed by, the parties. Lenders will also assess the ability of the Private Partner to convert payments received in local currency from the Contracting Authority or users into foreign currency where necessary to meet project costs or debt repayments denominated in that foreign currency. Non-convertibility of currency and exchange risk fluctuations can be key risks in some markets and potential obstacles to international investment if adequate mitigating measures are not agreed.

These matters are also key to Equity Investors who are looking to protect their investment and ensure the Private Partner will be able to generate high enough revenues not only to service debt but also to meet their expected equity return.

From the Contracting Authority’s perspective, the bankability of a PPP Project is key to whether or not it can succeed with its ambitions to procure infrastructure through PPP.¹² As risk allocation is so crucial to bankability, the Contracting Authority undertakes a difficult balancing act in structuring a PPP Project – ensuring it is bankable, while resisting pressure to accept more risk than is necessary or appropriate. [See Section F below](#). This is the key consideration underpinning the drafting and negotiation of PPP Contract provisions. Understanding the way long-term financing works and the internal credit approval processes lenders must satisfy in order to be able to lend to a PPP Project will help the Contracting Authority achieve this. The involvement of Lenders from an early stage of the procurement process, particularly while competitive tension between bidders exists, will enable the Contracting Authority to inform itself of, and take into account, project-specific bankability issues before final offers are submitted. The Guidance sets out the approach Lenders are used to seeing in relation to the contractual provisions addressed and the type of treatment which is likely to achieve credit approval.

¹² See footnote 5.

F. Risk Allocation

The underlying principle of a PPP arrangement is that the risks associated with carrying out a PPP Project are allocated to the Party best able to manage – or most incentivized to bear – them. This involves identifying which Party is best able to manage the likelihood that such risks will occur, as well as to manage the impact if they do actually occur. For example, a Private Partner who bears the risk of vandalism might opt for a design and materials that are more robust. In assessing the likely cost impact, the Parties will look at each other's ability to bear such cost and the related impact on price, as well as whether and how the cost impact could be offset or passed on (e.g. via insurance, increasing the price of the service to the end user (e.g. in a toll road) and/or by spreading the cost across tax payers).¹³ As mentioned in [Section E above](#), Lenders will be closely involved in this analysis and the procurement process should be designed so that Lenders' bankability issues are required to be reflected in bid proposals (potentially resulting in modification of the terms), so that these can be evaluated by the Contracting Authority during the competitive process and prior to signing the PPP Contract.

If risks are carefully assessed and transferred to the Party best able to control or mitigate them, this should result in a reduction of overall PPP Project cost and thereby improve value for money for the Contracting Authority. Contracting Authorities should therefore consider (only) retaining those risks that are not realistically capable of being accurately priced or properly assessed by a Private Partner and which the Contracting Authority is better placed to manage (e.g. practically or financially). By doing so, the Contracting Authority avoids having to pay the risk premium that will be charged by the Private Partner if it is required to assume such risks.

If risks are not allocated properly, the Contracting Authority may not be able to generate enough interest for the PPP Project, with the result that experienced bidders may not be willing to participate in the tender process, or may withdraw, if the draft PPP Contract is not amended to reflect an approach that is in line with market practice as well as sufficiently project-specific. This can lead to a failed tender process (where there are no or very few bidders) or to a flawed tender process with only inexperienced bidders or speculative bids.

Most importantly, the Parties should strive to achieve a balanced and reasonable risk allocation in the PPP arrangements that will provide an appropriate basis for a long-term partnership. This is key because in order to deliver value-for-money, most PPP Contracts need to run for a significant period of time, typically between 15 and 30 years. Because of their long-term and usually complex nature, PPP Contracts cannot specifically provide for the entire range of events that might potentially arise during their lifetime. All stakeholders in a PPP Project will need comfort that situations which are beyond their immediate control and which affect contractual performance will be dealt with in a way that allows them to arrive at a mutually acceptable solution. Key to this is each Party

¹³ For further insight into how and why risks are allocated to particular Parties, see the Global Infrastructure Hub's *PPP Risk Allocation Tool 2019 Edition*. [See link in Appendix A, Additional PPP Resources.](#)

acknowledging the imperative of keeping to the contractual bargain over the whole life of the PPP Contract and not undermining the carefully agreed risk allocation. Reducing uncertainty should also ensure greater value-for-money is achieved as uncertainty typically attracts a risk premium (i.e. the Private Partner will expect a higher price/return). As a result, PPP Contracts need to have flexibility built in to enable changing circumstances to be dealt with as far as possible within an agreed contractual framework.

As risk allocation is achieved primarily through the contractual structure, it is essential for Parties to understand not only how the PPP Contract works, but also its relationship with related agreements. These include the Project Agreements and any other documents to which the Contracting Authority is Party (such as the Lenders' Direct Agreement – see [Section 7, Lenders' Step-in Rights](#)) or which affect its obligations and liabilities – such as the Private Partner's debt and equity finance documents and its financial model (also known as Original Base Case). The PPP Contract should require the Private Partner to make the Contracting Authority aware of, and obtain its consent to, any material changes to such agreements. Failure to obtain consent to changes to the debt and equity finance documents or financial model, for example, should, amongst other things, mean that any unapproved changes will not be taken into account in assessing the Contracting Authority's liability for termination compensation by reference to such documents. As regards the PPP Contract itself, the interplay between its contractual provisions is so carefully balanced that they cannot be considered in isolation of each other – the PPP Contract must be looked at in its entirety, in addition to in relation to other Project Agreements and applicable law.

It is important to note that risk allocation is influenced by various factors, including the maturity of the market, the experience of the participants and the level of competition between bidders. Emerging Market governments and Contracting Authorities may therefore be able to transfer more risk to Private Partners once they establish successful track records in national/sectoral PPP markets, as these markets become increasingly attractive to Equity Investors and Lenders, and therefore more competitive. A consistent approach to risk allocation across successive projects within a sector (and, depending on the risk, a jurisdiction) can contribute substantially to establishing this initial track record.

G. Alternative PPP payment mechanisms and risk allocation

As mentioned in [Section E above](#), the payment mechanism and how payments under it may be affected is key to bankability. The model adopted may also influence how certain risks are agreed by the Parties to be managed. There are three main ways the Private Partner can be paid – by collecting fees from service users, by being paid by the Contracting Authority, or by a combination of the two. The common defining characteristic between these approaches is that payment is contingent on performance.

“User pays” model – In PPP Projects using this payment mechanism, the Private Partner provides a service to users and generates revenue by charging users for that service (e.g. some toll roads). These fees (or tariffs or tolls) can be supplemented by subsidies paid by

the Contracting Authority, which may be performance-based (for example, conditional on the availability of the service at a particular quality standard), or output-based (for example, payments per user).¹⁴ Under this approach, the Private Partner and its Lenders bear the “demand risk” associated with the PPP Project; namely, how many users will pay to use the asset. There may also be some scope for the Parties to agree that costs associated with the occurrence of certain risks may be managed by increasing the user fee commensurately and/or extending the term of the PPP Contract.

“Government pays” model – In PPP Projects using this payment mechanism, the Contracting Authority is the sole source of revenue for the Private Partner. This is more usual in PPP Projects where the Private Partner has no influence over user demand (e.g. in the case of a hospital or prison) or where user demand will be too low or uncertain to generate sufficient revenue for the PPP Project to be bankable. There may also be public law constraints or political obstacles with regard to “user pays” projects (for example, in some countries charging tolls for the use of public roads may require changes to the constitution; in other countries there may be restrictions on charging patients for essential health services or minors for education). Contracting Authority payments are usually conditional on the asset or service being available at a contractually-defined quality regardless of the level of use, and are often termed “availability payments”. In this approach, the Private Partner and its Lenders are exposed to the Contracting Authority’s credit risk and will assess it carefully.¹⁵

H. Accounting treatment considerations

An additional factor for governments procuring PPP Contracts has been the availability of advantageous accounting treatment, in particular the perceived ability to treat such investments as “off balance sheet”. However, this has attracted increasing scrutiny from accounting bodies around the globe due to a concern that governments may use PPPs to bypass spending controls (by taking public investment out of the budget and debt off the balance sheet), although they are still bearing substantial risk and significant contingent liabilities under PPP Contracts¹⁶. This has resulted in bodies such as Eurostat, the International Monetary Fund and national accounting boards (e.g. in Australia) embarking on measures focusing on the overall risk/reward balance under PPP Contracts for the purposes of determining whether they should be classified as on or off government balance sheets.

In the EU, for example, Eurostat¹⁷ currently requires EU governments to follow certain accounting rules for the debt and deficit treatment of PPP Projects (ESA2010). These

¹⁴ In some jurisdictions, fees (or tariffs or tolls) under a “user pays” model may also be supplemented by a minimum revenue guarantee provided by the Contracting Authority to make the project commercially viable and bankable.

¹⁵ See [Section L, PPP Contracts in Context and Section 3.2.1.1](#) for further discussion of pricing adjustments and constraints.

¹⁶ As mentioned above, it is therefore crucial for a Contracting Authority to assess the fiscal costs and risks associated with an envisioned project before deciding whether to procure it as a PPP or not. See [PPP as chosen procurement method, PPP Contracts in Context](#).

¹⁷ See [links in Appendix A, Additional PPP Resources](#).

focus on how construction risk, availability risk and demand risk are allocated between the Contracting Authority and the Private Partner to determine the accounting treatment that must be applied. Under these rules (which themselves have given rise to some debate), “user pays” PPP Contracts are by default off balance sheet due to the risk/reward balance, whereas “government pays” PPP Contracts may not be, depending on the risk allocation. While accounting treatment is not a factor which should drive negotiating approach, it is something Contracting Authorities should be aware of and should be taken into account when choosing the appropriate procurement model for the project. See [PPP as chosen procurement method](#) above.

I. Country and sector-specific differences

As the above highlights, the PPP model is becoming an increasingly global contracting approach for governments. It is important to remember, however, that PPP Project risks vary depending on the country where the PPP Project is located, the nature of the PPP Project and the assets and services involved.

A road PPP Project, for example, is very different from a hospital PPP Project – which in turn has some very different features to an airport PPP Project. Similarly, a defense PPP Project is likely to involve issues of national security which do not affect other sectors in the same way. The key is to understand where these differences lie and to apply the same principle of allocating each risk to the Party best able to manage it consistently with a view to maximising the value received by the Contracting Authority (measured by overall cost as well as quality of service provided by the PPP Project).

Many resources provide “standard” risk matrices and sample risk allocations, in some cases for specific project types. These can be useful when identifying project risks for a particular PPP Project. However, PPP Projects usually have unique features or circumstances – for example, the particular geological conditions on the route of a proposed road. Moreover, the typical risk allocation position in a Developed Market in an established jurisdiction may not be appropriate in an Emerging Market. This means that Contracting Authorities should ensure that experienced advisers identify a comprehensive list of project risks and analyze carefully how such risks should be allocated in the context of each individual PPP Project.¹⁸

J. PPP Contracts in different legal systems

Common law and civil law are the two main types of legal system adopted by countries nowadays and some countries have adopted features from both into their legal systems. While the approach to allocating risk under a PPP Contract should be fundamentally the same in both civil law and common law jurisdictions, how such risk

¹⁸ For sector-specific risk matrices, see the Global Infrastructure Hub’s: PPP Risk Allocation Tool 2019 Edition. [See link in Appendix A, Additional PPP Resources.](#)

allocation is drafted and the extent to which it is negotiable may differ according to the level of freedom the Parties have to enter into bespoke contractual arrangements.

An overarching consideration in relation to freedom to negotiate under both systems is whether the applicable procurement processes and rules limit the ability of the Parties to negotiate and amend the terms of a PPP Contract issued as part of a tender process, and whether any changes might give rise to procurement challenges or allegations of corruption. The Contracting Authority should take this into account when formulating the terms of the PPP Contract which will form part of its tender documentation to ensure it retains the flexibility it is likely to require over such a long term and avoid tendering an unnegotiable, unbankable, PPP Contract.

Aside from potential procurement law restrictions, underlying general laws may affect or apply to PPP contractual relationships without express inclusion in the relevant PPP Contract. In jurisdictions where this is the case, the Parties will need to verify whether and to what extent it is legally possible to amend or waive rights and obligations under such laws (taking into account how this may also affect third parties, such as users). Depending on the result of such analysis, the Parties may want to expressly spell out the underlying legal position in the PPP Contract for the sake of certainty. How such issues are addressed will depend entirely on the jurisdiction and Parties concerned and professional legal advice must be sought. Lenders will be equally concerned with this aspect.

Common Law System – In a common law system, parties typically enjoy extensive freedom of contract and few provisions are implied into a contract by law. Judicial decisions set precedents which will be followed in the determination of contractual disputes and therefore influence contractual drafting. A consequence of this freedom is that the terms of any contractual arrangements should be expressly set out in the relevant contract. In a PPP context, all arrangements governing the relationship between the Parties therefore need to be expressly set out in the PPP Contract itself.

Generally speaking, everything is permitted that is not expressly prohibited by law or by contract. If a government is embarking on a PPP program, it should ensure that certain protections are enshrined in applicable legislation and/or built into PPP Contracts for public policy reasons. For example, it may wish to expressly prohibit the service provider from cutting off the water or electricity supply of delinquent payers, or limit the toll or tariff a Private Partner can charge users, to reflect governmental obligations under relevant international treaties. It may also wish to expressly require that certain documents related to the transaction be disclosed under freedom of information legislation.

Civil Law System – A civil law system is a codified system of law which is generally more prescriptive than a common law system. Basic rights and duties are enshrined in an overarching constitution under which specific legal codes are promulgated (such as administrative and commercial legal codes). In addition, in many civil law jurisdictions, underlying principles of good governance and other administrative law rules affect public sector parties, and broad obligations such as “good faith” have an

important impact on contract performance. Broadly speaking, legislative enactments are considered binding for all, as opposed to judicial decisions as in common law jurisdictions (although case law may be relevant, for example with regard to financial hardship concepts and Force Majeure). Codified provisions and underlying principles may be implied into civil law contracts without being expressly included. As a result, less importance is generally placed on expressly setting out all the terms governing contractual Parties' relationships in the PPP Contract itself, partially because gaps or ambiguities can be remedied or resolved by operation of law. Accordingly, a civil law contract is often less detailed than an equivalent common law contract.

As in any jurisdiction, it is key for all Parties to understand how the underlying civil law operates and how it potentially affects the Parties' risk allocation negotiations. PPP Contracts typically fall under the administrative law umbrella and the Parties will have to take into account underlying administrative law principles which apply to contractual relationships (e.g. in the context of Force Majeure rights or rights of the Contracting Authority to voluntarily terminate a contract or rights to "economic rebalancing" or compensation for a Private Partner suffering financial hardship as a result of certain changes in circumstance).

Changing or overriding an administrative law principle by contract may or may not be legally possible and this will need to be confirmed on a case-by-case basis. Some civil law jurisdictions enjoy extensive freedom to contract (e.g. the Netherlands). However, in other jurisdictions (e.g. Poland), it may not be possible to derogate from certain principles or to completely waive certain rights, so the Parties will need to take this into account in their negotiations. A related issue for the Parties is what to include in the PPP Contract if underlying legal principles apply. Generally speaking, there is an increasing preference in civil law jurisdictions (e.g. Poland) to expressly set out the position so that the PPP Contract is clear on its face and is not relying on implied terms from underlying law. This is partly because this approach will be more familiar to Parties from common law jurisdictions, but also because relying on underlying law may create more interpretation risk and it is in the interest of all Parties to minimize the risk of different interpretations and ambiguity. An alternative, which may also be effective, is to refer to the underlying law (instead of copying it into the contract) and to set out expressly in the PPP Contract how the underlying principle or law is to be applied. It is advisable to include an express statement in the PPP Contract as to whether or not relevant provisions intend to derogate from applicable underlying law, and if so, to what extent.

Islamic law – In some countries with increasingly active PPP programs, Islamic law (shariah) provides the substance of the legal system. These jurisdictions can be organized as common law or (more often) civil law systems. In these countries, no legal instrument – whether legislation, regulation, court ruling or private or public contract – may contravene Islamic principles. The 2017 World Bank Group and Islamic Development Bank Report "Mobilizing Islamic Finance for Infrastructure Public-Private Partnerships"¹⁹ sets out how

¹⁹ See the Joint 2017 World Bank Group and Islamic Development Bank Report "Mobilizing Islamic Finance for Infrastructure Public-Private Partnerships". The report has two objectives: the first is to enhance the understanding of Islamic finance building blocks as they relate to financing infrastructure PPP Projects, and the second, and perhaps less well understood, is to explore how the building blocks of Islamic finance can fit within a PPP context. An updated edition of the report will be released later during 2019. [See link in Appendix A, Additional PPP Resources.](#)

Islamic finance may be applied to infrastructure and PPP Projects. This means that projects in these jurisdictions must be structured in such a way that they do not violate Islamic law's prohibitions against *riba* (interest) and *gharar* (uncertainty). This can be done by using well-established Islamic financing techniques (such as procurement-leasing (*istisnā-ijara*) and cost-plus financing (*murabaha*)). These structures, while compliant with the *shariah*, achieve the same commercial outcomes as their conventional counterparts.

K. Foundations for a successful PPP Contract

As highlighted in *Procuring Infrastructure Public-Private Partnerships 2018*²⁰, the regulatory environment is key to successful PPP procurement. The existence of a legal and administrative regime which permits PPP and provides for a clear and transparent procurement process is essential. Without this, the Contracting Authority may waste time and other resources as suitable private sector Parties are unlikely to invest time and resources (both financial and personnel) in participating in a PPP Project procurement process which may be lengthy and ultimately fail. Before any procurement process begins, governments in both civil and common law jurisdictions need to consider what additional legislation may be required in order to facilitate and permit PPP arrangements – this will include ensuring Contracting Authorities have the legal capacity and authority to enter into PPP Contracts (i.e. that they will not be acting “*ultra vires*” – beyond their powers) and that PPP arrangements in their desired form are legally permitted. Governments will also need to consider whether specific legislation is required to facilitate PPP Projects in a particular sector or (particularly in the case of civil law jurisdictions) is needed to limit the scope of an underlying law restriction which may be preventing or impeding the successful procurement of a PPP Project. This includes assessing any implications as regards potential financing, tax and security arrangements.²¹

In addition, the Contracting Authority should consider whether existing legislation places sufficient environmental, social and other important legal obligations on the Private Partner to adhere to standards to which the government and other public authorities are subject (or would be if the project were not procured by PPP or another procurement method involving the private sector). As with privatization and other mechanisms whereby the private sector takes on tasks previously carried out by the public sector, the standards and obligations applicable to the public sector do not always apply automatically to the private sector. In preparing for PPP, the Contracting Authority will need to investigate whether extra legislative action is required and/or whether specific contractual obligations need to be imposed to address any gaps identified.

A stable political, economic and legal regime and environment is also desirable. While certain associated risks can be managed under the PPP Contract, ultimately the risk of investing in and lending to a PPP Project where these conditions do not exist may

²⁰ See link in Appendix A, Additional PPP Resources.

²¹ For an overview of, as well as specifics on, PPP legal frameworks, see the PPP Reference Guide Version 3.0, dated April 2017. See link in Appendix A, Additional PPP Resources.

be too high for some private Parties, particularly when compared with alternative investment or lending opportunities. Jurisdictions without a clear legal framework and solid institutional basis are likely to be more susceptible to inefficient and corrupt procurement which not only stalls the completion of infrastructure projects but also lowers the quality of infrastructure.²² The involvement of export credit agencies and multilateral and development finance institutions can give Equity Investors and Lenders greater confidence in certain jurisdictions. This is due not only to their ability to offer more favorable financing terms or products such as political risk insurance in respect of commercial loans and equity, but also because of the relationship dynamics at government level. Similarly, the existence of bilateral investment treaties between governments may play a part in the private sector's decision to invest in some jurisdictions. These elements are additional factors in the negotiation of a well-balanced PPP Contract in such jurisdictions, but are not a substitute for a PPP Contract.

L. Environmental and social impact

As recognized by the G20 through its Principles for Quality Infrastructure²³, addressing social and environmental issues in any infrastructure project is key. This includes the protection of human rights, a consideration increasingly identified as important also within commercial contracts, supported by the development of international standards and in some cases domestic legal reforms. In particular, the United Nations Guiding Principles on Business and Human Rights (2011)²⁴ set out the responsibilities of business enterprises to (a) avoid causing or contributing to adverse human rights impacts through their own activities and address such impacts when they occur; and (b) seek also to prevent or mitigate adverse human rights impacts that are directly linked to their operations, products or services by their business relationships, even if they have not directly contributed to those impacts themselves. In terms of PPP, this should be reflected in measures to identify, avoid and/or mitigate potential adverse impacts on human rights and the inclusion of corresponding contractual provisions.

PPP Projects often involve new construction, the use of resources, and structural changes, all of which can impose considerable environmental and social impacts and costs. These risks differ between PPP Projects, depending on the type of project and its circumstances. There may be a risk of damage to the environment and/or local communities due to the construction and operation of the PPP Project and its location, or due to existing latent environmental conditions. The Contracting Authority should assess social and environmental impact during project preparation and in particular as part of its feasibility studies before the PPP Project is procured, so that particular risks as well as opportunities to tackle social and environmental issues can be specifically identified and taken into account in the tender requirements, output specification and PPP

22 Procuring Infrastructure Public-Private Partnerships 2018. [See link in Appendix A, Additional PPP Resources.](#)

23 See https://www.mof.go.jp/english/international_policy/convention/g20/annex6_1.pdf.

24 See https://www.ohchr.org/Documents/Publications/GuidingPrinciplesBusinessHR_EN.pdf.

Contract when the project is designed and tendered. The outcomes of environmental and social impact assessments are also crucial to ensure that any identified risks and their mitigation are adequately captured in the PPP Contract and also in order to ensure compliance with any relevant laws and treaties. As mentioned above in *PPP as chosen procurement method*, this is important for the Contracting Authority as its control over the environmental and social impact of the project during the life of the PPP Contract, and how the Private Partner mitigates or addresses such impact, will depend primarily on the contractual terms. The Contracting Authority should bear in mind that it will bear the consequences and the knock-on costs of such impact to the extent these are not the Private Partner's responsibility under the PPP Contract, while having less flexibility to implement mitigative measures than if it had chosen a more traditional procurement method where it retained operational control.

Treatment of environmental and social risks will form part of the due diligence process by the Private Partner and its Lenders and be specifically reflected in the underlying risk allocation in the PPP Contract²⁵ and by requirements on the Private Partner in the relevant financing documents. In this regard, it should be noted that all parties, including Lenders, export credit agencies and multilateral agencies, will as a rule be concerned to ensure that these aspects are dealt with appropriately. Many finance parties adhere to the "Equator Principles"²⁶ (which incorporate the IFC Performance Standards²⁷ as the relevant standards that apply to certain projects) and may have other internal policy requirements relating to social/environmental standards. In addition to any legal or contractual obligations, there are also wider reputational issues for the private sector parties involved (be they local or foreign investors or Lenders) who will not want to be perceived to be overlooking issues such as social and environmental considerations. In many cases, corporates as well as Lenders will also have internal requirements that need to be satisfied on these fronts.

Infrastructure projects can also bring certain benefits to the local economy and have a positive social and environmental impact which can help mitigate adverse effects, both during implementation and once the new asset is built and in operation. These benefits can include the delivery of new infrastructure to replace old or non-existent assets (such as roads and hospitals local people will benefit from); the delivery of vital infrastructure which might otherwise be unaffordable to build for many years, with the consequent advantage to the wider economy and public benefit; and the positive impact on local employment, business and innovation through the involvement of local companies and people during both the implementation and delivery phases. The PPP process gives both Parties an opportunity to find innovative solutions to important sustainability issues, both through the design of the project and its implementation.

25 For specific examples of risk allocation, see the Global Infrastructure Hub's PPP Risk Allocation Tool 2019 Edition, e.g. the Environmental and Social risk entries in its risk matrices. [See link in Appendix A, Additional PPP Resources.](#)

26 The Equator Principles are a risk management framework, adopted by financial institutions, for determining, assessing and managing environmental and social risk in development projects. [See link in Appendix A, Additional PPP Resources.](#)

27 [See link in Appendix A, Additional PPP Resources.](#)

Some PPP Contracts have provisions relating to energy savings/carbon reduction which affect the payment the Private Partner receives or implement a sharing mechanism for any savings to incentivize the Private Partner. For example, in a road project, the choice of materials may affect how much light – and therefore energy – is needed by the project or in a school project, the availability metrics may require the internal room temperatures to be within a range. One way the Contracting Authority can avoid potential adverse social impact related to tariffs and tolls etc. in a “user pays” PPP Project such as a toll road or an electricity project, for example, is by ensuring the Private Partner is restricted from certain tariff or toll increases where these would be commercially viable but would lead to discriminatory results.²⁸ These are some examples and ways in which PPP Contracts can be used to promote innovative and environmentally-friendly solutions.

Further studies and resources are available as set out in the footnotes²⁹.

M. Climate change

The increased risk and uncertainty of the impact of climate change presents challenges in ensuring the sustainability of PPP Projects. This is particularly the case for projects in areas especially vulnerable to extreme weather events or other changes to the habitat (for example, rising sea levels). As PPP Contracts are long term by nature, Contracting Authorities need to consider how their PPP Project might be affected by climate risks and how this should be addressed. This may have two aspects: a) climate change risk events affecting performance of the project (e.g. by flooding of a project facility, extreme temperatures melting rail lines or roads, landslides interrupting supply routes, or droughts affecting water supply) or b) climate change affecting the need or demand for the project service (e.g. by increased temperatures requiring more electricity to power air conditioning or requiring an increased water supply). Contracting Authorities face the challenge of how to balance financing infrastructure to meet near term needs, as well as factoring in the effect of the project on the environment (*see Section L*), mitigation of any associated contributory effect on climate change as well as measures to ensure the infrastructure will be resilient if natural disasters or other climate change-related risks occur – which may add in significant additional, and potentially unnecessary, cost.

²⁸ Tariff or toll increases may, for example, be discriminatory under international agreements to which the Contracting Authority/government is Party (e.g. International Covenant on Economic, Social and Cultural Rights, Convention on the Elimination of Discrimination Against Women, and the Convention on the Rights of the Child). The Contracting Authority itself also needs to be aware of such potential socio-political constraints when drafting and negotiating the PPP Contract so that any agreement permitting an increase in toll or tariff as a means of compensating for increased costs is consistent with its obligations under such international agreements. *See also Section 1.2.3.6.*

²⁹ See PPPLRC: Gender & PPPs: <https://ppp.worldbank.org/public-private-partnership/ppp-sector/gender-impacts-ppps/impacts-ppps-gender-inclusion>; Pro-Poor PPPs: <https://ppp.worldbank.org/public-private-partnership/ppps-poor>; and Gender Equality, Infrastructure and PPPs – A Primer, WBG 2019: <https://library.pppknowledge.org/documents/5720>], Environment: see <http://www.worldbank.org/en/topic/environment>.

As with all aspects of a PPP Contract, Contracting Authorities need to consider climate change issues from an early stage and assess how such risks should be addressed and mitigated over the whole project cycle. As a first stage, project feasibility studies should assess the likelihood of the impact of climate change on the project and the impact of the project on climate change and this should inform the tender requirements specified by the Contracting Authority, as well as the terms of the PPP Contract. The World Bank has developed climate and disaster risk screening tools³⁰ which can help Contracting Authorities identify and assess risks and there is other related policy, financial and technical support available to governments from multilateral agencies and other sources³¹. Retrofitting infrastructure for the consequences of climate change is likely to be more expensive than building it with designed-in resilience and mitigative measures in the first place³², so as far as possible the Contracting Authority should aim to specify requirements which factor in resilience and mitigative measures and incentivized the Private Partner to design and build the relevant asset accordingly. Setting such resilience requirements will be easier where there is historical data and past experience to rely on in terms of natural disaster events (such as heavy rain data in Japan³³). As regards mitigation of the project's own impact on climate change, the Contracting Authority may specify or invite proposals as regards energy and fuel sources (such as requiring renewable energy for captive power supplies or implementation of battery solutions). In setting procurement requirements and evaluating bids, Contracting Authorities need to take into account that higher initial costs which take account of disaster resilience and climate change mitigation will greatly benefit the sustainability of the project and help reduce costs in the long-run. Evaluation criteria weighting should ideally reflect this in a meaningful way so that the Contracting Authority does not evaluate solely on price. Another approach is for Contracting Authorities to identify relevant potential climate-related events or impacts in tender documents and require bidders to propose solutions to address the risk of their occurrence.

Related to design requirements is the allocation of responsibility for managing the effects of climate risks if they occur. This is because the Private Partner will want to take into account necessary disaster recovery management measures or appropriate contingency measures when bidding its contract price and the cost of such measure will in part depend on the design of the project asset and the materials chosen to build it. While Force Majeure provisions typically address extreme weather conditions and provide for the parties to share the risk of their occurrence, a more nuanced approach to specific risks can allocate an increased level of risk to the Private Partner in

30 See <https://climatescreeningtools.worldbank.org/> and Climate-Smart PPPs: <https://ppp.worldbank.org/public-private-partnership/climate-smart/climate-smart-ppps>.

31 See Climate change and natural disasters: <https://pppknowledgelab.org/guide/sections/15-climate-change-and-natural-disasters>.

32 See Climate risks and resilience in Infrastructure PPPs: Issues to be considered: https://ppiaf.org/documents/2870?ref_site=ppiaf.

33 World Bank. 2017. "Resilient Infrastructure Public Private Partnerships (PPPs): Contract and Procurement – The Case of Japan"

appropriate cases and at the same time provide other benefits. In Japan, for instance, experience from previous natural disasters has informed how Force Majeure is defined in subsequent PPP Projects. For example, earthquakes may qualify as Force Majeure depending on their seismic intensity, or (as in a toll road project) additional costs of Force Majeure may only be borne by the government if resulting from heavy rains over a certain threshold per hour or 24 hour period or from certain wind speeds (and if the disaster recovery project is in accordance with certain national legislation). Experience in Japan has also indicated that private sector responsibility for certain events may have facilitated a faster and more efficient response time than if the public sector were solely responsible³⁴. This may be because the private sector has to consider disaster response in the planning stage and is also obliged to respond in an emergency. Payment incentives can also encourage the Private Partner to respond effectively following a disaster – for example, maintaining or swiftly restoring a service can lead to reduced payment deductions (either by virtue of the normal payment mechanism or through additional incentivization measures).

To ensure that satisfactory measures are in place to meet design requirements and disaster recovery obligations, the Contracting Authority can require certain rights of inspection and place the Private Partner under reporting obligations. Deductions from payments where measures are below specification is also a way to incentivize the Private Partner to meet its obligations fully and Lenders will also be keen to ensure that the Private Partner has satisfactory measures in place to meet its contractual obligations.

Insurance also plays a key part in managing climate change risks. In considering the extent to which the Private Partner should be responsible for such risks, the Contracting Authority should take into account the availability of insurance for such climate change events and the cost of such insurance. Requiring the Private Partner to place relevant insurances, if available, may add cost into the contract price but may be better value for money for the Contracting Authority than bearing the risk itself. It also effectively means that costs resulting from the occurrence of the insured event will not be eligible for compensation under the Force Majeure provisions if they were required to be insured³⁵. The cost of insurance premiums will also help drive the Private Partner's behaviour in building in resilience to the insured asset and/or ensuring it is well-maintained. The Contracting Authority's approach to setting insurance requirements and evaluating bids is important in this regard, however, to avoid Private Partners negotiating lower insurance premiums in order to lower costs, which could leave the PPP Project with lower levels of insurance in the event of a climate change-related event. Insurance for certain natural disaster events may become increasingly hard or costly to obtain as insurance markets respond to the increasing occurrence of such events – particularly in certain

34 Resilient Infrastructure Public Private Partnerships (PPPs): Contract and Procurement – The Case of Japan, Washington, DC

35 This is the case in Chile where catastrophic risks are required by PPP law to be covered by insurance which has led to the private sector bearing most of the cost of certain earthquakes, for example: <https://pppknowledgelab.org/guide/sections/15-climate-change-and-natural-disasters>.

regions or sectors – and some domestic insurance markets may simply not have capacity to insure certain events. In this regard, Contracting Authorities could seek to encourage governments to look to support the development of insurance and reinsurance markets, while taking into account the likely need to assume some risk for natural disasters.

The Contracting Authority may want to consider contractual rights to require certain changes to be implemented after contract signature to address climate change risks. Most PPP Contracts contain provisions by which the Contracting Authority can require variations if it pays for them and these may be sufficient to address climate change measures. While it must be recognized that imposing costs on the Private Partner as a result of later requirements is unlikely to be bankable where the Private Partner has no means of absorbing the cost, the Contracting Authority should consider whether a more developed forum for discussing climate change specific variations is appropriate (such as bespoke change management mechanisms that apply if a climate change event (or pattern of events) occurs – for example, abnormally high temperature over several years. This could, for example, involve incentive measures for the Private Partner. The Contracting Authority should, however, also bear in mind that adapting a PPP Contract is almost invariably more costly than building in capacity and flexibility at contract signature, so as mentioned above it is vital for it to tackle these issues at the procurement stage as far as possible. Similar issues arise in relation to changes in law to tackle climate change and whether it is appropriate for the Private Partner to bear the cost of such changes. This is likely to depend on the nature of the change (i.e. whether it specifically affects the project rather than other businesses or is more general such as requiring all businesses to use electric cars).

Ensuring resilience and disaster recovery management is likely to become increasingly important in PPP Projects and the approaches adopted can contribute to wider climate adaptation and resilience and mitigation strategies. At an individual project level, if feasibility studies indicate that climate change risks are likely to require a costly and uncertain process of adaptation and mitigation over time (such as evolving specifications, maintenance standards or preventative measures), then the Contracting Authority should consider whether PPP is the best procurement method for the project in question.

The World Bank’s Global Infrastructure Facility (GIF) and the Tokyo Disaster Risk Management (DRM) Hub have initiated the “Resilient Infrastructure PPPs – Contracts and Procurement” project to support a developing body of global knowledge on infrastructure PPP in relation to disaster and climate resilience. This includes country reports³⁶ on how sustainability issues are being addressed in PPP Projects (in particular climate change events and disaster response management), where further measures can usefully be taken and what lessons can be drawn.

Further studies and resources are available as set out in the footnotes³⁷.

³⁶ Resilient Infrastructure Public Private Partnerships (PPPs): Contract and Procurement – The Case of Japan, Washington, DC

³⁷ See pages on Climate Smart PPPs on the PPPLRC

N. Sustainable Development

Investment in quality infrastructure is crucial to achieving sustainable development and empowering communities around the world³⁸ as demonstrated by the G20's Principles for Quality Infrastructure³⁹. Under the aegis of these principles and the United Nations' Sustainable Development Goals⁴⁰, the development agenda⁴¹ offers an opportunity to think more broadly about the role of PPPs in increasing investment in quality infrastructure. One of the targets of the Sustainable Development Goals is to “encourage and promote effective public, public-private and civil society partnerships, building on the experience and resourcing strategies of partnerships.”⁴² The challenge for Contracting Authorities procuring long term PPP Contracts is to fulfil near term infrastructure needs without compromising longer term sustainability needs and the ability of future generations to meet future needs. As highlighted in [Section M](#), this is particularly difficult with increasing unpredictability in respect of certain factors affecting sustainability, such as climate change.

When planning a PPP Project, Contracting Authorities (and governments generally) should ideally have a clear understanding from a holistic perspective how individual PPP Projects fit into the country's overall sustainability plan so that essential services can continue to be delivered to meet growing needs, as well as tackle challenges such as climate change. In tandem with understanding demographic and socio-economic forecasts, governments need an overarching plan to ensure that communities are able to develop in a way which will support future needs, promotes inclusivity and poverty reduction and provides employment and skills development opportunities across sections of society which might otherwise be overlooked.

In addition to the sustainability considerations in relation to environmental/social impact and climate change flagged in [Section L](#) and [Section M](#), at individual PPP Project level, the Contracting Authority should consider other social sustainability measures, for example, targeted at reducing wealth, gender or other social polarization. Where appropriate for the particular PPP Project, the Contracting Authority could, for example, consider setting project tender requirements that a certain proportion of employees have to be young/untrained/female/from particular ethnic groups, and this could tie in with government incentives providing subsidies or tax breaks for businesses satisfying such criteria. Another approach could be to require the Private Partner to provide certain specialized training or employment for local people (varying from specific construction and engineering skills through to supporting roles, such as preparing packed lunches for workers). These measures can help increase local employability and

38 Procuring Infrastructure Public-private Partnerships 2018. [See link in Appendix A, Additional PPP Resources.](#)

39 https://www.mof.go.jp/english/international_policy/convention/g20/annex6_1.pdf.

40 United Nations, Sustainable Development Goals: <https://www.un.org/sustainabledevelopment/sustainable-development-goals/>.

41 <https://sustainabledevelopment.un.org/content/documents/21252030%20Agenda%20for%20Sustainable%20Development%20web.pdf>.

42 [See https://sustainabledevelopment.un.org/sdg17](https://sustainabledevelopment.un.org/sdg17).

engagement and create opportunities for local people to become part of the project’s own supply chain or for additional revenue streams to be created which benefit the wider community. The appropriateness of such measures will depend on the particular PPP Project and will need to be considered on a case-by-case basis.

Various initiatives have been launched by international bodies, such as UNECE, the Global Infrastructure Hub (GIH) and the World Bank Group⁴³, which highlight some of these issues and how these might be approached in PPP Projects. For example, the GIH has developed a tool to address inclusivity and social equity in the planning, design and implementation of major infrastructure projects⁴⁴ and the UNECE International Centre of PPP Excellence⁴⁵ focuses on People-first PPPs and has published papers on “Draft Guiding Principles on People-first Public-Private Partnerships (PPPs) for the UN Sustainable Development Goals (SDGs)”⁴⁶ and “Women’s empowerment in PPPs”⁴⁷.

Where applicable, these considerations will be highlighted in the relevant sections of this Guidance.

Further information on sustainability issues in a PPP context can be found in the sources footnoted and also in the links in [Appendix A](#).

O. Conclusion: the importance of a project-specific approach

As highlighted at the outset, understanding the whole context of a PPP Project is critical for Contracting Authorities when devising and negotiating the terms of a PPP Contract. Risk allocation has a direct impact on bankability and pricing, which determines whether a PPP Project will be affordable for a Contracting Authority or users and financeable by a Private Partner – and ultimately whether the asset and/or service will be provided at all by means of a PPP. There is no “one size fits all” PPP Contract and contractual provisions cannot be looked at in isolation due to their close interplay.

This Guidance is intended to help Contracting Authorities carefully assess the issues specific to their own PPP Project and jurisdiction in developing PPP contractual provisions. It explains the rationale for the drafting of certain material provisions that have formed the basis of many successfully procured PPP transactions around the globe and which have been developed through detailed risk allocation assessment and

43 See <https://ppp.worldbank.org/public-private-partnership/public-private-partnerships-by-topic>.

44 See <https://www.gihub.org/resources/publications/reference-tool-on-inclusive-infrastructure-and-social-equity/>.

45 See <https://www.uneceppp-icoe.org/people-first-ppps/>. The mission statement is “To strengthen the impact of PPPs by putting people first in projects, eradicating poverty, supporting vulnerable members of society and protecting the planet”.

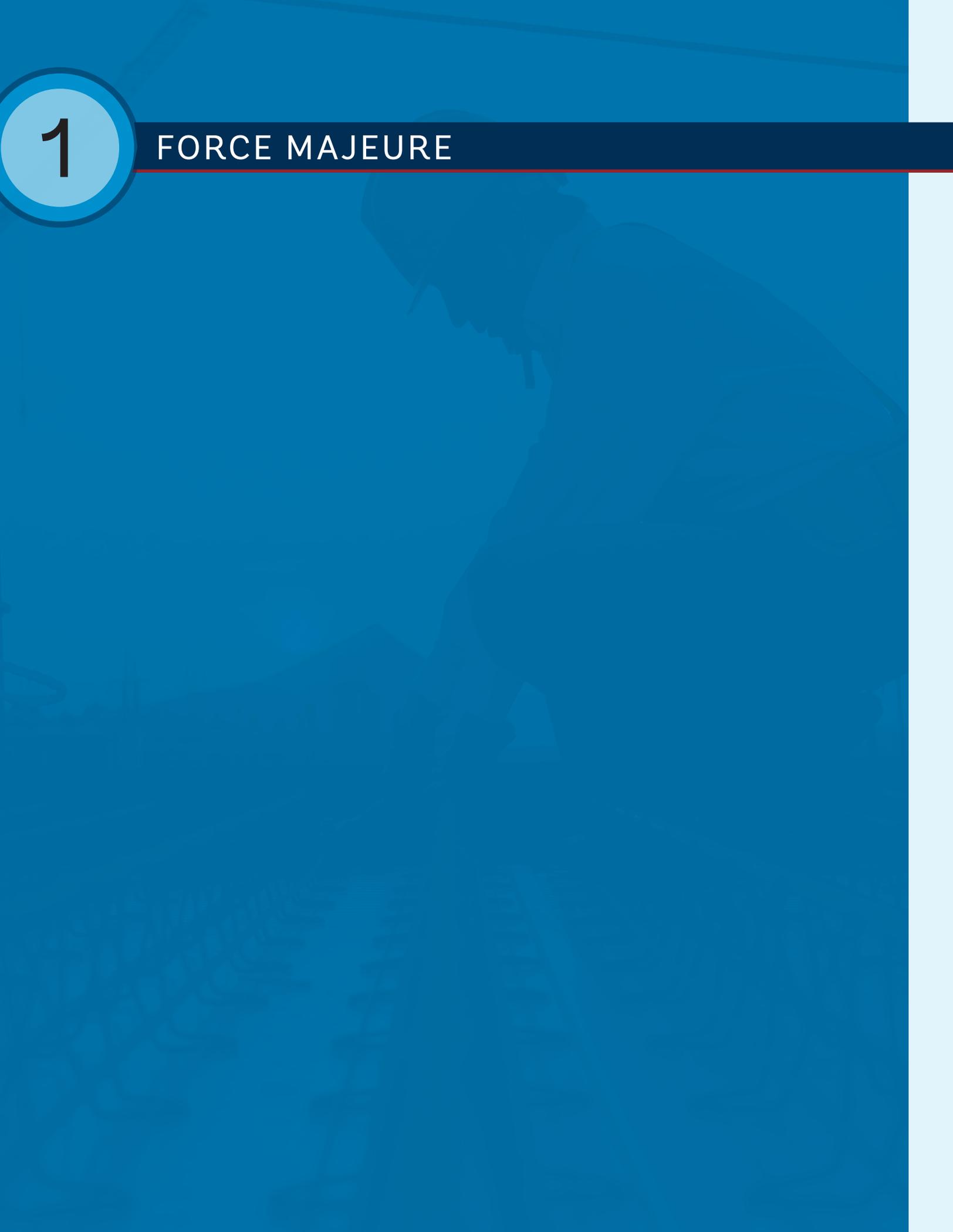
46 See <https://www.unece.org/ppp/wpppp1.html> and https://www.unece.org/fileadmin/DAM/ceci/documents/2017/PPP/WP/ECE_CECI_WP_PPP_2017_CRP9.pdf.

47 See <https://www.unece.org/ppp/wpppp1.html> and https://www.unece.org/fileadmin/DAM/ceci/documents/2017/PPP/WP/ECE_CECI_WP_PPP_2017_CRP12.pdf.

negotiation between Contracting Authorities, Private Partners and Lenders. Its goal is to help Contracting Authorities negotiate key aspects of PPP Projects confidently and efficiently and to reduce the time and money being spent negotiating contractual terms which may ultimately result in an unaffordable or unbankable PPP Contract.

1

FORCE MAJEURE



1.1 KEY ASPECTS

1.1.1 The concept of Force Majeure

“Force Majeure” was originally a civil law concept, but it is now widely used in commercial contracts, including those governed by the laws of common law jurisdictions.

Force Majeure essentially refers to events or circumstances which:

- (a) are beyond the control of the contracting Parties; and
- (b) make it impossible for one Party to fulfil all or a material part of its contractual obligations (i.e. they are prohibitive in nature as far as contractual performance is concerned).

1.1.2 Why do PPP Contracts contain Force Majeure provisions?

The aim of Force Majeure provisions in a PPP Contract is to allocate the financial and timing consequences of Force Majeure events between the Contracting Authority and its Private Partner⁴⁸. The starting assumption for both Parties should be that the risk of a Force Majeure event occurring is shared because it is outside both Parties’ control and neither is better placed than the other to manage the risk of such occurrence or its consequences.

The provisions are typically drafted mutually, but short-term consequences under the PPP Contract are most likely to affect the Private Partner, whereas the broader impact will mainly be on the Public Authority and users/society more generally. This raises some important issues which are the focus of this [Section 1](#):

- (1) what events qualify as Force Majeure events;
- (2) whether and how the Private Partner should be compensated as a result of a Force Majeure event (e.g. for increased costs and/or loss of revenue);
- (3) whether and for how long key milestones under the PPP Contract should be deferred as a result of a Force Majeure event;
- (4) whether the Private Partner or the Contracting Authority should be relieved from its obligations to perform under the PPP Contract and from the related consequences (e.g. the risk of termination due to default); and
- (5) whether the PPP Contract should be terminated if a Force Majeure event persists for a significant period of time and what termination compensation should be paid, if any.

⁴⁸ See the Global Infrastructure Hub’s: *PPP Risk Allocation Tool 2019 Edition*, (e.g. the Force Majeure risk entries in its risk matrices. [See link in Appendix A, Additional PPP Resources.](#)

This Guidance assumes in considering the impact of Force Majeure on the Parties that the main obligations of the Contracting Authority are financial as opposed to positive obligations of service or raw material provision. The impact of Force Majeure on the Contracting Authority would require specific consideration in cases where it was under such obligations.

CIVIL AND COMMON LAW DIFFERENCES

Many jurisdictions have a concept of Force Majeure under general law⁴⁹. In some cases, this can limit the freedom of the Parties to agree alternatives in a PPP Contract as it may not be possible to derogate entirely from the scope of the legal concept. This is particularly the case in civil law jurisdictions. However, most PPP Contracts include specific Force Majeure provisions, whether they are civil law or common law governed, as this provides contractual certainty for the Parties and avoids delay in addressing the consequences if Force Majeure occurs. This is essential to protect the Contracting Authority and to make the PPP Project bankable for Lenders and Equity Investors alike. It is advisable to include an express statement in the PPP Contract as to whether or not the relevant provisions intend to derogate from applicable underlying law, and if so, to what extent.

1.1.3 Relationship to other provisions

In a traditional commercial contract, for example between two private sector entities, shared Force Majeure risk would typically include “acts of God” such as natural disasters and epidemics (often referred to as “natural Force Majeure”) as well as “political” events such as general strikes, nationalization and a public sector refusal to grant licenses (often referred to as “political Force Majeure”).

In a long-term PPP Contract, where one of the Parties is a public sector entity, there is close scrutiny of the type of political Force Majeure events which may arise during the life of the PPP Contract and how each risk should be allocated. This is because political Force Majeure is seen as more within the control of the public sector (and entirely beyond the control of the Private Partner). Deciding whether the risk should be borne by the Contracting Authority alone, shared by the Parties, or borne by the Private Partner as a commercial risk may in practice be difficult. It will inevitably depend on the situation in the relevant jurisdiction, the type of event being considered and the level of contingency that the Private Partner would price into its bid to cover the risk if allocated to it. For example, while it is usually accepted that the type of political risk which should lie wholly with the Contracting Authority includes deliberate acts of state such as outright nationalisation of the PPP Project, the position as regards war events will depend on the jurisdiction concerned. If any kind of civil or external war event is highly unlikely, the Private Partner may be comfortable with the risk being treated as a shared Force Majeure risk and any contingency it prices into its bid will be relatively low. In more volatile jurisdictions where the war risk is high, however, the Private Partner may not be prepared to bear any risk at all (or alternatively would price such a high contingency into its bid that the PPP Contract may prove very expensive or even unaffordable). In this instance, such events may be more appropriately treated as Contracting Authority risk, or looked at more individually so that, for example, civil war may be classed as Contracting Authority risk, but external war events classed as shared Force Majeure risk.

49 In France, for example, the affected Party is relieved from its obligations if Force Majeure prevents performance. French jurisprudence has defined the characteristics of a Force Majeure event as (i) beyond the control of the parties, (ii) unforeseeable and (iii) impossible to overcome.

If there are political risk events to be allocated solely to the Contracting Authority, it is likely that these events will require separate treatment in bespoke provisions. In this Guidance, events in this category are treated as “Material Adverse Government Action” (“MAGA”) events. They are given separate treatment in their own contractual provision and are discussed in more detail in [Section 2, Material Adverse Government Action](#). A similar type of approach is seen, for example, in the PPP airport sector in the Philippines and also in certain African power projects (such as the International Finance Corporation’s Zambia Scaling Solar Program). [See Section 2, Material Adverse Government Action](#).

In some jurisdictions (such as Australia and the UK), there is no need for a specific MAGA provision as Private Partners accept that the type of political risks likely to arise are limited and can be dealt with through the Force Majeure shared risk provisions, together with separate provisions dealing with specific events for which risk is allocated either to the Contracting Authority (such as Contracting Authority breach of contract and change in law) or to the Private Partner.⁵⁰ [See also Section 2.1.3, Material Adverse Government Action and Section 3, Change in Law](#).

There is no right or wrong approach and the fundamental principle remains the same – risks should be allocated to the Party best able to control and/or manage them and the PPP Contract should address them in the clearest way possible.

CIVIL AND COMMON LAW DIFFERENCES

Force Majeure provisions differ from so-called “hardship clauses” which deal with unexpected circumstances where performance becomes more onerous for a Party without being impossible. Hardship clauses stem from underlying statutory legal concepts in certain jurisdictions (e.g. France⁵¹) and are not usually found in common law contracts.

Notably, PPP Contracts in civil law countries often derogate from or clarify and complete underlying statutory legal hardship provisions in favor of an agreed contractual risk allocation where this is legally effective. This is to provide certainty for the Parties and is the recommended approach for Contracting Authorities where possible under the applicable governing law. As mentioned in [Section 1.1.2 above](#), it is advisable to include an express statement in the PPP Contract as to whether or not the relevant provisions intend to derogate from applicable underlying law. [See Section J, PPP Contracts in Context](#).

⁵⁰ This is part of an approach which typically distinguishes between (a) events which entitle the Private Partner to the same type of full relief (namely, both cost reimbursement and extensions of time) and are sometimes termed “Compensation Events”; (b) events which only entitle the Private Partner to extensions of time (known as “Relief Events”); and (c) “Force Majeure Events” (which are a shared risk but usually have a narrow scope as some political and natural Force Majeure risks are instead treated as Relief or Compensation Events). See the *Infra Australia PPP Guidelines* and the *UK PF2 Guidance*.

⁵¹ In France, administrative courts will enforce the doctrine of hardship (*imprévision*), which allows a party to claim compensation through an increase in the contract price where the circumstances of the contract have changed in a manner which could not have been foreseen by the parties (i.e. by events that are unforeseeable, beyond the control of the parties and have a fundamental impact on the economic balance of the contract). Unlike Force Majeure, however, performance is not impossible. French PPP Contracts may provide that *imprévision* can be invoked in accordance with case law or may define expressly the financial threshold deemed to trigger the Private Partner’s right to claim compensation. This hardship circumstance is intended to be temporary. The Contracting Authority is entitled to terminate the PPP Contract in circumstances where the price increase is too significant or if it is foreseen that the situation will last indefinitely.

1.1.4 Force Majeure and related Project Agreements

The Private Partner and its Lenders will review Force Majeure provisions in detail and will want to ensure that the Force Majeure provisions in the Project Agreements mirror those under the PPP Contract (both in terms of definition and consequences). The Project Agreements should generally provide the Sub-contractor with no greater protection against the risk of Force Majeure than the Private Partner enjoys under the PPP Contract (so that there is “equivalent project relief”). This is to ensure that the Private Partner does not find itself in a position where it is obliged to give a Sub-contractor Force Majeure relief to which it is not itself entitled under the PPP Contract. The contractual arrangements will, however, need to address how to take into account the impact of the Force Majeure Event at Sub-contractor level in order to assess appropriate consequences under the PPP Contract.

Similarly, when the PPP Contract sets out conditions precedent to the Private Partner’s entitlement to any Force Majeure protection (e.g. notice requirements and the obligation to supply supporting information), these conditions need to be reflected in the Project Agreements. While this is primarily an issue for the Private Partner and its Lenders, it is in the Contracting Authority’s interests to ensure requirements for this flow down are in place to ensure there is no negative impact on the PPP Contract. *See also Section 2.1.4, Material Adverse Government Action and Section 3.1.4, Change in Law.*

While following the Force Majeure approach in internationally recognized forms of construction contract⁵² may be appropriate for some PPP Contracts, the starting point for a Contracting Authority should always be to consider what the appropriate risk allocation position is for its PPP Contract and for this position to then flow down into (as opposed to up from) the Project Agreements. This may well result in a different approach to construction industry standard forms and means that the construction sub-contract will be a form of contract that reflects the approach in the PPP Contract and is therefore specific to the relevant project. This is usually the right approach in PPP Projects where financing is on a limited recourse basis and the SPV transfers the risks assumed under the PPP Contract to its Sub-contractors under the Project Agreements resulting in a construction contract and operation and maintenance agreement that are “back-to-back” with the PPP Contract. Such flow down structures are likely to be critical to the bankability of the PPP Project.

1.2 KEY CONSIDERATIONS FOR THE CONTRACTING AUTHORITY

1.2.1 Defining the events or circumstances that qualify as “Force Majeure”

1.2.1.1 Freedom to contract – Before drafting and negotiating Force Majeure provisions, the Contracting Authority needs advice from its legal advisers about how much contractual freedom the Parties have under the PPP Contract’s governing law to (i) define the concept of Force Majeure in the PPP Contract and (ii) specify its consequences.

⁵² For example, the forms of construction contract produced by FIDIC (The International Federation of Consulting Engineers).

CIVIL AND COMMON LAW DIFFERENCES

In jurisdictions which have an underlying legal concept of Force Majeure (typically civil law jurisdictions), the Parties' ability to derogate from the legal definition of Force Majeure and amend or create their own definition of Force Majeure and its effects may be limited and must be verified on a case-by-case basis. In France, for example, Force Majeure is defined by French jurisprudence as an event beyond the control of the Parties, unforeseeable and impossible to overcome. In Belgium, Parties include details on the scope and consequences of Force Majeure, taking into account Belgian legislation and jurisprudence.

In other jurisdictions (typically common law jurisdictions, but also, for example, the Netherlands⁵³ and Poland), the Parties will have no restriction on their ability to mutually agree on the scope of Force Majeure and the consequences of an event occurring.

1.2.1.2 Different Approaches – There are broadly two main approaches to defining Force Majeure:

- (a) **Approach 1: an open-ended catch-all definition** including all events beyond the reasonable control of the affected Party which satisfy certain criteria such as foreseeability and avoidability and prevent the affected Party performing. Despite such a general approach, it is also common to list specific events considered to be Force Majeure under this definition, recognizing that any such list is only illustrative and is not exhaustive. This can be advisable in jurisdictions where the courts are unlikely to expand upon the contractual definition given by the Parties to ensure such events are included. *See Section 1.2.1.3 and Section 1.4, Sample Drafting 1, Clause (1).*

EMERGING AND DEVELOPED MARKET DIFFERENCES

This catch-all approach is often seen in civil law-governed contracts and may be more appropriate in emerging and less stable PPP markets where it may be more challenging to expect a Private Partner to manage the consequences of the type of events which meet the definition criteria. For example, if there are limited available resources in the country itself, more dependence may have to be placed on an external supply chain than in a resource-rich country. An open-ended definition may also provide more certainty in jurisdictions without PPP case law/precedent, as Force Majeure often requires an element of “unforeseeability” (*see Section 1.2.1.3*) and an open-ended category is more in line with that concept than listing (i.e. foreseeing) unforeseeable events.

Contracting Authorities should, however, consider carefully the effect of an open-ended definition as a wide definition will result in the risk of such events being shared, whereas it may be appropriate for the Private Partner to bear more risk in respect of certain events in some cases (e.g. by qualifying or excluding certain events). This is an important consideration as regards natural disaster and climate risk events, for example. *See Sections 1.2.1.2(c) and Section 1.2.1.5.*

⁵³ In the Netherlands, the PPP Contract may typically include wording waiving statutory rights in respect of “unforeseen events” – this type of express approach may be persuasive if such derogation were to be tested in court.

- (b) **Approach 2: an exhaustive list of specific events or circumstances** which are (expressly or inherently) beyond the control of the affected Party and prevent it from performing. These typically include (i) political events (e.g. wars, acts of terrorism, strikes and protests) to the extent treating them as a shared risk is agreed appropriate, (ii) natural disaster events (e.g. earthquakes, landslides, floods) including, if appropriate, climate risk events (see [Section 1.2.1.5](#)), and (iii) events such as nuclear explosions. An example of this is the Dutch Model which sets out a very limited list of Force Majeure events, as do the UK PF2 Guidance (under which the events listed are essentially uninsurable) and the Infra Australia PPP Guidelines. See [Section 1.5, Sample Drafting 1A, Definition of “Force Majeure Event”](#).

EMERGING AND DEVELOPED MARKET DIFFERENCES

Some types of event which might be treated as Force Majeure in Emerging Markets may be treated in Developed Markets as “Relief Events” which are at the Private Partner’s risk and if they occur only entitle the Private Partner to relief from breach of contract to the extent they cause it to miss a key performance date under the PPP Contract (i.e. “time” relief). The Private Partner has been prepared to take a view on such risks and how best to manage them where markets are developed and predictable.⁵⁴

- (c) **Exclusions and qualifications:** in relation to both Approach 1 and Approach 2, it is not uncommon to specify events which are specifically excluded from the definition of Force Majeure or which only qualify if they occur to a sufficient degree. In this case, the drafting focus will shift to what is not Force Majeure as opposed to what is. For example, in countries where certain natural events regularly occur (such as seasonal rains resulting in floods) and which should have formed part of the Private Partner’s due diligence when formulating its proposed price, the degree of such events should be specified so that only “exceptional” occurrences qualify as Force Majeure (e.g. floods of a scale that occur not more frequently than once in every [100] years or earthquakes over a specified seismic intensity). The same approach may be appropriate in respect of certain climate risk events (e.g. only including heavy rains above a specified rate or temperatures outside a specified range) – see [Section 1.2.1.5 and Section M, PPP Contracts in Context](#). It may be helpful in certain civil jurisdictions to set out the rationale for excluding certain events, as the courts may have the power to consider them as Force Majeure even though expressly excluded by the Parties.

Particular sectors may have specific requirements as well – for example, defense PPP Projects might exclude certain events if the PPP Contract is intended to operate during times of war; and environmental PPP Projects or PPP Projects involving chemical treatment may also need to have a narrower definition if the Private Partner is intended to deal with a certain degree of chemical contamination (such as a hospital or defense project).

⁵⁴ This is part of the approach described in the footnote to [Section 1.1.3 Force Majeure](#).

Analysing historic data and drawing on previous experience can assist the Contracting Authority in qualifying or excluding events appropriately, for example as regards climate risk events and natural disasters⁵⁵. As highlighted in [Section F and Section M, PPP Contracts in Context](#), bidders' design and price will be affected by what falls within the Force Majeure provisions, so this must be considered carefully by the Contracting Authority during the feasibility and procurement phases.

Whichever drafting approach is selected, above all, the Contracting Authority and its advisers must carefully consider the specific nature and individual circumstances of the PPP Project in question to ensure that the definition is appropriate for that PPP Project (and not simply adopted from a previous PPP Project or another sector or jurisdiction). This is particularly the case bearing in mind the consequences of a Force Majeure event and the Contracting Authority's potential liability (e.g. if ongoing payments are required or termination results) and ability to restrict the uncertainty that comes with prolonged Force Majeure.

1.2.1.3 Foreseeability and avoidability – To qualify as a Force Majeure event, the definition may also require that an event was not foreseeable, or if it was foreseeable that it could not reasonably have been avoided. Practice varies between jurisdictions and may depend on underlying legal concepts or the nature and extent of the agreed list of Force Majeure events. Climate change events are an example of the type of events which may have become increasingly foreseeable (although not necessarily predictable), but which in many cases are likely not to be within the affected Party's power to prevent, avoid or overcome. [See Section 1.2.1.5.](#)

CIVIL AND COMMON LAW DIFFERENCES

In many civil law jurisdictions the legal definition of Force Majeure requires that the event is unforeseeable and unavoidable from the point of view of the Party whose obligations are affected. Contracting Authorities in these jurisdictions therefore often want to include these requirements in the contractual Force Majeure definition, coupled with a reasonableness test as regards a Party's inability to control and/or prevent an event, even if it is in fact foreseeable. [See Section 1.4, Sample Drafting 1, Clause \(1\)\(b\).](#)

While [Section 1.4, Sample Drafting 1](#) illustrates this civil law approach, PPP Contracts in common law jurisdictions would not typically include this concept of foreseeability, nor would they in some civil law jurisdictions (e.g. the Netherlands). [See Section 1.5, Sample Drafting 1A.](#) However, in some cases the extent to which the impact of the Force Majeure event could have been reasonably prevented/mitigated may be key in determining entitlement to relief from breach of contract⁵⁶ (a factor which should be borne in mind particularly in the context of climate risk treatment, for example – [see Section 1.2.1.5 and Section M, PPP Contracts in Context.](#))

⁵⁵ See for example the approach outlined as regards seismic intensity and heavy rains in Japan: <http://documents.worldbank.org/curated/en/479931516124878843/pdf/122703-WP-PUBLIC-P161727-ResilientInfrastructurePPPJapanCaseStudyFINALweb.pdf>

⁵⁶ For example, see the Infra Australia PPP Guidelines.

1.2.1.4 Insurance – The Private Partner typically bears the responsibility for placing appropriate insurances to protect the project and its Lenders will have a keen interest in ensuring that it has adequate cover. Nevertheless, under the PPP Contract, Contracting Authorities typically also require the Private Partner to insure material project risks (e.g. accidental damage, third party liabilities). In the early days of PPPs, the definition of Force Majeure was often based on whether a particular event could be insured against. If there was insurance for a specific political or natural event, it could not be regarded as Force Majeure. Conversely, “uninsurable” events tended to be treated as Force Majeure. Currently, the relationship between insurability and Force Majeure is less straightforward, although the ability of the Parties to insure against certain risks, and to bear the relevant insurance premium costs, must be considered when assessing what insurances the Private Partner should be contractually required to place and the scope of any associated Force Majeure compensation provisions.

It may be appropriate to exclude certain insurable events from the Force Majeure provisions (or to qualify them or limit the application of the provisions) to the extent the Private Partner is able to manage the risk through insurance (and will have factored the premium cost into its pricing) and is entitled to appropriate relief for breach of contract and delay penalties (*see Section 1.2.3.1, Section 1.2.3.2 and Section 1.2.3.3*). This is relevant, for example, when considering the extent to which climate risk (*see Section 1.2.1.5*) and natural disaster events should qualify as Force Majeure events. Equally, if the insurable event is agreed to be a Force Majeure event (e.g. because it cannot be managed solely through insurance and treatment as, for example, a relief event⁵⁷), this will influence any additional relief that may be agreed by the Contracting Authority. Insurance proceeds paid⁵⁸ (other than to compensate third parties) may also be deducted from any termination amount payable. The Contracting Authority should also expect that the costs of insurance will be reflected in pricing – either ultimately being passed on to third party users via the approved tariff or fee (under the “user pays” model) or to the Contracting Authority itself (under the “government pays” model).

Generally, uninsurability is addressed in separate provisions, although some jurisdictions may not recognize the concept of uninsurability or may not typically address it contractually due to the existence of general law provisions. *For further detail see Section 1.3 and definition of “Uninsurability”.*

1.2.1.5 Climate change risk events – Although market practice in this area is still developing, the impact of climate change and the treatment of climate risk events are coming under increasing scrutiny in PPP Projects. This is in respect of both “one-off” extreme weather events, as well as more gradual climate change effects such as rising temperatures and sea levels. Both have potentially significant consequences in long term PPP Projects, although will be more of a risk in some projects than in others, depending on the nature/sector and the physical location of the PPP Project, and the resources needed for it. The Parties may (for example) want to specify certain types of extreme weather conditions or changes in habitat which qualify as Force Majeure events in order to address climate change risks as they relate to their specific project (for example, sea levels rising beyond a certain level where this would adversely affect a project located on the coast). This approach recognizes that, while the possibility of climate change and its consequences may have become increasingly foreseeable, it is unlikely to be in the affected Party’s power to prevent, avoid or overcome certain events

⁵⁷ See footnote to *Section 1.1.3*.

⁵⁸ Or, depending on the jurisdiction, and timing of actual payment by the insurers, payable.

on its own. As highlighted above, the Parties should carefully assess whether the legal system in the country in which their PPP Project is located allows for inclusion of such events under Force Majeure. The Sample Drafting does not include specific examples as this is extremely project-specific and market practice is still developing.

Climate risks will be shared risk events under the Force Majeure provisions. Some events (or degrees of event) may be insurable and, as mentioned in [Section 1.2.1.4](#), it may be appropriate for the Contracting Authority to require the Private Partner to insure against these risks and/or to exclude them from the full scope of the Force Majeure provisions (or to set certain thresholds before they qualify as Force Majeure events).⁵⁹ The Contracting Authority should bear in mind that the occurrence of certain climate risk events over the life of the PPP Contract may affect insurance premiums and availability (and some local insurance markets may not have capacity to cover such risks in the first place). This insurance risk should form part of any assessment as to how to treat climate risks in the PPP Contract. To the extent that climate risks are excluded from the Force Majeure regime (and subject to any applicable underlying laws), the Private Partner will bear the risk of their occurrence unless an alternative risk sharing or management mechanism is in place in the PPP Contract. [See Section 1.2.1.4, Section 1.3 and Section M, PPP Contracts in Context.](#)

1.2.2 Consequences of Force Majeure Event

If a Force Majeure event occurs, the Parties need to discuss how, and the extent to which, performance of the PPP Contract can continue and how the effects of the Force Majeure event can be mitigated or managed. The PPP Contract may include an express provision to this effect ([see Section 1, Sample Drafting 1A, Clause \(4\)](#)) but in practice this should happen anyway (and will be necessary to properly assess any relief given to the Private Partner under the relevant provisions ([see Section 1.2.3](#)). These discussions may include action such as Contracting Authority step-in, where applicable ([see Section 4, Contracting Authority Step-in Rights](#)).

1.2.3 Relief for Private Partner non-performance

Contracting Authorities are likely to be asked to consider whether the Private Partner should be entitled to any relief if a Force Majeure event occurs preventing it from performing. Apart from being unable to meet its contractual obligations, the Private Partner may incur additional costs and suffer loss of revenue to the extent it is unable to commence or continue to provide the service. In the construction phase, a delay to completion may also cause the Private Partner to incur additional financing costs (e.g. additional interest during construction) or if it has to reschedule its repayment obligations). In the operating period it is likely to still be incurring fixed costs (in particular debt service costs), which it may be unable to meet and its financial position may be materially affected. This applies whether the “user pays” or “government pays” payment model is being used ([see Section G, PPP Contracts in Context](#)).

While the underlying principle of Force Majeure is that losses lie where they fall and Parties should bear their own costs and damages, different approaches can be taken. The Contracting Authority should assess the extent to which it is prepared to pay

⁵⁹ See, for example, <http://documents.worldbank.org/curated/en/479931516124878843/pdf/122703-WP-PUBLIC-P161727-ResilientInfrastructurePPPJapanCaseStudyFINALweb.pdf>.

compensation to the Private Partner to prevent a payment default under its project or financing agreements while a Force Majeure event subsists (e.g. by continuing to pay an availability payment or other compensation) and/or to enable it to make up lost revenues and costs incurred if the PPP Contract is to resume (e.g. via an extension of the operating period or increased tariff).

Although it is typical for a PPP Contract to expressly include some additional relief (particularly in respect of Force Majeure events occurring during the construction phase), it is impossible to know in advance what will be appropriate following every Force Majeure occurrence as the effects may vary greatly (some may have a greater or longer term impact than others). In practice, if a Force Majeure event occurs, the Parties will be discussing how to facilitate continued performance of the PPP Contract (including agreeing at the time on any additional relief) and a contractual provision reflecting this is often included. *See Section 1.5, Sample Drafting 1A, Clause (4).*

The availability of insurance will be relevant to the determination of relief (*see Section 1.2.1.4 and Section 1.3*), as will the period of time that a Force Majeure event must subsist before either Party may be entitled to terminate the PPP Contract. Not surprisingly, the period of time that must elapse before termination rights arise tends to be shorter in PPP Contracts where no financial compensation is expressed to be payable to the Private Partner during the subsistence of a Force Majeure event.

It is worth noting in this context that if termination ultimately occurs, the Contracting Authority will most likely pay compensation to the Private Partner (e.g. at a minimum in an amount equal to the outstanding senior debt). *See Section 8, Termination Payments.*

Typically, the Party claiming relief for a Force Majeure event will be obliged to take reasonable action to mitigate its effects and provide a mitigation strategy to the other Party. Failure to do so may affect its rights to relief. In some cases, the Parties may agree to exclude certain measures from the mitigation requirement.

Types of relief are discussed in *Sections 1.2.3.1–1.2.3.8*. The extent to which one or more of these will apply will depend on the circumstances.

1.2.3.1 Relief from breach of contract –The occurrence of a Force Majeure event affecting the Private Partner’s ability to fulfil its contractual obligations will generally allow it relief from its obligations under the PPP Contract so that it is not in breach of contract, but the Contracting Authority should ensure that relief is given only to the extent that the Private Partner’s inability to perform its obligations is directly caused by the Force Majeure event. *See Section 1.4, Sample Drafting 1, Clauses (3) and (5) and Section 1.5, Sample Drafting 1A, Clause (1).*

It is also typically accepted that the Private Partner is (at least partially) excused from further performance of its affected obligations under the PPP Contract while the Force Majeure event is continuing. *See Section 1.4, Sample Drafting 1, Clauses (3) and (5) and Section 1.5, Sample Drafting 1A, Clause (1).*

1.2.3.2 Liquidated damages relief – If the Private Partner is liable to pay liquidated damages to the Contracting Authority if it fails to meet certain construction phase milestones (such as the scheduled date for commencing operations), it will typically want to be expressly relieved from such liability to the extent it relates to the obligations it is unable to fulfil due to the Force Majeure event. Market practice is to

expressly provide for such relief upfront in the PPP Contract by granting the Private Partner entitlement to apply to extend the milestone dates (by the period of delay caused by the Force Majeure event). [See Section 1.2.3.3.](#)

1.2.3.3 Extension of time for performance – The Contracting Authority usually expressly grants the Private Partner an extension of time in respect of delays to the commencement of operations that are attributable to Force Majeure events during the construction phase. This will include postponing the date on which the construction of the PPP Project should have been completed by the Private Partner (the mechanic for doing this may be set out in another clause dealing more generally with extensions of time) and the date on which any corresponding liability for liquidated damages arises. [See Section 1.2.3.2.](#)

1.2.3.4 Increased finance costs pre-completion – If Force Majeure delays completion of the PPP Project asset, the Private Partner will not be able to commence service operations and start earning revenue to meet its debt service obligations. It may incur additional interest and commitment fees and the costs of rescheduling its repayment obligations. If the Private Partner adds in some contingency pricing against this risk, this will have value-for-money implications for the Contracting Authority. In recent years, PPP Contracts in some jurisdictions (e.g. the Netherlands) have expressly provided for certain compensation in this regard, with mechanics distinguishing between different types of debt and lengths of delay.

1.2.3.5 Continued availability payment – Under the “government pays” model ([see Section G, PPP Contracts in Context](#)), it may be appropriate risk sharing for the Private Partner to (a) continue to be paid as if it is performing in full, (b) to be paid an adjusted amount to cover debt service costs (but not the operation and maintenance cost savings that may arise from not performing or lost profit), or (c) not to be paid at all. This will in part depend on the availability of insurance (such as business interruption insurance). Another possibility is to adjust the performance regime in respect of any part of the service that is able to be provided in order to reduce any payment deductions.

EMERGING AND DEVELOPED MARKET DIFFERENCES

The extent to which compensation is paid (or relief from deductions under the payment mechanism is granted) during the continuation of a Force Majeure event can vary according to jurisdiction. It is less common in some Emerging Markets for a Contracting Authority to make additional payments during a Force Majeure event unless it is a political risk event considered within its control (i.e. a type of MAGA event as described in [Section 2.2.1](#)).

In Developed Markets (particularly some civil law jurisdictions), Contracting Authorities may be more willing to make payments. However, in some jurisdictions, such as the UK, it is more common for the PPP Contract to identify specific risks that the Private Partner cannot bear (such as a volatile raw materials price) and provide expressly for financial relief on their occurrence.

1.2.3.6 Tariff increases – Where the PPP Contract has a “user pays” model (*see Section G, PPP Contracts in Context*), the Contracting Authority may allow the Private Partner to be compensated for increased costs and lost revenues by increasing the relevant toll payments or tariffs (for example the tariffs in a concession for a water or waste water network) if the PPP Contract resumes. The Contracting Authority will need to consider any social and political ramifications of this approach in particular in Emerging Markets where the economic situation may not be stable, as well as if it is legally possible to increase the relevant toll payments or tariffs.⁶⁰ The PPP Contract may provide upfront that any restrictions on the Private Partner’s ability to set the relevant tolls or tariffs are to be lifted as necessary to take account of relevant costs arising from Force Majeure events. However, where tariff increases are subject to an overarching regulatory regime or where such measures would imply a high political risk, it may not always be possible to achieve an increase even if justifiable under the PPP Contract. In this instance the Contracting Authority would have to effect the compensation due by some other means. It should also be noted that Lenders may consider any compensation mechanism involving increased tariffs as increasing the overall risk profile (e.g. if user demand may then decrease) and may accordingly prefer upfront payment by the Contracting Authority.

1.2.3.7 Extension to the operating period – The Contracting Authority may also grant an extension to the operating period if it considers it appropriate to compensate the Private Partner in this way in respect of lost revenues (or costs incurred) due to Force Majeure.

1.2.3.8 Interim costs/lump sum compensation – Despite compensation being granted through one or more of the above means (such as by way of an extension to the operating period or increased tariffs), additional costs (e.g. for capital works) may nevertheless need to be incurred by the Private Partner before any actual compensation from the Contracting Authority is received. One way for Contracting Authorities to address this, which is not uncommon in certain developed jurisdictions, is for the Private Partner to have an obligation to seek financing for such additional costs on the best possible terms. If such financing is not available or the Contracting Authority rejects the terms, the Contracting Authority either becomes the lender of last resort or is required to make an upfront payment, typically on a lump sum reimbursement basis.

1.2.3.9 Performance regime relief – Where the PPP Contract include a bonus/penalty (or penalty only) regime based on the achievement of certain key performance indicators, it may be appropriate to grant the Private Partner certain relief in this regard.

1.2.4 Termination

In many PPP Contracts, a prolonged Force Majeure event (typically in excess of six to 12 consecutive months) will trigger a right for either Party to terminate the PPP Contract if it is unlikely that circumstances will return to normal and the Parties cannot agree a solution within the specified period.

As mentioned in *Section 1.2.3*, where no financial compensation is payable to the Private Partner during the subsistence of a Force Majeure event, the termination right tends

⁶⁰ Higher user fees may be commercially viable, but discriminatory under international agreements to which the Contracting Authority/government is party (e.g. International Covenant on Economic, Social and Cultural Rights, Convention on the Elimination of Discrimination Against Women, and the Convention on the Rights of the Child).

to arise sooner – typically when the Force Majeure event has subsisted for 180 days (six months) or more. *See Section 1.4, Sample Drafting 1, Clause (8) and Section 1.5, Sample Drafting 1A, Clause (5).*

The Contracting Authority will want to consider the critical nature of, and impact on, the services or infrastructure provided under the PPP Contract to determine the appropriate period. It may want to include the ability to exercise step-in rights (*see Section 4, Contracting Authority Step-in Rights*) or an asymmetrical termination right (where the Private Partner’s right to terminate arises after a longer period than the Contracting Authority’s) if it likely to be in a better position than the Private Partner to guarantee on-going performance of the PPP service or asset if a Force Majeure event occurs. This may, for example, be the case if resolving or mitigating the consequences of the Force Majeure event requires intervention by public sector disaster relief services (army, fire brigade, etc.) or other measures that can only be taken by the government or Contracting Authority (such as legislative action, prosecution, etc.).

Some jurisdictions may distinguish between types of Force Majeure event in determining rights to terminate. For example, under the Infra Australia PPP Guidelines the Contracting Authority may terminate at any time following the occurrence of an “Uninsurable Force Majeure” event (for which it is insurer of last resort). *See Section 1.3.4.*

If the Private Partner has the ability to terminate the PPP Contract on the basis of a prolonged Force Majeure event, the Contracting Authority may want to include an option to require the PPP Contract to continue, provided that the Private Partner is adequately compensated. Whether this is acceptable to the Private Partner (and its Lenders) on a long term basis will depend on the specific project. It may be more appropriate in “government pays” rather than “user pays” projects due to the additional affordability issues from the Contracting Authority’s perspective.

EMERGING AND DEVELOPED MARKET DIFFERENCES

The option described above is more likely to be encountered in a more Developed Market for the reasons outlined. Under the Infra Australia PPP Guidelines and the UK PF2 Guidance, for example, the Contracting Authority has the right to prevent termination by the Private Partner after the end of the specified period by paying the Private Partner as if the service was being fully provided (subject to applicable mitigation obligations). *See Section 1.5, Sample Drafting 1A, Clause (7).*

As mentioned in *Section 6.1.3*, some jurisdictions may provide for termination rights in other circumstances of prolonged delay where a shared risk approach is appropriate. In the Netherlands, for example, rights exist where the scheduled availability date is exceeded by a certain period due to zoning or permitting issues; the approach is similar to Force Majeure termination and consequences and may similarly provide for asymmetric termination rights.

1.2.5 Determining the amount of a Force Majeure termination payment

If the PPP Contract allows for termination for prolonged Force Majeure, it typically provides that the Contracting Authority pays compensation to the Private Partner reflecting the principle that Force Majeure is neither Party's fault and the financial consequences should be shared. This does not mean that the Contracting Authority should pay "full" compensation (i.e. repayment of all debt, equity and break costs) as this would result in the Contracting Authority bearing all the financial pain. The usual payment amount results in the Private Partner losing all its forecast equity return (i.e. its profit) but being compensated for the equity it has invested (net of distributions received up to the point of termination) and being able to repay all of its outstanding senior debt which is sufficient to address bankability concerns. *See Section 8.5, Termination Payments and Section 8.7, Sample Drafting 8, Schedule, Clause (3).*

EMERGING AND DEVELOPED MARKET DIFFERENCES

Where certain natural risks are insurable (and would reasonably be expected to be insured against as good operating practice), the Contracting Authority may succeed in negotiating paying no termination compensation in respect of such events (or a reduced amount reflecting insurance payments received (or receivable – *see Section 1.2.1.4*) by the Private Partner). This to some extent reflects the practice in more Developed Markets mentioned in *Section 1.2.1.2(b)* where these type of events may instead be classified as "Relief Events" which are at the Private Partner's risk and entitle it to time relief only (but no ultimate right of termination). This will of course depend on the risk assessment by the Private Partner and its Lenders. Any differing treatment agreed upfront for different types of Force Majeure event should be clearly expressed in the PPP Contract.

1.3 UNINSURABILITY

1.3.1 Why do PPP Contracts contain uninsurability provisions?

As mentioned in *Section 1.2.1.4*, although the Private Partner is typically responsible for placing appropriate insurances, the Contracting Authority will usually consider what the Private Partner's insurance needs are and whether the PPP Contract should require the Private Partner to take out certain insurances. The availability and cost of, and the obligation to take out, relevant insurances will be relevant to how the risk of certain events is allocated (such as Force Majeure events), as well as to what deductions may be applied to termination payments in respect of insurance proceeds receivable.

Equity Investors and Lenders may seek protection in the PPP Contract for the Private Partner in case required insurance cover becomes unavailable, less extensive or more costly. Without express contractual protection, uninsurability risk will typically lie with the Private Partner (who will also be in breach of its obligations to maintain the unavailable insurance). This is likely to attract a pricing premium (if indeed it is bankable), depending on the circumstances of the PPP Project and the risk assessment conducted by the Private Partner and its Lenders. Some jurisdictions may address uninsurability through general law provisions, or may not recognize the concept of

uninsurability⁶¹. The Contracting Authority should therefore take specialist advice on how relevant contractual provisions may interplay with general law.

Where there is a known risk of uninsurability in respect of a particular required insurance at the time the PPP Contract is being negotiated (for example, insurance against terrorism or vandalism), this may be addressed through bespoke contractual provisions.

As highlighted in [Section M, PPP Contracts in Context and Section 1.2.1.4 and 1.2.1.5](#), the availability of insurance plays an important part in assessing how the risk of natural disaster and climate risk events should be allocated under the PPP Contract. The Parties may need to develop bespoke mechanisms for addressing the risk of particular insurances becoming unavailable as a result.

1.3.2 Definition of “Uninsurability”

Uninsurability is therefore a somewhat misleading term as it typically does not mean that insurance is not available at all. The usual definition of uninsurability in respect of a particular risk covers:

- (a) the unavailability of insurance on the international insurance market by insurers of an adequate credit rating/reputable insurers of good standing; and
- (b) where insurance premiums are prohibitively high (not merely more expensive) – for example, at such a level that the risk is not generally being insured against in the worldwide insurance market with reputable insurers of good standing by contractors in the relevant country.

EMERGING AND DEVELOPED MARKET DIFFERENCES

Wider reference criteria may be required in certain markets in respect of limb (b) of the definition above – for example, if there is not a sufficient pool of contractors in the relevant country to draw a meaningful market practice comparison. This is likely to be the case particularly in some Emerging Markets.

1.3.3 Consequences of uninsurability

Negotiating a solution – The effect of uninsurability provisions are typically that, if a particular risk becomes uninsurable in accordance with the agreed contractual definition (and not as a result of the Private Partner’s actions), the Parties will negotiate a mutually satisfactory solution for managing the risk, failing which the Contracting Authority will become the insurer of last resort. Any availability payment will then be reduced accordingly to reflect the premium no longer being paid by the Private Partner. The position as regards third party liability insurance is slightly different because clear responsibility is needed in order for the Private Partner and its employees to continue to operate – the Contracting Authority should have the option either to accept the risk itself

⁶¹ See reference to Bulgaria in Termination and Force Majeure Provisions in PPP Contracts – Review of current European practice and guidance (March 2013) – EPEC/Allen & Overy LLP. [See link in Appendix A, Additional PPP Resources.](#)

or to terminate the PPP Contract (on a Force Majeure termination compensation basis). In some jurisdictions, this approach applies to any insurance that becomes unavailable.

Relief from breach – The Contracting Authority usually grants relief to the Private Partner from the obligation to insure, but only to the extent the Private Partner’s own acts or omission have not caused the insurance to become unavailable. If it has caused the unavailability, the Private Partner will be in breach of the PPP Contract which is likely to give the Contracting Authority a right to terminate for Private Partner default (*see Section 8, Termination Payments*).

Insurer of last resort – If the Contracting Authority accepts becoming insurer of last resort, it will be liable for the consequences of the occurrence of the uninsurable risk. It is therefore important that the Contracting Authority is able to manage the risk transferred to it (for example by taking out insurance policies itself or being otherwise able to manage the potential cost impact, for example, by self-insuring)⁶². The Private Partner should also be required to periodically approach the insurance market (e.g. once every three months) to see if the risk can be insured again.

EMERGING AND DEVELOPED MARKET DIFFERENCES

In negotiating an insurer of last resort option, the Private Partner and its Lenders will carefully assess the credit of the Contracting Authority. This type of provision is therefore likely to be seen more in established jurisdictions. In less established jurisdictions there may be more negotiation over whether taking out a particular insurance should be an obligation in the first place and how this risk might otherwise be managed, and/or the risk of the event occurring may instead be managed through the Force Majeure provisions.

1.3.4 Termination

If the Contracting Authority is insurer of last resort and the uninsurable risk occurs, the PPP Contract should provide that the Contracting Authority may either terminate (on a Force Majeure termination compensation basis plus, if applicable, the amount of any third party liability claims) or pay the Private Partner an amount equivalent to the insurance proceeds that would have been payable and continue the PPP Contract. Under the Infra Australia PPP Guidelines, the Contracting Authority’s right to terminate only arises if the uninsurable risk occurs and is also a Force Majeure event (but it can then be exercised at any time). This is separate to the termination option described in *Section 1.3.3* where the Contracting Authority does not become insurer of last resort.

Given that uninsurability is beyond both Parties’ control, it is generally accepted that if termination occurs the Contracting Authority should pay the Private Partner some level of termination compensation, usually calculated on the same basis as Force Majeure termination compensation.⁶³

⁶² In many jurisdictions it is common for public authorities to self-insure (instead of taking out insurance); this may be appropriate for the service or asset covered by the PPP Contract.

⁶³ For more detail on Uninsurability in a Developed Market and sample drafting, please see the Infra Australia PPP Guidelines, South Africa PPP Guidelines and the UK PF2 Guidance.

1.4 SAMPLE DRAFTING 1

(open-ended catch-all definition, including concept of foreseeability)

Definition of Force Majeure Event

- (1) In this PPP Contract, a “Force Majeure Event” means any event or circumstance or combination of events or circumstances:
 - (a) beyond the reasonable control of the Party affected by such event, circumstance or combination of events or circumstances (the “Affected Party”);
 - (b) which was not foreseeable or, if foreseeable, could not have been prevented or avoided or overcome by the Affected Party having taken all reasonable precautions and due care;
 - (c) which directly causes the Affected Party to be unable to comply with all or a material part of its obligations under this PPP Contract; and
 - (d) which is not the direct result of a breach by the Affected Party of its obligations under this PPP Contract or, in respect of the Private Partner, under any other Project Agreement. *[obligations should include compliance with Applicable Law]*
- (2) Force Majeure Events include but are not limited to the following circumstances, provided that they meet the criteria set forth in Clause (1) above:
 - (a) plague, epidemic and natural disaster, such as but not limited to, storm, cyclone, typhoon, hurricane, tornado, blizzard, earthquake, volcanic activity, landslide, tsunami, flood, lightning, and drought;
 - (b) fire, explosion, or nuclear, biological or chemical contamination (other than caused by the negligence of the Private Partner, its contractors, or any Sub-contractor, supplier or vendor);
 - (c) war (whether declared or not), armed conflict (including but not limited to hostile attack, blockade, military embargo), hostilities, invasion, act of a foreign enemy, act of terrorism, sabotage or piracy[, in each case occurring outside the Country];
 - (d) civil war, riot, rebellion and revolution, military or usurped power, insurrection, civil commotion or disorder, mob violence, act of civil disobedience[, in each case occurring outside the Country];
 - (e) radioactive contamination or ionising radiation[, occurring outside the Country]; or
 - (f) general labor disturbance such as boycotts, strikes and lock-outs, go-slow, occupation of factories and premises, excluding similar events which are unique to the PPP Project and specific to the Private Partner or to its sub-contractors[, and occurring outside the Country].

As outlined in Section 1.2.1.5, Limb (b) indicates that certain events (e.g. climate change-related) may be foreseeable but not reasonably avoidable by the Private Partner. See also boxes below.

It may be appropriate to include, qualify or exclude certain natural disasters/ climate risk events depending on the individual project circumstances. See Section 1.2.1, in particular 1.2.1.5, and Section M, PPP Contracts in Context.

List of events to be negotiated for the specific project circumstances, taking into account also whether certain political risks should be treated separately as Material Adverse Government Action or not.

Consequences of Force Majeure Event

- (3) If a Force Majeure Event has occurred, the Affected Party shall be entitled to relief from its obligations under the PPP Contract if it meets the requirements of Clause (4) below.
- (4) To obtain relief under Clause (3) above, the Affected Party must:
 - (a) as soon as practicable, and in any event within [] (● *business*) days after it became aware that the Force Majeure Event has caused or is likely to cause a breach of an obligation under this PPP Contract, give to the other Party a notice of its claim for relief from its obligations under the PPP Contract, including (i) satisfactory evidence of the existence of the Force Majeure Event; (ii) full details of the nature of the Force Majeure Event; (iii) the date of occurrence; (iv) its likely duration; and (v) details of the measures taken to mitigate the effect of the Force Majeure Event;
 - (b) within [] (● *business*) days of receipt of the notice referred to in clause (a) above, give to the other Party full details of the relief claimed, as well as information on all actions being taken by the Affected Party to mitigate the consequences of the Force Majeure Event;
 - (c) demonstrate to the other Party that:
 - (i) the Affected Party, and its contractors, could not have avoided such occurrence or consequences by steps which they might reasonably be expected to have taken, without incurring material cost;
 - (ii) the Force Majeure Event directly caused the need for the relief claimed;
 - (iii) the relief claimed could not reasonably be expected to be mitigated by the Affected Party, including recourse to alternate sources of services, equipment and materials and construction equipment, without incurring material cost; and
 - (iv) the Affected Party is using all reasonable endeavors to perform its affected obligations under this PPP Contract.
- (5) If the Affected Party has complied with its obligations under Clause (4) above, then it shall be excused from the performance of its obligations under this PPP Contract to the extent it is prevented, hindered or delayed in such performance by reason of the Force Majeure Event.
- (6) [If information required under Clause (4) above is provided after the dates referred to in that clause, then the Affected Party shall not be entitled to any relief during the period for which the information is delayed.]
- (7) The Affected Party shall notify the other Party as soon as practicable after the Force Majeure Event ceases or no longer causes the Affected Party to be unable to comply with the applicable obligations under this PPP Contract. Following such notification this PPP Contract shall continue to be performed on the terms existing immediately prior to the occurrence of the Force Majeure Event.

This period of time needs careful consideration – notice should be timely but allow the affected Party a reasonable time to fully develop a mitigation strategy.

Termination due to Prolonged Force Majeure

- (8) If a Force Majeure Event subsists for a continuous period of more than [180-360 calendar] days, either Party may in its discretion terminate this PPP Contract by issuing a written termination notice to the other Party which shall take effect [thirty (30) calendar] days after its receipt. If, at the end of this [thirty (30)]-day period, the Force Majeure Event continues, the PPP Contract shall be terminated pursuant to clause [insert reference to the clause governing termination] and the Private Partner shall be entitled to the compensation set out under clause [insert reference to Compensation on Termination for Force Majeure clause].
- (9) If the Private Partner gives notice to the Contracting Authority under Clause (8) above that it wishes to terminate the PPP Contract, then the Contracting Authority has the option either to accept such notice or to respond in writing on or before the date falling ten [(10)] days after the date of its receipt stating that it requires the PPP Contract to continue. If the Contracting Authority gives the Private Partner such notice, then:
- (a) the Contracting Authority shall pay to the Private Partner the [insert defined term for availability payment] from the day after the date on which the PPP Contract would have terminated under Clause (8) above as if the [insert defined term for the service] was being fully provided; and
 - (b) the PPP Contract will not terminate until expiry of written notice (of at least [thirty (30)] days) from the Contracting Authority to the Private Partner that it wishes the PPP Contract to terminate.

Drafting to be adapted as appropriate for a "user pays"/ "demand risk" model. See Section 1.2.4.

1.5 SAMPLE DRAFTING 1A

(Exhaustive list of specific events, no concept of foreseeability)

Required Definition

”Force Majeure Event” means the occurrence after the date of the PPP Contract of:

- (a) war, civil war, invasion, armed conflict, terrorism or sabotage; or
- (b) nuclear, chemical or biological contamination unless the source or the cause of the contamination is the result of the actions of or breach by the Private Partner or its sub-contractors; or
- (c) pressure waves caused by devices travelling at supersonic speeds,

which directly causes either Party (the “Affected Party”) to be unable to comply with all or a material part of its obligations under this PPP Contract.

It may be appropriate to include (and if applicable qualify or exclude) certain natural disasters/ climate risk events and war events depending on the individual project circumstances. See Section 1.

Consequences of Force Majeure Event

- (1) No Party shall be entitled to bring a claim for a breach of obligations under the PPP Contract by the other Party or incur any liability to the other Party for any losses or damages incurred by that other Party to the extent that a Force Majeure Event occurs and it is prevented from carrying out obligations by that Force Majeure Event. For the avoidance of doubt (but without prejudice to Clauses (5) or (7) below), the Contracting Authority shall not be entitled to terminate this PPP Contract for a [insert defined term for Private Partner Default] if such [Private Partner Default] arises from a Force Majeure Event.
- (2) Nothing in Clause (1) above shall affect any entitlement to make deductions or any deductions made as a result of [insert reference to clauses addressing pricing and payment mechanism] in the period during which the Force Majeure Event is subsisting.
- (3) On the occurrence of a Force Majeure Event, the Affected Party shall notify the other Party as soon as practicable. The notification shall include details of the Force Majeure Event, including evidence of its effect on the obligations of the Affected Party and any action proposed to mitigate its effect.
- (4) As soon as practicable following such notification, the Parties shall consult with each other in good faith and use all reasonable endeavors to agree appropriate terms to mitigate the effects of the Force Majeure Event and facilitate the continued performance of the PPP Contract.
- (5) If no such terms are agreed on or before the date falling [120] days after the date of the commencement of the Force Majeure Event and such Force Majeure Event is continuing or its consequence remains such that the Affected Party is unable to comply with its obligations under this PPP Contract for a period of more than [180] days, then, subject to Clause (6) below, either Party may terminate the PPP Contract by giving [thirty (30)] days’ written notice to the other Party.

For example, if the Force Majeure Event occurs during the construction phase, the Parties could agree that relevant milestone dates are postponed by such time as is reasonable, taking into account the likely effect of the delay.

See also Section 1.2.2.

- (6) If the PPP Contract is terminated under Clause (5) above or Clause (7) below:
- (a) compensation shall be payable by the Contracting Authority in accordance with [insert reference to Compensation on Termination for Force Majeure clause – *see Section 8, Sample Drafting 8, Clause (3)*]; and
 - (b) the Contracting Authority may require the Private Partner to transfer its title, interest and rights in and to any [*insert defined term of relevant Project assets*] to the Contracting Authority in accordance with [*Handback clause*].
- (7) If the Private Partner gives notice to the Contracting Authority under Clause (5) above that it wishes to terminate the PPP Contract, then the Contracting Authority has the option either to accept such notice or to respond in writing on or before the date falling ten [(10)] days after the date of its receipt stating that it requires the PPP Contract to continue. If the Contracting Authority gives the Private Partner such notice, then:
- (a) the Contracting Authority shall pay to the Private Partner the [*insert defined term for availability payment*] from the day after the date on which the PPP Contract would have terminated under Clause (5) above as if the [*insert defined term for the service*] was being fully provided; and
 - (b) the PPP Contract will not terminate until expiry of written notice (of at least [*thirty (30)*] days) from the Contracting Authority to the Private Partner that it wishes the PPP Contract to terminate.
- (8) The Parties shall at all times following the occurrence of a Force Majeure Event use all reasonable endeavors to prevent and mitigate the effects of any delay and the Affected Party shall at all times during which a Force Majeure Event is subsisting take all steps in accordance with industry good practice to overcome or minimize the consequences of the Force Majeure Event.
- (9) The Affected Party shall notify the other Party as soon as practicable after the Force Majeure Event ceases or no longer causes the Affected Party to be unable to comply with the applicable obligations under this PPP Contract. Following such notification the PPP Contract shall continue to be performed on the terms existing immediately prior to the occurrence of the Force Majeure Event.

Drafting to tie in with handback provisions— see Section 9, Handback of Assets at End of Contract.

Drafting to be adapted as appropriate for a “user pays”/ “demand risk” model. See Section 1.2.4.

2

MATERIAL ADVERSE GOVERNMENT ACTION

2.1 KEY ASPECTS

2.1.1 *The concept of MAGA*

The concept of “Material Adverse Government Action” (or MAGA), is applicable to contracts, such as PPP Contracts, where one of the Parties is a public sector entity, or government. MAGA events typically:

- (a) delay or prevent the Private Partner from performing its contractual obligations; and/or
- (b) have a material adverse financial impact on the Private Partner; and
- (c) are within the public sector entity/government’s control or are best managed by the public sector entity/government as compared to the Private Partner,

and therefore the risks associated with such events are allocated to the public sector entity/government.

MAGA events are also referred to as “political risk” or “political Force Majeure”. As described in [Section 1, Force Majeure](#), depending on the specific PPP Project circumstances, some forms of political Force Majeure may be treated as shared Force Majeure risk (or in some cases even a Private Partner risk). In this Guidance, MAGA events can be clearly contrasted with Force Majeure events as the risk of their occurrence is allocated entirely to the Contracting Authority and they are given separate treatment in their own contractual provision.

2.1.2 *Why do PPP Contracts contain MAGA provisions?*

MAGA risks are not within the Private Partner’s control but the Private Partner can be adversely affected by their occurrence. Because of the potential impact of MAGA events on the Private Partner’s ability to perform its contractual obligations and be paid, the Private Partner and its Lenders will carefully assess the risk of such events occurring and will expect any significant MAGA risks to be identified and allocated to the Contracting Authority under the PPP Contract. [See Section 2.2.1.](#)

Transferring any MAGA risks to the Private Partner is likely to have two consequences because of the Private Partner’s lack of control over the occurrence or management of such events: (i) at a minimum, to attract a high pricing premium (which could render the PPP Project unaffordable), or (ii) simply to make the PPP Project unattractive to the private sector (with the risk that there will be no bidders) and unbankable.

The purpose of a MAGA clause is therefore to allocate certain agreed types of political risk to the Contracting Authority, address the consequences of such risks occurring (including possible termination) and provide the Private Partner with appropriate relief and compensation.

2.1.3 Relationship to other provisions

All PPP Contracts will contain provisions addressing circumstances for which the Contracting Authority is responsible, but these provisions vary depending on the specific PPP Contract and jurisdiction.

EMERGING AND DEVELOPED MARKET DIFFERENCES

In some established, stable markets, there is typically no need for a specific MAGA provision as Private Partners accept that the type of MAGA risks likely to arise are limited and can be dealt with through the Force Majeure shared risk provisions, together with separate provisions dealing with specific events for which risk is allocated to the Contracting Authority (such as Contracting Authority default and other events for which the Contracting Authority is responsible and which simply entitle the Private Partner to time and/or cost relief and change in law)⁶⁴.

Contracting Authorities in other, typically less established markets may find it expedient if the PPP Contract includes MAGA provisions as well as Force Majeure provisions to ensure the PPP Project is viable for the Private Partner (this has been the case in recent PPP Projects in the Philippines). The inclusion of specific MAGA provisions in such jurisdictions may be because of an actual or perceived increased likelihood of certain MAGA events, or be due to a lack of track record in administering successful PPP Contracts over very long periods of time and across political cycles free from political interference.

Even where included, MAGA provisions may be structured differently as political risks will vary between jurisdictions. Some Contracting Authorities will also choose to address events such as change in law and Contracting Authority default in separate provisions, while others will include them in the MAGA provisions. The South Africa PPP Guidelines, for example, have a MAGA-type provision entitled “Unforeseeable Conduct” which addresses a material effect on the Private Partner’s finances of any unforeseeable discriminatory Contracting Authority action, including change in law. (Contracting Authority default is more usually dealt with in a separate provision and this Guidance treats change in law separately.)

As a result, while not all PPP Contracts will include MAGA provisions in the precise form set out in [Section 2.3, Sample Drafting 2](#), the key is to ensure that the concepts are included, the risks allocated and the consequences made clear in the PPP Contract to ensure clarity and bankability. [See also Section 1.1.3, Force Majeure and Section 3, Change in Law.](#)

2.1.4 MAGA and related Project Agreements

As with Force Majeure, the Parties will need to consider how MAGA provisions flow down to other Project Agreements so that the Private Partner is not left with mismatching contractual positions. [See also Section 1.1.4, Force Majeure and Section 3.1.4, Change in Law.](#)

⁶⁴ This is part of the approach described in footnote 50 to [Section 1.1.3, Force Majeure.](#)

2.2 KEY CONSIDERATIONS FOR THE CONTRACTING AUTHORITY

2.2.1 Defining the events or circumstances that qualify as MAGA

2.2.1.1 **Defined List** – The consequences of a MAGA event occurring are borne by the Contracting Authority, so it is vital to consider carefully what events qualify and how it can minimize the risk of any occurrence. It is recommended that an exhaustive list of clearly defined events is agreed, with the common factor being that their occurrence has a material adverse effect on the Private Partner’s ability to perform its obligations, or on its rights under the PPP Contract, or on its financial status⁶⁵. However, as far as possible such materiality should be clearly defined to avoid the risk of disputes. See further [Section 2.2.1.3](#) and [Section 2.3, Sample Drafting 2, Clauses \(1\) and \(2\)](#).

2.2.1.2. **Events** – As mentioned in [Section 1, Force Majeure](#), the dividing line between political risk (which is allocated to the Contracting Authority) and certain commercial risks (which the Private Partner is expected to take or share) is, in practice, likely to be a difficult one to draw. It is usually accepted that MAGA events include war-related events within the relevant country, as well as deliberate acts of state such as outright nationalisation or expropriation of the PPP Project (including creeping expropriation, which is often carried out indirectly and over a period of time) and a declaration of a moratorium on international payments and restrictions on currency conversions into foreign exchange. MAGA may also include failures by the Contracting Authority or other public entity to grant licenses (provided of course the permit issue is not in any way attributable to the Private Partner, who should be responsible for compliance of the design with applicable laws) or comply with certain critical public sector obligations.⁶⁶

Apart from these more obviously political events, there may be certain risks which result in increased costs and are outside the control of the Private Partner and could have a political aspect to them. For instance, there could be a politically inspired strike, which could force up the price of key raw materials which are obliged to be purchased locally or a dock strike could prevent the importation of materials.

It is worth noting that some MAGA risks will seem more clearly within the Contracting Authority’s control than others (e.g. where the event is controlled by it or occurs as a clear result of its actions, as opposed to happening through a higher or more distant arm of government). However, as the nature of these risks is such that they cannot or will not be borne by the Private Partner (or will result in unaffordable pricing), market practice is that these risks are typically accepted by the Contracting Authority. One approach which the Contracting Authority may find helpful is to sub-categories MAGA events into “fault” and “non-fault” events, even though they are both still at its risk.

The individual circumstances of the PPP Project and jurisdiction will need to be taken into account. For example, failure to provide raw water of a certain quality in a water

65 A reciprocal position is sometimes seen – for example, the “Unforeseeable Conduct” provisions in the South Africa PPP Guidelines also address cases where there is a beneficial effect on the Private Partner’s finances.

66 MAGA should not as a rule include failure by the Contracting Authority/government to enact laws crucial for the implementation of the relevant PPP Project. If the legal framework required for the PPP to start and be implemented is not in place, the PPP Project is unlikely to be bankable and the private sector will be reluctant to spend time and resources bidding. If enabling legislation is necessary, this type of issue should be dealt with as a condition precedent to be satisfied before the PPP Contract is effective. Also, MAGA does not include non-compliance by the Contracting Authority with its obligations under the PPP Contract (which are addressed under provisions dealing with Contracting Authority breach).

sector PPP Project will be a MAGA event if the Contracting Authority is contractually responsible for such supply. Similarly, in a project involving the operation of a tolled highway, port or airport, if the Contracting Authority agrees not to build a competing road, port or airport within a certain distance of the project asset because of the financial effect this is likely to have on the PPP Project (or agrees that there are contractual consequences if it does), construction of such competing asset will be a MAGA event. This is common in demand risk projects where the Private Partner's financial model is reliant on generating user revenue from the asset.

EMERGING AND DEVELOPED MARKET DIFFERENCES

Some jurisdictions are more politically volatile than others. If a political event (such as war) is highly unlikely, the Private Partner may be comfortable with the risk being treated as a shared Force Majeure risk. In more volatile jurisdictions, however, certain events may be more appropriately treated as Contracting Authority risk under MAGA provisions. Alternatively, it may be appropriate to differentiate between certain political risks so that they are classified as Force Majeure Events if they occur outside the relevant country and as MAGA events if they occur within the relevant country. The Contracting Authority must consider carefully what distinctions, if any, are appropriate for its jurisdiction and PPP Project. *See Section 2.3, Sample Drafting 2, Clause (2).*

2.2.1.3 Materiality – In defining MAGA events, the Contracting Authority will want to consider whether or not all occurrences of the relevant type of events should qualify as MAGA and trigger the contractual consequences. The Contracting Authority may be able to agree certain criteria which an event has to satisfy in order for the Private Partner to be entitled to relief – this could, for example, include a “materiality” threshold related to the effect of the event on the Private Partner. However, the Contracting Authority is strongly advised to define, to the extent possible, any threshold clearly (e.g. by reference to a specific monetary value established by reference to the PPP Project financial model), as any undefined reference to materiality will immediately give rise to a debate over its meaning. The same applies wherever any similar term is used in the PPP Contract. *See Section 2.3, Sample Drafting 2, Clause (1).*

2.2.2 Relief for Private Partner non-performance

As with Force Majeure, the Private Partner will be concerned about both its inability to meet its contractual obligations as a result of a MAGA event and its resulting loss of revenue. The factors mentioned in *Section 1.2.3, Force Majeure* will be relevant in determining the Private Partner's entitlement to relief. However, because MAGA risk is allocated to the Contracting Authority, market practice is that the Private Partner should be kept in the position it would have been in had the MAGA event not occurred.

This principle applies equally in PPP Contracts which do not have a specific MAGA clause, but provide a more general regime for time and/or cost relief for the Private Partner as a result of Contracting Authority acts or omissions.

The PPP Contract typically provides that the Private Partner is granted relief from breach of contract and from its obligations to perform under the PPP Contract to the extent it is affected by the MAGA event (including from the requirement to pay delay liquidated

damages). If the event occurs in the construction phase, the Private Partner will usually be contractually entitled to an extension of time for meeting key dates such as the scheduled date for commencing operations. *See Section 2.3, Sample Drafting 2, Clauses (3)-(5)(b).*

The PPP Contract also often expressly provides that the Private Partner will continue to receive payment from the Contracting Authority under the PPP Contract as if it were still performing, and related deductions under the payment mechanism will be suspended.

The Contracting Authority will typically accept an obligation to compensate the Private Partner for losses and additional costs incurred as a result of a MAGA event. These will include any loss of revenue to the extent the Contracting Authority may not have continued payment since the MAGA event (and financing costs incurred due to any inability to meet payments as a consequence), as well as costs to mitigate and rectify the effects of the MAGA event (i.e. increased PPP Project costs). The Private Partner should still be obliged to mitigate its loss and, as with Force Majeure, its right to relief will be subject to its compliance with its notice and mitigation obligations. *See Section 2.3, Sample Drafting 2, Clauses (5) and (6).*

It may be possible for the Contracting Authority to agree a reduced level of relief entitlement in PPP Contracts which distinguish between “fault” and “non fault” MAGA events. *See Section 2.2.1.2 and Section 2.2.4.*

If the PPP Contract is able to continue, the Contracting Authority may be able to negotiate compensating the Private Partner through tariff increases and/or an extension of the operating period. *See Section 2.3, Sample Drafting 2, Clause (5).*

The procedures to be followed when a MAGA event occurs are similar to a Force Majeure situation. *See Section 2.3, Sample Drafting 2, Clause (4).*

2.2.3 Termination

Similar to the prolonged Force Majeure position, both Parties typically have the right to terminate the PPP Contract if a MAGA event lasts longer than a certain period of time (generally between six to 12 months). *See Section 2.3, Sample Drafting 2, Clause (8).* How this is expressed in the PPP Contract may vary between jurisdictions. In recent PPP Contracts in the Philippines, termination rights are achieved by defining protracted MAGA as a Contracting Authority default. In some jurisdictions, the Contracting Authority may only be entitled to terminate following MAGA-style events by implementing a voluntary termination.

2.2.4 Determining the amount of a MAGA termination payment

Consistent with the allocation of risk for MAGA events to the Contracting Authority, the amount payable to the Private Partner on a MAGA termination is typically similar to the termination payment for a Contracting Authority default. *See Section 8.3, Termination Payments and Section 8.7, Sample Drafting 8, Schedule, Clause (1).*

It may be possible for the Contracting Authority to negotiate differing levels of compensation according to the particular MAGA event. For example, it may be possible to agree to pay the Contracting Authority default termination amount for events where there is clear fault (such as outright expropriation or failure to grant a permit), while agreeing on a lesser amount (for example, still covering at least outstanding debt and contributed equity) for events less obviously within its direct sphere of control and influence. This will depend entirely on the circumstances applicable to the individual PPP Project.

2.3 SAMPLE DRAFTING 2

Definition of Material Adverse Government Action

- (1) For the purposes of this PPP Contract, “Material Adverse Government Action” means any act or omission by the Contracting Authority or any relevant public authority [*define if necessary*] or event set out in Clause (2) below, which occurs during the term of this PPP Contract and which (i) directly causes the Private Partner to be unable to comply with all or some of its obligations under the PPP Contract and/or (ii) has a [*Material*] Adverse Effect] on its [costs or revenues] [*insert defined terms*].
- (2) For the purposes of Clause (1) above any act or omission shall mean and be limited to the following circumstances:
 - (a) failure of any relevant public authority to grant to the Private Partner or renew any permit or approval that is required for the purposes of the Private Partner’s proper performance of its obligations and/or enforcement of its rights under this PPP Contract, in each case within the required timeframe under [Applicable Law], except where such failure results from the Private Partner’s non-compliance with [Applicable Law];
 - (b) any act of war (whether declared or undeclared), invasion, armed conflict or act of foreign enemy, blockade, embargo or revolution, [*occurring inside [name of country]*];
 - (c) radioactive contamination or ionising radiation, [*originating from a source in [name of country]*];
 - (d) any riot, insurrection, civil commotion, act or campaign of terrorism, [*occurring inside [name of country]*];
 - (e) any strike, work-to-rule, or go-slow which is not primarily motivated by a desire to influence the actions of the Affected Party so as to preserve or improve conditions of employment by the Affected Party, [*occurring inside [name of country]*];
 - (f) expropriation, compulsory acquisition or nationalization by any relevant authority of any asset or right of the Private Partner, including any of the shares in the Private Partner;
 - (g) any act or omission of any relevant authority adversely affecting the legality, validity, binding nature or enforceability of this PPP Contract; and
 - (h) [*add any event specific to the PPP Project for which government/Contracting Authority is responsible or has contractually agreed not to do, such as failure to construct planned connecting infrastructure, a government-responsibility pollution event, or construction of unauthorized competing infrastructure (e.g. a free road adjacent to the PPP tolled road)*].

Where possible, undefined materiality qualifications should be avoided to minimize the risk of dispute.

If “material adverse effect” drafting is used it is advisable to define it by reference to a specified monetary impact.

Define Applicable Law with care if also used in other contexts such as change in law – see Section 3.3.

Drafting subject to the position adopted in this respect in the Force Majeure provisions. See Sections 1.4 and 1.5.

See Section 2.2.1.2

Consequences of Material Adverse Government Action

(3) If a Material Adverse Government Action occurs, the Private Partner (i) shall be excused from the performance of its obligations under the PPP Contract to the extent that it is prevented, hindered or delayed in such performance by reason of the Material Adverse Government Action and (ii) shall be entitled to compensation under this PPP Contract, in each case subject to and in accordance with the provisions of this Clause [whole clause].

(4) To obtain relief pursuant to Clause (5) below, the Private Partner must:

(a) as soon as practicable [and in any event within [●] business days] after the Private Partner becomes aware that the Material Adverse Government Action has occurred, give to the Contracting Authority a notice of its claim for payment of compensation and/or relief from its obligations under the PPP Contract, following which the Parties shall consider in good faith any option to mitigate the impact of the Material Adverse Government Action;

Insert reasonable time period, e.g. seven business days.

(b) within [●] business days of receipt by the Contracting Authority of the notice referred in Clause (4)(a) above, give full details of (i) the Material Adverse Government Action and (ii) any Estimated Change in Project Costs and/or loss of revenue claimed and/or delay and/or any breach of the Private Partner's obligations under this PPP Contract; and

Insert reasonable time period given the level of detail required to be specified in full.

(c) demonstrate to the Contracting Authority that:

(i) the Private Partner could not avoid such occurrence or consequences by actions which it might reasonably be expected to have taken without incurring [material] costs;

(ii) the Material Adverse Government Action was the direct cause of the Estimated Change in Project Costs and/or loss of revenue and/or delay and/or breach of the Private Partner's obligations under this PPP Contract;

(iii) time lost and/or relief from the obligations under the PPP Contract claimed, could not be mitigated or recovered by the Private Partner; and

(iv) the Private Partner is using reasonable endeavors to perform its affected obligations under the PPP Contract.

(5) If the Private Partner has complied with its obligations under Clause (4) above, then the Contracting Authority shall:

(a) compensate the Private Partner for the Estimated Change in Project Costs as adjusted to reflect the actual costs reasonably incurred [*and loss of revenue*];

(b) give the Private Partner such relief from its obligations under this PPP Contract as is reasonable for such Material Adverse Government Action; and

Drafting to reflect whether the Contracting Authority has continued paying the Private Partner through this process.

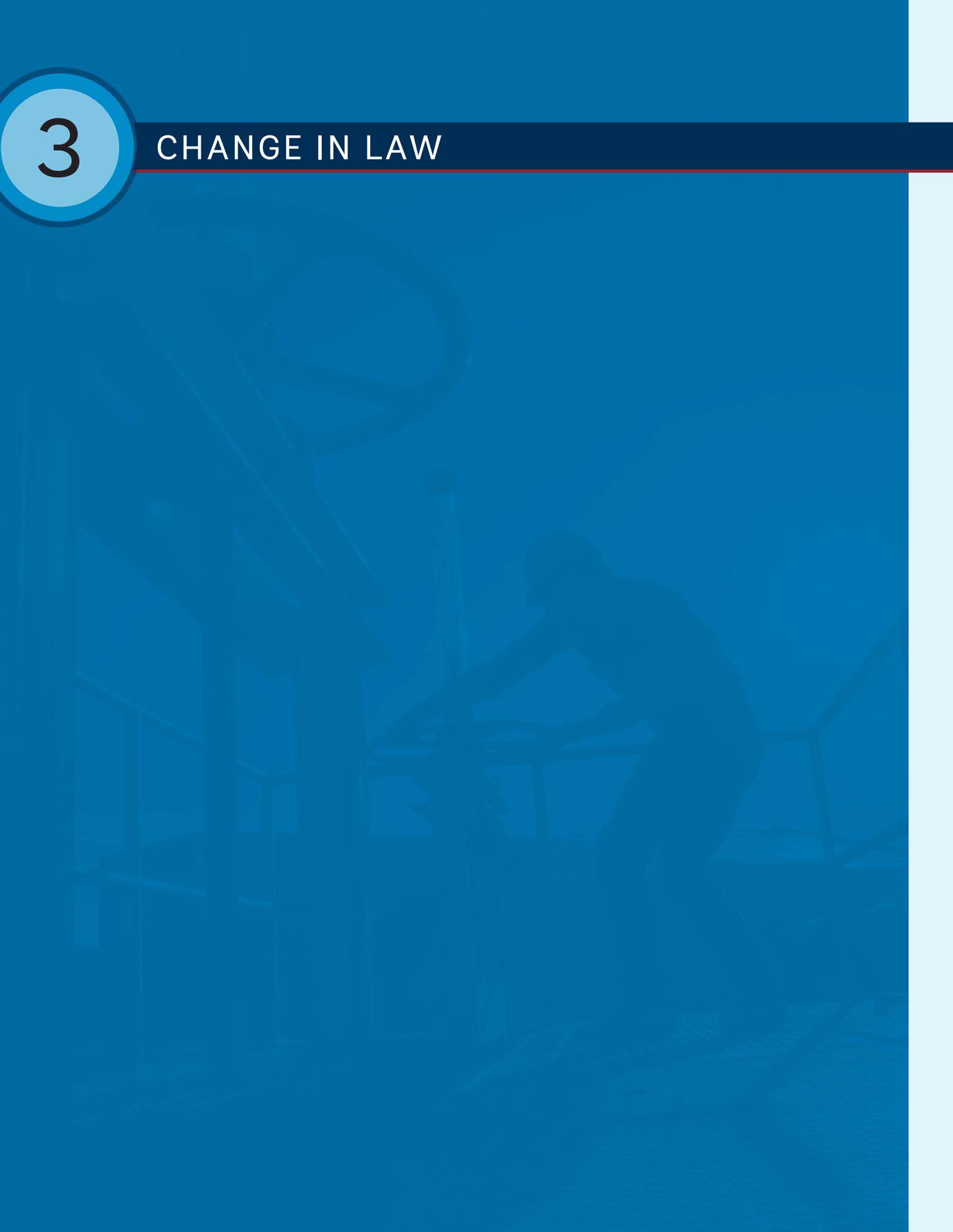
- (c) if the Material Adverse Government Action occurs during the [*insert defined term for Construction Period*] and causes a delay in achieving the [*insert defined term for scheduled services commencement date*], such date shall be postponed by such time as is reasonable
- (6) [In the event that information is provided after the dates referred to in Clause (4) above, then the Private Partner shall not be entitled to any extension of time, compensation or relief from its obligations under this PPP Contract in respect of the period for which the information is delayed.]
- (7) If the Contracting Authority and the Private Partner cannot agree on the extent of any compensation, delay incurred, or relief from the Private Partner's obligations under this PPP Contract, as applicable, or the Contracting Authority disagrees that a Material Adverse Government Action has occurred, the Parties shall resolve the matter in accordance with Clause [*insert reference to dispute resolution clause*].

Termination due to Prolonged Material Adverse Government Action

- (8) If a Material Adverse Government Action subsists for a continuous period of more than [*180-360 calendar*] days, a Party may in its discretion terminate this PPP Contract by issuing a written termination notice to the other Party which shall take effect [*thirty (30) calendar*] days after its receipt. [If, at the end of this [*thirty (30) calendar*]-day period, the Material Adverse Government Action continues,] the PPP Contract shall be terminated pursuant to Clause [*insert reference to clause governing termination*] and the Private Partner shall be entitled to the compensation set out under Clause [*insert reference to Compensation on MAGA termination clause*].

3

CHANGE IN LAW



3.1 KEY ASPECTS

3.1.1 *The concept of change in law*

All contracting parties must operate within the law and so must factor the cost, time and any other implications of complying with applicable law into the performance of their contractual obligations. Over a long-term contract, changes in law may be introduced which were unanticipated at the outset of the contract. These changes may take different forms, such as the implementation of new or amended statutes or the introduction of mandatory codes of practice or new binding case law, and will vary across jurisdictions according to the applicable legislative framework. Changes in law can make performance of a contract more costly, difficult or even impossible under its original terms. How contracts treat such consequences of changes in law will depend on a number of factors, in particular how pricing is fixed under the contract and the length of the contract term.

3.1.2 *Why do PPP Contracts contain change in law provisions?*

In PPP, the Private Partner will typically be expressly obliged under the PPP Contract to comply with all applicable law. It assesses how it will carry out its obligations and what price it will charge based on detailed due diligence of the circumstances known to it at the time of bidding, including the existing legal environment. Any risks or uncertainties will attract an appropriate level of contingency pricing.

An unexpected change in law may make the Private Partner's performance of its contractual obligations easier or less costly, or may make it wholly or partially impossible, delayed or more expensive. Through no fault of its own it may find itself in breach of contract, as well as being unable to earn its expected income and also required to incur additional costs to comply with the change. Some changes in law could, for example, entail significant expenditure if additional capital works are required (e.g. to meet new safety or environmental standards – including legislation in relation to climate change – or to provide mandatory disabled access) and may also reduce full performance of the service while implemented. Similarly, additional taxes may be levied.

Without specific contractual provisions, unless relief is available through non-contractual legal doctrines under the relevant governing law, change in law risk would lie entirely with the Private Partner because it has contracted to provide a specified service at a specified price, and the scope of its obligations and its pricing can only be changed in accordance with the PPP Contract.

CIVIL AND COMMON LAW DIFFERENCES

In common law jurisdictions, without express contractual provisions, change in law risk would typically lie with the Private Partner as outlined above. In civil law jurisdictions, Private Partners may sometimes rely on underlying legal principles such as hardship provisions which give relief from adverse financial consequences of certain circumstances (*see Section 1.1.3, Force Majeure*). However, widespread market practice across civil and common law jurisdictions has shown that the private sector is unwilling to enter into PPP Contracts on such a basis as both Lenders and Equity Investors require express contractual certainty in relation to the potentially significant impact of changes in law.

It is market practice for PPP Contracts in both civil and common law jurisdictions to contain provisions expressly allocating the risk of certain changes in law which occur after a specified date (typically linked to when the Private Partner's pricing is set) and which satisfy certain criteria as regards foreseeability. They also address how the consequences of changes in law are to be managed. Change in law provisions generally provide the Private Partner with relief from contractual breach to the extent compliance with the new law affects the Private Partner's ability to perform its obligations and also set out how any resulting costs of compliance or necessary changes to the PPP Contract scope are treated. Treatment may vary depending on the type of change in law and the PPP Project circumstances.

Contractual change in law provisions do not (and cannot) prevent changes in law, enactment of which is the prerogative of the relevant governing entity. They do not prevent governments from implementing changes in law during the life of the PPP Contract, for example, to meet national/international commitments as regards the environment, human rights or climate change. What the contractual provisions do is address the commercial consequences of such changes, for the reasons outlined above and discussed further in this *Section 3*.

As change in law may also benefit the Private Partner, change in law clauses are often reciprocal, to ensure the Contracting Authority benefits from the "positive" financial consequences of a legislative change. *See Section 3.3, Sample Drafting 3, Clause 1(d)–(f) and Clause (3)(c) and Section 3.4, Sample Drafting 3A, Clause 1(d)–(f) and Clause (3)(c)*.

3.1.3 Relationship to other provisions

EMERGING AND DEVELOPED MARKET DIFFERENCES

As mentioned in *Section 2.1.3, Material Adverse Government Action*, some PPP Contracts include change in law as a MAGA event (as is the case in recent PPP Contracts in the Philippines). This may be appropriate if the treatment agreed for this form of political risk is the same as for other MAGA events, as may be more common in less established markets where legislative change may be a real risk factor. However, it is generally recommended that change in law is addressed in a separate provision, particularly in jurisdictions where the consequences are unlikely to lead to termination or where the provisions involve a detailed approach to risk allocation (e.g. in established markets). In any event, there should be no duplication of treatment under different clauses for the same type of event.

Another approach is to have a separate change in law clause, but to have the associated compensation/relief provisions in another clause which provides a single mechanic applicable to various risks for which the Contracting Authority is responsible. This approach is seen, for example, in Australia, the Netherlands and in certain United States markets where change in law and certain other defined events (sometimes called “Compensation Events”) typically entitle the Private Partner to the same type of relief (namely both cost reimbursement and extensions of time)⁶⁷. *See also Section 1.1.3, Force Majeure and Section 2.1.3, Material Adverse Government Action.*

As change in law may also affect the scope of the service provided, it is advisable for the PPP Contract to contain a mechanism by which the Parties can discuss and negotiate such matters and implement such variations as are necessary. To avoid duplication, this is typically achieved by using the variation procedure usually included to cater for changes in scope which may be proposed by the Parties during the ordinary course of the PPP Contract.

3.1.4 Change in law and related Project Agreements

As with other provisions in the PPP Contract, the treatment of change in law under the Project Agreements should ensure the Private Partner is not obliged to give its sub-contractors more protection than the Private Partner is entitled to under the PPP Contract. *See Sections 1.1.4, Force Majeure and 2.1.4, Material Adverse Government Action.*

3.2 KEY CONSIDERATIONS FOR THE CONTRACTING AUTHORITY

There are a number of factors to take into account for any Contracting Authority negotiating change in law provisions.

3.2.1 Understanding market practice

Contracting Authorities may at first resist the idea of granting change in law protection to Private Partners which is unavailable to other businesses and investors in the same country on the basis that it seems preferential and those other parties appear to accept and manage the risk. However, as described above and set out in more detail below, there are a number of reasons why such protection is justifiable in PPP procurement where the key aim is to procure long-term private sector financing for infrastructure, including from international participants.

3.2.1.1 Lack of pricing flexibility – Unlike other businesses which can pass on increased costs to their customers or can take a view on the risk because their contracts are usually much shorter term, the Private Partner will not typically have the same flexibility. It will have priced its proposal to perform the PPP Contract on the basis of the legal framework in effect at the time of pricing and the PPP Contract will typically contain an agreed pricing formula in both the “user pays” and “government pays” payment models (*see Section G, PPP Contracts in Context*) which will limit the ability to increase pricing. Although these formulae will typically incorporate some form of indexation which will reflect general cost inflation, indexation will not compensate for significant costs (such as capital expenditure) arising from changes in law. The Private Partner will therefore be unable to recover these unless they are expressly addressed under the PPP Contract.

⁶⁷ This is part of the approach described in the footnote to *Section 1.1.3, Force Majeure*.

Even if the payment mechanism is a “user pays” toll or tariff where arguably costs could be passed on to the users of the facility, as highlighted in [Section 1, Force Majeure](#), the Contracting Authority is likely to want to place contractual constraints on any price increases for public policy (and customer protection) reasons. Another factor against simply increasing the toll or tariff is that significant price increases could undermine users’ desire for the service and result in lower PPP Project revenues than forecast by the Private Partner in its Original Base Case. The ability to impose increases will also be influenced by the level of demand and the nature of the project – for example, if it is effectively a monopoly service (such as a port or airport) in a particular area.

3.2.1.2 Bankability – The starting point for the Private Partner and its Lenders will be that change in law is a form of political risk that it cannot control or manage and should therefore be expressly allocated to the Contracting Authority under the PPP Contract. Even if the Contracting Authority is not directly responsible for the change in law, the Private Partner will argue (with some justification) that as an arm of government it is fair and more appropriate for the Contracting Authority to bear the risk⁶⁸.

EMERGING AND DEVELOPED MARKET DIFFERENCES

The allocation of change in law risk is a key bankability point and will be particularly relevant in jurisdictions where changes in law are less predictable or more likely due to underdeveloped or less stable legal or regulatory frameworks.

3.2.1.3 Cost to the Contracting Authority – Even if the Private Partner and its Lenders are willing to accept the risk of adverse changes in law over the long life of the PPP Contract, this risk will need to be priced into the contractual price (or tariff). Not only is pricing this risk likely to be a difficult exercise, but the Contracting Authority (or users) may then end up with an unnecessarily expensive PPP Contract if the risk never materializes.

From the Contracting Authority’s perspective, it should be able to obtain a lower priced service from the Private Partner the more change in law risk it accepts as the Private Partner in turn should be able to reduce its contingency pricing. This needs to be weighed against any perceived benefit of transferring change in law risk to the Private Partner – which should include assessing the risk that a drastic change in law may leave the Private Partner financially unable to continue to provide the relevant infrastructure in accordance with the PPP Contract or even unable to obtain financing and sign the PPP Contract at all.

The Contracting Authority should also bear in mind that change in law provisions may also address circumstances where a change in law has a beneficial effect on the Private Partner’s ability to perform and/or its costs, in which case the Contracting Authority should also benefit (for example, if a costly health and safety legal requirement is reduced or lifted).

⁶⁸ See the Global Infrastructure Hub’s PPP Risk Allocation Tool 2019 Edition – e.g. the Regulatory/Change in Law entries in its risk matrices. [See link in Appendix A, Additional PPP Resources.](#)

3.2.2 Defining what qualifies as “change in law”

Although a degree of change in law protection will almost always be required, Contracting Authorities should carefully consider the scope of change in law provisions. The starting point is to define “change in law” by agreeing (a) what is law (often termed “Applicable Law”), (b) what constitutes a change in that law, (c) the qualifying date after which such change must have occurred, and (d) foreseeability criteria before that date (i.e. if it was “in the public domain”). These elements are discussed below.

3.2.2.1 Applicable Law – The Contracting Authority and its legal advisers will need to carefully consider the definition of “Applicable Law” and how it ties in with other definitions in which it is incorporated (in particular the definition of “change in law”). The definition will depend on the relevant country as the way laws are implemented varies across jurisdictions. The key principle is that it should be limited to obligations with which the Private Partner must legally comply, including:

- legislation (which must itself be clearly defined);
- case law to the extent that it constitutes binding precedent (for example in some common law jurisdictions);
- binding judicial or administrative orders or decrees;
- international human rights or environmental treaties that are directly applicable in the respective jurisdiction or have been incorporated into its national law;⁶⁹
- mandatory industry guidelines with which the Private Partner is bound to comply under the PPP Contract; and
- international conventions (for example, in sectors heavily regulated by international treaties, such as airports). The Contracting Authority will need to consider whether it is appropriate for these to qualify, as well as the likely impact of change on the Private Partner. [See Section 3.3, Sample Drafting 3, Required Definitions, “Applicable Law” definition.](#)

The definition of Applicable Law may encompass tax law although this may alternatively be included as a separate limb in its own right. The definition should not include governmental approvals or permits which should be treated separately in the PPP Contract, except to the extent the terms of such approvals or permits are incorporated in specific legislation and therefore subject to potential change in law. [See Section 2.2.1.2.](#)

Contracting Authorities will want to consider excluding specific legislation, such as environmental legislation linked to recycling, renewable energy or climate change measures, or social legislation linked to human rights. This may be justified to the extent such changes would also impact commercial and other private sector contracts. However, measures to tackle the effects of climate change on PPP Projects could, for example, require costly capital expenditure to retrofit which the Private Partner may have no way of absorbing, so the approach in this regard is likely to depend on the nature of the change and may require a bespoke or nuanced approach (see, for example,

⁶⁹ If the Parties agree the Private Partner should comply with institutional or industry standards or principles which are not legally binding, the PPP Contract would typically specify the relevant version to be complied with, e.g. the version in effect at the bid submission (or contract signature) date. Any changes would not usually fall under change in law or be required to be complied with.

Sections 3.2.3.2 and 3.2.3.3). The Contracting Authority will want to strike a balance between, on the one hand, incentivising the Private Partner to design and implement the PPP Project in accordance with best practice, to use best available techniques and to anticipate future developments, and, on the other hand, avoiding pricing going up to include contingency pricing for too many unforeseeable and uncontrollable legislative developments, which may ultimately never happen. Consideration of these important issues is critical as part of the Contracting Authority’s feasibility studies and tender documentation preparation and the Contracting Authority will need to be mindful of its national and international commitments as regards these matters. *See Section L, Section M and Section N, PPP Contracts in Context.*

3.2.2.2 Change in Applicable Law – Changes will be defined by reference to the qualifying elements of Applicable Law. In some jurisdictions, a change in interpretation of Applicable Law could also have a major impact on the Private Partner’s ability to deliver and operate a PPP Project even though the Applicable Law itself has not changed, so the definition of a change should take this into account.

CIVIL AND COMMON LAW DIFFERENCES

Depending on the jurisdiction, it may be appropriate for the definition of change in law also to include any modification in the interpretation or application of any Applicable Law. This is particularly likely in common law jurisdictions. *See Section 3.3, Sample Drafting 3, Required Definitions, “Change in Law” definition.*

3.2.2.3 Qualifying Date – The Private Partner is expected to have conducted thorough due diligence of the legal framework in determining its pricing and ability to perform its obligations under the PPP Contract. Accordingly, change in law should only include changes which were not “in the public domain” during the period when the pricing was developed and then submitted. This date is key and will usually be no later than the bid submission date. A later date may be appropriate if the Private Partner has had the opportunity to amend its pricing before signing the PPP Contract to take into account any changes in law in the interim period. This will be particularly relevant where there is a long period between bid submission and contract signature. In the absence of a bidding process, an appropriate date will similarly need to be identified (and may be the date final pricing is submitted or the date of contract signature). As pricing is not developed overnight, it is customary in some jurisdictions for this date to be set at six weeks prior to submission of pricing so as to permit pricing to be determined on a clear basis. *See Section 3.3, Sample Drafting 3, Required Definitions, “Change in Law” definition, reference to “Setting Date”.*

3.2.2.4 Awareness of change – Classifying what changes in law are “in the public domain” at the relevant time will need to be looked at on a case-by-case basis because the legislative process varies from one jurisdiction to another. The basic principle as regards legislation is that anything enacted in draft form as at the relevant pricing date qualifies as being in the public domain, so would not constitute a change in law under the PPP Contract once enacted. It may in some circumstances be appropriate to use other “foreseeability” criteria – these should be as objectively ascertainable as possible. If there is a particular concern or uncertainty in relation to the effect of a proposed change in law on the Private Partner’s obligations under the PPP Contract (e.g. in relation to its timing of enactment or actual scope), this can be addressed

specifically in the PPP Contract. For example, the Parties may want to specifically address changes anticipated in relation to national or international governmental commitments as regards the environment, human rights or climate change. *See Section 3.3, Sample Drafting 3, Required Definitions, “Change in Law” definition, limb (b).*

3.2.3 Different risk allocation approaches

There are several approaches to allocating change in law risk but the ability for a Contracting Authority to share change in law risk with the Private Partner will depend on the risk of legislative or regulatory volatility in the jurisdiction and sector concerned, as well as the maturity of the market. The extent to which any resulting increased costs can be passed on to third party users will also be relevant. *See Section 3.2.3.4.*

EMERGING AND DEVELOPED MARKET DIFFERENCES

In some Emerging Markets, the Private Partner may expect the Contracting Authority to bear all forms of change in law risk, while in others the Private Partner may accept a certain monetary threshold up to which it accepts any change in law risk.

In more mature markets, the Private Partner is able to accept greater general change in law risk but is likely to expect the Contracting Authority to bear the risk of general changes requiring capital expenditure once the asset is built and operational, as well as the risk of changes which are discriminatory against the Private Partner or the PPP Project or the type of services being provided. Contracting Authorities will need to consider what approach will provide the optimum balance between affordability, bankability and risk transfer.

3.2.3.1 Approach (a): All risk borne by the Contracting Authority – In some markets the Contracting Authority typically bears all the risk of change in law and provides full relief to the Private Partner. This may be the only way that private finance can be raised in its jurisdiction for the bankability reasons mentioned above. As mentioned in *Section 3.2.1.3*, this risk allocation should also enable the Private Partner to offer a more competitive price without the need for contingency pricing.

EMERGING AND DEVELOPED MARKET DIFFERENCES

Although a Contracting Authority may bear all change in law risk at the start of a PPP program, once a track record and/or legal environment is established in its jurisdiction which gives the private sector greater confidence in the stability and predictability of the regime, Contracting Authorities procuring new PPP Projects may be able to explore some risk transfer to the Private Partner. *See Section 3.3, Sample Drafting 3.*

3.2.3.2 Approach (b): Basic risk sharing by the Private Partner – One way in which change in law risk can be allocated between the Private Partner and the Contracting Authority is by setting a minimum cost threshold, generally on a yearly basis, below which the Private Partner will not be compensated. In other words, the Private Partner will only be entitled to compensation to the extent that it is able to demonstrate that the aggregate costs incurred as a result of a change in law exceed the agreed threshold during a specified period in time, e.g. per calendar year. Subject to an appropriate threshold being set, this approach will generally be acceptable to Lenders as it makes

the risk quantifiable. Unlike Approach (c) below, there is no distinction between general and discriminatory changes (although changes in tax legislation would as a rule have to be discriminatory to qualify). This approach has been seen in some recent PPP Contracts in the Philippines and an example is set out in [Section 3.3, Sample Drafting 3](#).

EMERGING AND DEVELOPED MARKET DIFFERENCES

Contracting Authorities will need to consider whether, depending on their jurisdiction, this basic risk-sharing approach constitutes good value for money as it is likely to attract some contingency pricing.

Setting a clear monetary threshold is preferable to the approach seen in some PPP Contracts where “materiality” criteria are included in defining a qualifying change in law but no clear monetary threshold. This does not provide any certainty for the Parties (or the Lenders) and disputes are likely unless it is clearly defined. A sample of this approach is given in [Section 3.3, Sample Drafting 3, Clause \(3\)\(c\)](#) and [Section 3.4, Sample Drafting 3A, Clause \(3\)\(c\)](#).

3.2.3.3 Approach (c): More developed risk sharing – Over the last two decades, a more developed approach to sharing change in law risk has been seen in certain jurisdictions and has become part of standardized contract templates⁷⁰. A version of this approach is set out in [Section 3.3, Sample Drafting 3A](#), and is based on the following risk allocation:

- **Discriminatory Changes in Law** – these are changes in law which are discriminatory because they apply to the PPP Project and not to similar projects, or to the Private Partner and not to other persons, or to PPP operators and not to other parties;
- **Specific Changes in Law** – these are changes in law specifically impacting the provision of services the same as or similar to the PPP Project services or the shareholders of businesses providing such services (the Contracting Authority will want to clearly define the nature of the services);

Discriminatory and Specific Change in Law risk is allocated to the Contracting Authority to address the Private Partner’s concern that laws may be passed that have the effect of singling out itself or private operators of infrastructure in a manner that has an adverse impact on expected equity return. For example, this could be the introduction of a tax or surcharge which only applies to its PPP Project or that is only applicable to its business because it is being operated by the private sector, or the implementation of more significant environmental regulations that are not being imposed on public sector operators of similar assets;

- **General Changes in Law requiring capital expenditure in operating period** – these are general changes in law (i.e. excluding Discriminatory Changes in Law and Specific Changes in Law) which require the Private Partner to incur capital expenditure after construction completion during the operating period. The risk of these changes is also allocated to the Contracting Authority on the basis that, in the jurisdictions where this applies, the view is that this approach offers the

⁷⁰ See the Infra Australia PPP Guidelines and the UK PF2 Guidance and the definition of “Relevant Change in Law” in the Dutch Model.

Contracting Authority better value for money as the Private Partner has no means of absorbing potentially significant costs once the PPP Project is operational and the relevant asset built and may otherwise factor in contingency pricing; and

- **Any other Changes in Law** – these are all other changes in law including those which trigger capital expenditure during the construction period (but excluding the categories above). The risk of these changes is allocated to the Private Partner throughout the duration of the PPP Contract on the basis that the Private Partner is able to manage and absorb any price implications. The ability to pass the risk of changes requiring capital expenditure in the construction phase will, however, depend on the length of the construction period and the predictability of the legal regime. A particularly long period and/or less stable regime may make this unbankable and a different risk allocation might be needed.

EMERGING AND DEVELOPED MARKET DIFFERENCES

Under this more developed risk sharing approach the Private Partner will bear (some of) the general business risk that applies to all businesses. It is considered generally more beneficial to the Contracting Authority, but this approach may not be bankable in every jurisdiction and should be contemplated on a case-by-case basis.

Even in markets using this approach there will be instances where this risk allocation is not fully achievable due to the nature of the PPP Project and the extent to which the applicable legal and regulatory regime is settled.

3.2.3.4 Approach (d): All risk borne by the Private Partner – This is highly unusual and likely to be achievable only in very established, legally stable markets where the Private Partner is legally able to pass on any increased costs to third party users via a toll or tariff (i.e. under the “user pays” model – [see Section G, PPP Contracts in Context and Section 1.2.3.6](#)) and without adverse impact on user demand. Even so, certain events with a change in law effect are nonetheless likely to be dealt with specifically elsewhere in the PPP Contract (e.g. discriminatory actions such as expropriation and other MAGA types of event).

If the PPP Project does allow the Private Partner to transfer the costs of a change in law to its end-users, the protection which the Contracting Authority gives the Private Partner should be more limited.

3.2.4 Relief and Compensation

Relief from breach – The Private Partner should be protected from breach of contract to the extent (a) its performance is prevented or delayed by a change in law it does not bear the risk of and (b) a variation in PPP Project scope is required in order to comply with a change in law (in which case the PPP Contract should include a mechanism for implementing such variation, for example by means of a Contracting Authority requested variation)⁷¹. [See Section 3.3, Sample Drafting 3, Clauses \(1\), \(2\) and \(3\)](#).

⁷¹ In some jurisdictions, due to the type of service involved, the Private Partner may be subject to “public service obligations” under general law which require continuity of service (e.g. in France). Where applicable, the Parties should bear this in mind when drafting/negotiating relief provisions.

Cost compensation – The PPP Contract will need to set out how any compensation to which the Private Partner is entitled is implemented. This will depend on the payment model, but could include:

- (a) an increase in the availability payment paid by the Contracting Authority;
- (b) a permitted increase in the toll or tariff paid by the end-users;
- (c) reducing any fees payable by the Private Partner (as applicable);
- (d) a lump sum payment by the Contracting Authority to the Private Partner; or
- (e) an extension to the term of the PPP Contract.

Extension of time for performance – If the event occurs in the construction phase, the Private Partner will usually be contractually entitled to an extension of time for meeting key dates such as the scheduled date for commencing operations, to the extent any delay is attributable to the change in law.

For background to the above *see Section 1.2.3, Force Majeure and Section 3.3, Sample Drafting 3, Clause (3)(c) and Section 3.4, Sample Drafting 3A, Clause (3)*. As mentioned above, change in law relief and compensation may also be addressed under separate Compensation Event clauses (with their own applicable thresholds and caps).

Mitigation – The Private Partner should be required to mitigate any costs or delays it incurs associated with the change in law. *See Section 3.3, Sample Drafting 3, Clauses (2) and (3)*.

3.2.5 Termination

The Parties should determine whether, and in which circumstances, the occurrence of a change in law could allow the affected Party to terminate the PPP Contract.

CIVIL AND COMMON LAW DIFFERENCES

In civil law jurisdictions it is common to have a specific termination event where performance of the PPP Contract would entail a breach of law that cannot be remedied by a Contracting Authority variation.

This is not usually seen in common law jurisdictions with established legal frameworks as the Private Partner and its lenders are able to take a view that it is highly unlikely that a change in law would result in such drastic consequences without means of holding the government accountable.

If termination provisions are considered necessary, similar reasoning applies as for Contracting Authority default and MAGA, resulting in the same compensation scheme. *See Section 3.3, Sample Drafting 3, Clause (5) and Section 3.4, Sample Drafting 3A, Clause (5) and Section 8, Termination Payments and Section 8.7, Sample Drafting 8, Schedule, Clause (1)*.

3.3 SAMPLE DRAFTING 3

OPTION 1: Protection Against All Changes in Law

Required Definitions

<p>"Applicable Law"</p>	<p>means any [decree, resolution, law, statute, act, decision, ordinance, rule, directive (to the extent having the force of law), order, treaty, code or regulation or any interpretation of the foregoing by a relevant authority having jurisdiction over the matter in question, as enacted, issued or promulgated by any relevant authority, in each case applicable case applicable in [insert jurisdiction in which the PPP Project is located]; [Drafting to be adapted for the relevant jurisdiction – any reference to amendments, modifications, extensions, replacements or re-enactments must not cut across Change in Law definition].</p>
<p>"Change in Law"</p>	<p>means, after the [Setting Date,] any of the following events:</p> <ul style="list-style-type: none"> (i) the enactment of any new Applicable Law; (ii) the repeal, modification or re enactment of any existing Applicable Law; and/or (iii) a change in the interpretation or application of any Applicable Law, <p>which</p> <ul style="list-style-type: none"> (a) adversely affects (x) the ability of a Party to comply with its obligations under the PPP Contract or (y) [the Base Case Equity IRR]; and (b) was not [published as a draft law] in the [insert applicable publication source for legislation] or in effect at the Setting Date [Adapt as appropriate for “in the public domain”].
<p>"Estimated Change in Project Costs"</p>	<p>means the aggregate of any estimated increase in construction costs, operating costs and financing costs less the aggregate of any estimated reduction in construction costs, operating costs and financing costs.</p>

This date could be a period of time before bid submissions but is usually no later than the bid date. See discussion under Section 3.2.2.3.

Definition and limbs (i)–(iii) and (b) will need to tie in with the definition of Applicable Law to avoid argument or circularity and will also need to reflect the law making process in the relevant jurisdiction.

Occurrence of a Change in Law

- (1) If a Change in Law occurs or is shortly to occur, then any Party may, within [thirty (30) business] days starting from the day it was aware (or should have been aware) of the Change in Law, notify the other Party to express an opinion on its likely effects, giving details of its opinion of:
 - (a) any necessary change to the terms of this PPP Contract including any necessary Contracting Authority variation;
 - (b) whether relief from compliance with obligations is required;

The variations process will be dealt with under a different clause.

- (c) whether any deadline under the PPP Contract should be postponed;
 - (d) any (positive or negative) estimated change of revenue that will directly result from the relevant Change in Law;
 - (e) any (positive or negative) estimated change in the costs of the PPP Project that will directly result from the Change in Law; or
 - (f) any capital expenditure that is required or no longer required as a result of a Change in Law.
- (2) As soon as practicable and in any event within [*thirty (30) business*] days after receipt of any notice from the affected Party, the Contracting Authority and the Private Partner shall discuss and agree the matters referred to in Clause (1) above and any ways in which either Party can, if applicable, mitigate the effect of the Change in Law, including, in relation to the Private Partner:
- (a) providing evidence that the Private Partner has used reasonable endeavors (including (where practicable) the use of competitive quotes) to oblige its sub-contractors to minimize any increase in costs and maximize any reduction in costs;
 - (b) demonstrating how any capital expenditure to be incurred or avoided is being measured in a cost effective manner, including showing that when such expenditure is incurred or would have been incurred, foreseeable Changes in Law at that time have been taken into account by the Private Partner;
 - (c) giving evidence as to how the Change in Law has affected prices charged by any similar businesses to the PPP Project; and
 - (d) demonstrating that any expenditure that has been avoided on account of the Change in Law has been taken into account in the amount which in its opinion has resulted or is required under Clause (1)(e) or (1)(f) above,

provided that if the Parties cannot agree on the effects of the Change in Law, the matter shall be referred for determination in accordance with clause [*insert reference to the dispute resolution clause*].

Consequences of a Change in Law

- (3) If the Parties have followed the procedure set out under Clauses (1) and (2) above, then:
- (a) the affected Party shall be excused from the performance of its obligations under the PPP Contract to the extent it is prevented, hindered or delayed in such performance by reason of the Change in Law;
 - (b) if the Change in Law has occurred before the services commencement date, the scheduled services commencement date shall be postponed to take into account the effect of such Change in Law; and

(c) the Parties shall agree on the amount and payment of any compensation to reflect the Estimated Change in Project Costs as adjusted to take into account the actual increase or reduction in costs reasonably incurred as a result of the Change in Law, *[provided that no compensation shall be made in relation to a Change in Law under this clause unless the claiming Party can demonstrate that the aggregate impact of all Changes in Law that have occurred during [insert relevant period in time, e.g. calendar year] exceeds [insert amount]]*.

Delete provision if no materiality threshold is to be included.

(4) If the notice and relevant information are not provided within the period referred to under Clause (1) above, the affected Party shall not be entitled to any compensation or relief from its obligations under the PPP Contract in respect of the period for which the information is delayed.

Termination due to a Change in Law

(5) If a Change in Law:

(a) results in the Private Partner not being able to achieve the *[insert defined term for services commencement date]* within *[●]* months after the *[insert defined term for scheduled services commencement date]*; or

(b) prevents a Party from performing its material obligations under this PPP Contract for a period of *[●]* consecutive days; or

(c) results in performance of the PPP Contract being illegal and such illegality cannot be remedied by a Contracting Authority variation,

(d) either Party may in its discretion terminate this PPP Contract by issuing a written termination notice which shall take effect *[thirty (30) calendar]* days after receipt of such termination notice. If, at the end of this *[thirty (30)]*-day period, the Change in Law continues, the PPP Contract shall be terminated pursuant to clause *[insert reference to the clause governing termination]* and the Private Partner shall be entitled to the compensation set out under clause *[insert reference to Change in Law termination payments clause]*.

3.4 SAMPLE DRAFTING 3A

OPTION 2: Protection against Discriminatory and Specific Changes in Law and Changes in Law in the operating period requiring capital expenditure

Required Definitions (see also definitions in Section 3.3, Sample Drafting 3)

"Capital Expenditure"	means any expenditure which is treated as capital expenditure in accordance with generally accepted accounting principles in <i>[insert Country]</i> from time to time.
"Discriminatory Change in Law"	means a Change in Law, the terms of which expressly <i>[affect][apply to]</i> : (a) the PPP Project and not to similar projects; and/or (b) the Private Partner <i>[or its sub-contractors in their capacity as such]</i> and not to other persons; and/or (c) Parties undertaking PPP Projects and not other persons.
"General Change in Law"	means a Change in Law which is not a Discriminatory Change in Law or a Specific Change in Law.
"Qualifying Change in Law"	means: (a) a Discriminatory Change in Law; (b) a Specific Change in Law; or (c) a General Change in Law which comes into effect during the <i>[insert defined term for operating period]</i> and which involves additional capital expenditure for the PPP Project.
"Specific Change in Law"	means any Change in Law which specifically refers to (i) the provision of <i>[services the same as or similar to the services provided under the PPP Contract – define]</i> and/or (ii) the holding of shares in companies whose main business is providing <i>[services the same as or similar to those provided under the PPP Contract – define]</i> .

Qualifying Change in Law

- (1) If a Qualifying Change in Law occurs or is shortly to occur, then either Party may, within *[thirty (30) business]* days starting from the day it was aware (or should have been aware) of the Qualifying Change in Law, notify the other Party to express an opinion on its likely effects, giving details of its opinion of:
 - (a) any necessary change in the obligations of the Private Partner;
 - (b) whether any changes are required to the terms of this PPP Contract to deal with the Qualifying Change in Law including any necessary Contracting Authority variation;
 - (c) whether relief from compliance with obligations is required, including the obligation of the Private Partner to achieve any contractual deadline and/or meet any contractual performance requirement during the implementation of any relevant Qualifying Change in Law;

The variations process will be dealt with under a different clause.

- (d) any (positive or negative) change of revenue that will directly result from the relevant Qualifying Change in Law;
 - (e) any (positive or negative) estimated change in the costs of the PPP Project that will directly result from the Qualifying Change in Law; or
 - (f) any capital expenditure that is required or no longer required as a result of a Qualifying Change in Law taking effect during the operation period of this PPP Contract.
- (2) As soon as practicable and in any event within [thirty (30) business] days after receipt of any notice from the affected Party, the Contracting Authority and the Private Partner shall discuss and agree the issues referred to in Clause (1) above and any ways in which either Party can, if applicable, mitigate the effect of the Qualifying Change in Law, including, in relation to the Private Partner:
- (a) providing evidence that the Private Partner has used reasonable endeavors (including (where practicable) the use of competitive quotes) to oblige its sub-contractors to minimize any increase in costs and maximize any reduction in costs;
 - (b) demonstrating how any capital expenditure to be incurred or avoided is being measured in a cost effective manner, including showing that when such expenditure is incurred or would have been incurred, Changes in Law at that time have been taken into account by the Private Partner;
 - (c) giving evidence as to how the Qualifying Change in Law has affected prices charged by any similar businesses to the PPP Project; and
 - (d) demonstrating that any expenditure that has been avoided on account of the Qualifying Change in Law has been taken into account in the amount which in its opinion has resulted or is required under Clauses (1)(e) or (1)(f) above,

provided that if the Parties cannot agree on the effects of the Qualifying Change in Law, the matter shall be referred for determination in accordance with clause [insert reference to the dispute resolution clause].

Consequences of a Qualifying Change in Law

- (3) If the Parties have followed the procedure set out under Clauses (1) and (2) above, then:
- (a) the affected Party [*i.e. the Private Partner*] shall be excused from the performance of its obligations under the PPP Contract to the extent it is prevented, hindered or delayed in such performance by reason of the Qualifying Change in Law;
 - (b) if the Qualifying Change in Law has occurred before the services commencement date, the scheduled services commencement date shall be postponed to take into account the effect of such Qualifying Change in Law; and

- (c) the Parties shall agree on the amount and payment of any compensation to reflect the Estimated Change in Project Costs as adjusted to take into account the actual increase or reduction in costs reasonably incurred or obtained as a result of the Qualifying Change in Law, *[provided that no compensation shall be made in relation to a Qualifying Change in Law under this clause unless the claiming Party can demonstrate that the aggregate impact of all Qualifying Changes in Law that have occurred during [insert relevant period in time, e.g. calendar year] exceeds [insert amount]].*
- (4) In the event that the notice and relevant information are not provided within the periods referred to under Clause (1) above, the affected Party shall not be entitled to any compensation or relief from its obligations under the PPP Contract in respect of the period for which the information is delayed.

Delete proviso if no materiality threshold is to be included.

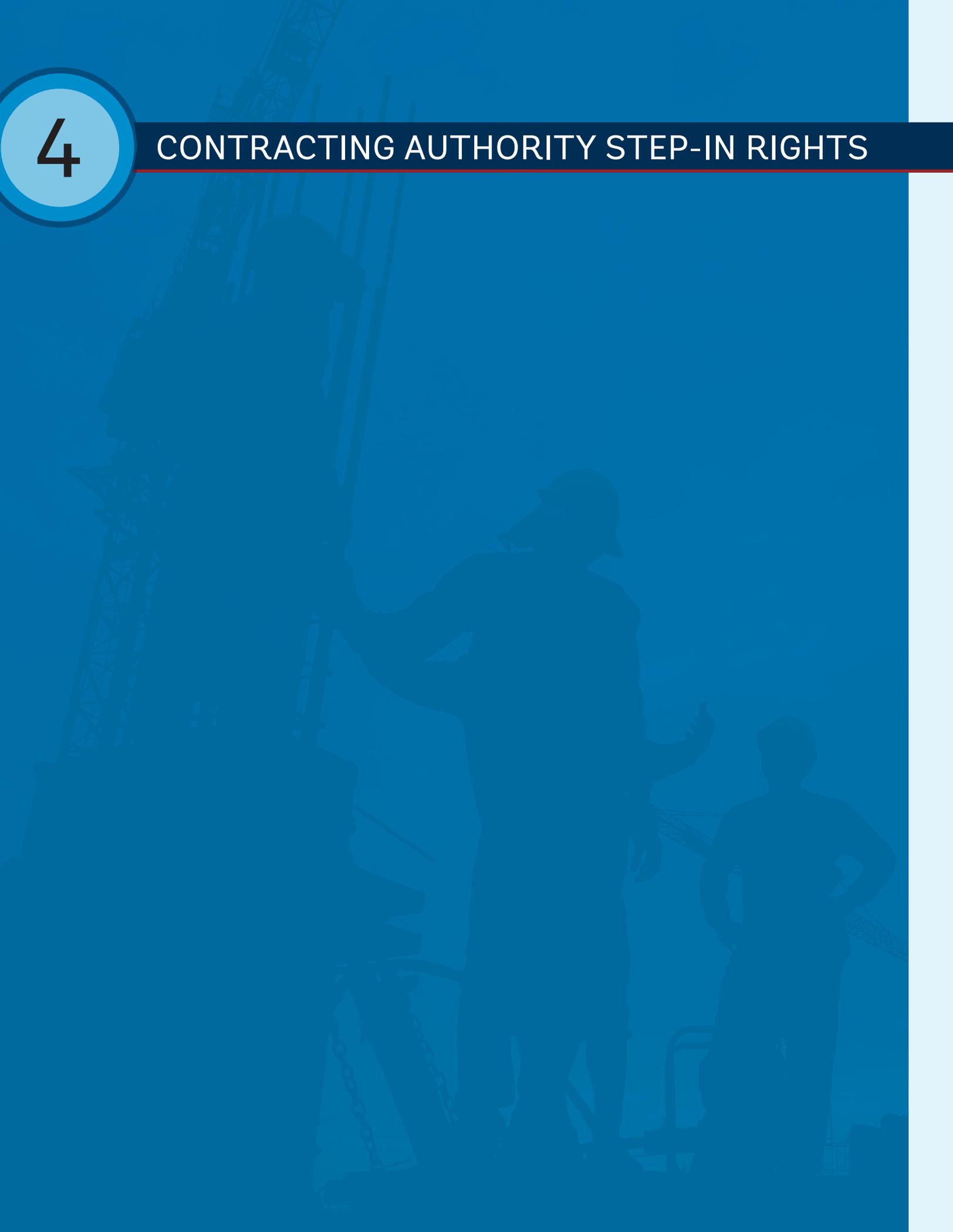
Termination due to a Qualifying Change in Law

- (5) If a Qualifying Change in Law:
 - (a) results in the Private Partner not being able to achieve the *[insert defined term for services commencement date]* within [●] months after the *[insert defined term for scheduled services commencement date]*; or
 - (b) prevents a Party from performing its material obligations under this PPP Contract for a period of [●] consecutive days; or
 - (c) results in performance of the PPP Contract being illegal and such illegality cannot be remedied by [a Contracting Authority] variation,

either Party may in its discretion terminate this PPP Contract by issuing a written termination notice which shall take effect *[thirty (30) calendar]* days after receipt of such termination notice. If, at the end of this *[thirty (30)]*-day period, the Qualifying Change in Law continues, the PPP Contract shall be terminated pursuant to clause *[insert reference to the clause governing termination]* and the Private Partner shall be entitled to the compensation set out under clause *[insert reference to Change in Law termination payments clause]*.

4

CONTRACTING AUTHORITY STEP-IN RIGHTS



4.1 KEY ASPECTS

4.1 *The concept of step-in*

A common description of “step in” in a general contractual context is that it allows one party to “step into the shoes” of another party and exercise rights and, in some cases, carry out contractual obligations in certain circumstances. This could be when the other party is in serious default or where an event has occurred or is subsisting which necessitates such action. Generally, step-in is in respect of private sector obligations and in most cases it would not be legally possible for a private sector party to step into the public sector’s shoes. Step-in is usually for a limited timeframe and the aim is to give the party stepping in the opportunity to manage and rectify the situation without termination of the relevant contract. In some circumstances it may be a third party (such as a Lender or regulator) who is entitled to step into the relevant contract, but a contractual party may also be entitled to step into its counterparty’s shoes in some situations.

This [Section 4](#) sets out the Contracting Authority’s rights under the PPP Contract to step into the shoes of the Private Partner (its counterparty) to carry out certain aspects of the PPP Project. This can be contrasted with [Section 7, Lenders’ Step-in Rights](#) which describes the rights the Lenders have under the Direct Agreement to step into the Private Partner’s (their borrower’s) obligations under the PPP Contract.

4.1.2 *Why do Contracting Authorities have step-in rights under PPP Contracts?*

Circumstances may arise during the life of a PPP Contract where it is appropriate for the Contracting Authority to be able to take swift action itself in relation to the construction works or operating services. Such situations would typically involve some form of genuine emergency and/or threat relating to the structure of the project facility or the works, health and safety or the environment; national security; or where the Contracting Authority has to ensure discharge of a statutory duty (see [Section 4.2.2](#) for further description). This may be as a result of an external event outside the Private Partner’s control or alternatively result from the Private Partner’s significant poor performance and/or breach of its contractual obligations. By stepping in, the Contracting Authority effectively takes over some or all of the Private Partner’s contractual obligations to run the PPP Project for a period with the aim of fixing or managing a short-term serious issue.

In some jurisdictions, the PPP Contract only provides for contractual step-in in a Private Partner breach scenario, in circumstances where the Contracting Authority has a statutory (or equivalent) duty to ensure that the relevant services provided under the PPP Contract are not disrupted. This is often where powers to step-in in other circumstances are provided for under legislation.

While the Contracting Authority may have legislative powers to act in certain emergency scenarios, it is good practice where possible for the Contracting Authority to ensure that it also has the requisite contractual ability to manage the whole or affected part of the PPP Project in the Private Partner's place, whatever the step-in reason. The Parties will also want the PPP Contract to be clear as to the responsibility for step-in costs and any consequent liabilities (although again in some jurisdictions these aspects will be addressed under the relevant legislation).

Contracting Authorities should note that step-in rights may not be appropriate for all types of PPP Project to the full extent outlined in this [Section 4](#) (or even at all). This may be the case, for example, if the Contracting Authority has no relevant operating expertise for a type of PPP Project and there is no scope for finding suitably qualified contractors to assist it. In these projects, the Contracting Authority may instead prefer simply to rely on other contractual provisions (e.g. in relation to Private Partner default or Force Majeure or rights to take specific action if the Private Partner fails to, such as to place required insurances and deduct the cost from amounts due to the Private Partner).

In some jurisdictions, the Contracting Authority may only need step-in rights in certain phases. This depends on the project and sector in question (e.g. in a French motorway project, step-in exists in the construction phase for delayed completion, but not in the operation phase, whereas in a prison project the reverse is true). Conversely, Contracting Authorities may need full contractual step-in rights in PPP Projects involving essential public services and/or the discharge of a statutory duty in order to safeguard provision of the relevant service (e.g. social PPP Projects such as hospitals and prisons). The Contracting Authority should also consider the need for step-in rights where suspension of the service provided may seriously affect government and the general public, (for example, the suspension of road or air traffic, or the blockading of a port, may have a huge impact on the import of essential supplies such as food).

4.1.3 Relationship to other provisions

In some circumstances the event giving rise to step-in may also fall under another contractual provision, such as Force Majeure, MAGA, change in law, Uninsurability or Private Partner default. For example, a Private Partner failure to secure the project site may result in the Contracting Authority stepping in with police/military to expel protestors to protect the site/employees/users. Alternatively, a chemical leak from a nearby industrial site might be categorized as a Force Majeure event and require Contracting Authority intervention to safeguard and clear the site. The step-in provisions will need to dovetail with these provisions in terms of both mechanics and consequences. *See Section 1, Force Majeure, Section 1.3, Uninsurability, Section 2, Material Adverse Government Action, Section 3, Change in Law and Section 6.5, Private Partner Default Termination; and Section 4.2.2, Section 4.2.8 and Section 4.3, Sample Drafting 4, Clause XX.1(e).*

The Contracting Authority should also seek appropriate rights of access under the PPP Contract to enable it to monitor performance and carry out spot checks at the project sites during the contract term. These rights are separate to the step-in rights described in this [Section 4](#) but performance monitoring can be an early indicator of problems which could lead to the need to step in.

4.1.4 Contracting Authority step-in and related Project Agreements

The Contracting Authority's rights to step into the PPP Contract should be reflected in the relevant Project Agreements. The Private Partner must ensure that the counterparties to the Project Agreements (and any other relevant agreements) recognize the Contracting Authority's rights to step in by including appropriate provisions in those agreements (as well as passing down any corresponding financial liabilities). It would also be advisable to include provisions to this effect in any agreement the Contracting Authority enters into with such counterparty directly itself. In addition, some PPP Contracts contain clauses whereby the Private Partner commits to the Contracting Authority having direct access to Sub-contractors and stepping into the Private Partner's rights and obligations under the Sub-contracts; the Sub-contractors agree to this right through the back-to-back Sub-contracts.

4.2 KEY CONSIDERATIONS FOR THE CONTRACTING AUTHORITY

4.2.1 Scope of step-in rights

The ability to step in should always be the Contracting Authority's right but not its obligation and the PPP Contract should set out clearly the terms on which step-in is permitted. The Contracting Authority should not be under any contractual obligation under the PPP Contract, any Project Agreement or its Direct Agreement with the Private Partner's Lenders to remedy any breach or mitigate any risk in respect of which it is stepping in. [Section 4.3, Sample Drafting 4, Clause XX.1\(f\)](#).

The Contracting Authority should have the right of stepping in to take over the whole or the affected part of the project and to take such other steps, including accessing relevant parts of the project, as it reasonably considers necessary in the circumstances. In some jurisdictions, this can include requiring the Private Partner to act or perform its obligations as directed by the Contracting Authority. [Section 4.3, Sample Drafting 4, Clause XX.1\(b\)](#).

Circumstances allowing for step-in are usually limited. This is because step-in by the Contracting Authority (or a third party appointed by the Contracting Authority) can have a significant effect on the Parties' overall rights, obligations and liabilities under the PPP Contract. For example, if the Contracting Authority or its nominee implements a different technical solution for a specific aspect of the PPP Project than the solution planned by the Private Partner, this may impact maintenance and operational risk at a later stage (e.g. if there are interface issues with aspects of its own planned delivery). The Parties will need to agree how such risk will be allocated – the Private Partner may argue that it should not be responsible for the knock-on effects of a third party/ Contracting Authority solution. Generally speaking:

- if step-in is a consequence of the Private Partner's default in the first place, most PPP Contracts allocate full responsibility for the consequences of step-in to the Private Partner;
- if step-in is due to a risk only partially allocated to the Private Partner, interface risk may be shared or may depend on the degree of involvement or effect of the step-in measures; and

- if step-in is not due to the Private Partner, the Contracting Authority will be responsible for the consequences of step-in.

At a project-specific level, considerations around the maturity of the market, the underlying legal framework, precedents regarding step-in and project-specific elements will determine the optimal risk allocation. In France, for example, where contractual step-in is on Private Partner breach only, the Private Partner bears all the cost consequences, sometimes subject to a cap (e.g. 15% of total project price), a limited period (e.g. six months) and possible eventual termination by the Contracting Authority after six to twelve months of step-in. The Dutch model similarly only provides for contractual step-in following a Private Partner default and after a reasonable period, when the Contracting Authority is entitled to remedy the breach itself or through a nominee and may recover the costs (plus a surcharge) from the Private Partner. [Section 4.2.8](#) and [Section 4.2.9](#) describe the market position where the scope of the Contracting Authority's step-in rights is broader than just on Private Partner breach.

To protect the Private Partner, contractual mitigants can include an obligation upon the Contracting Authority to use qualified third parties and/or an obligation to inform and involve the Private Partner during the step-in.

EMERGING AND DEVELOPED MARKET DIFFERENCES

The scope and terms of the Contracting Authority step-in is a key bankability point due to the potential impact on the Parties' rights, obligations and liabilities under the PPP Contract, as outlined above. It will be very relevant in PPP Projects where the Private Partner and its Lenders have particular concerns over the Contracting Authority's potential effect on the delivery of the PPP Project. They may only agree to such rights in sectors and jurisdictions where the Contracting Authority is committed to ensuring continuous delivery of the essential public service and has demonstrable experience in such delivery or where satisfactory mitigation can be agreed (such as a Contracting Authority guarantee or indemnity).

4.2.2 Step-in circumstances

The Contracting Authority may want the ability to step in to avert, mitigate or manage situations including:

- (a) Emergencies – where intervention by the Contracting Authority and the emergency services (e.g. fire, police and – in some cases – the military) is necessary in respect of the type of issues described in [Section 4.2.2\(b\)](#); *See Section 4.3, Sample Drafting 4, Required Definitions, Emergency.*
- (b) Social or environmental risks – where intervention by the Contracting Authority is necessary to protect the health and safety of people (staff, occupants, users or the general public), animals, property (of third parties or the facility/works themselves) and/or the environment (but not in the emergency scenario described in [Section 4.2.2\(a\)](#)); and

- (c) Statutory duty – where the Contracting Authority is under a duty specifically placed on it/government by legislation to ensure provision of certain essential services and, for example, to ensure continuity of service, intervention by the Contracting Authority is necessary if fulfilment of such duty (i.e. through delegation to the Private Partner under the PPP Contract) is at risk.

As highlighted in [Section 4.1.3](#), there may be some overlap between these situations and with other contractual events. [See Section 4.2.6, Section 4.2.8 and Section 4.3, Sample Drafting 4, Clause XX.1\(a\) and \(e\).](#)

The Contracting Authority should only expect the PPP Contract to entitle it to exercise step-in rights where it reasonably believes that it (or a third party it appoints) is better placed to act than the Private Partner and that such action is essential in the circumstances. As mentioned in [Section 4.2.1](#), the scope and terms of the Contracting Authority's step-in rights are key bankability points and the Private Partner will want to ensure that the Contracting Authority's right to intervene is well-defined and limited to essential interventions.

4.2.3 Timeframe of step-in

The time period during which the Contracting Authority steps in will depend on the relevant circumstances but could range from hours to weeks or, in some cases, even longer. It is usually shorter than the period agreed under the PPP Contract in respect of how long Force Majeure (and, if applicable, MAGA) events may subsist before termination rights arise (or, in the case of a Force Majeure (or MAGA) step-in, the same). If Contracting Authority step-in is likely to be for a long-term indefinite period and there is no prospect of step-out, the appropriate approach may well be to take action under the Force Majeure (or MAGA) provisions or other relevant contractual termination processes applicable to the step-in trigger event. [See Section 4.1.3 and Section 4.3, Sample Drafting 4, Clause XX.1\(b\)\(iv\).](#)

4.2.4 Private Partner obligations on step-in

As further described in [Section 4.2.8 and Section 4.2.9](#), the Private Partner may in some step-in scenarios be expressly relieved of its obligations which are affected by the step-in and/or, in some cases, the Contracting Authority may require the Private Partner's performance to be adapted or supplemented. In addition to setting out the Contracting Authority's rights on stepping in, the PPP Contract often also places the Private Partner under a contractual obligation to (a) assist the Contracting Authority when it steps in by providing access rights and resources (including personnel) as reasonably required; and (b) not do anything to hinder the Contracting Authority's legitimate exercise of its step-in rights. [Section 4.3, Sample Drafting 4, Clause XX.1\(c\).](#)

In some jurisdictions (e.g. in states in Australia) the Private Partner irrevocably appoints the Contracting Authority (and its nominees) as its attorney with full power to exercise its step-in rights – this is contained in the security also granted by the Private Partner in favor of the Contracting Authority to secure the exercise of its step-in rights and associated costs. Lenders will also expressly recognize the Contracting Authority's step-in rights in the Direct Agreement and give them priority over their own rights of enforcement and recognize the Contracting Authority's priority in recovering its step-in costs.

As highlighted in [Section 4.1.4](#), the Private Partner must also ensure that the counterparties to the Project Agreements (and any other relevant agreements) are required similarly to cooperate.

4.2.5 Standards on step-in

The Contracting Authority should consider whether it is willing to accept any obligation as regards the standards it must meet when exercising its step-in rights. In some jurisdictions, the Contracting Authority may be obliged to use reasonable endeavors to carry out the PPP Project in accordance with the PPP Contract (e.g. in some states in Australia) and/or to act in accordance with good industry practice when stepping in without Private Partner breach (e.g. the UK). What is reasonable will depend on the circumstances of stepping in and should take into account other relevant rights and duties of the Contracting Authority. [See Section 4.3, Sample Drafting 4, Clause XX.1\(d\)](#). In other jurisdictions, it may be understood under applicable law that the Contracting Authority is liable for performing works and services to an appropriate standard on stepping-in and the Parties may agree that no express contractual provision is required.

4.2.6 Contracting Authority liability for Private Partner losses on step-in

The Contracting Authority should consider the extent to which it is contractually responsible for any liability for losses suffered by the Private Partner as a result of Contracting Authority step-in and be aware of any pricing implications of its position on this risk allocation issue. The position usually differs according to the reason for its step-in (such as whether this is due to Private Partner breach or not as described further in [Sections 4.2.8 and 4.2.9](#)). As highlighted in [Section 4.2.8](#), treatment will also depend on whether the reason for step-in is attributable to an event addressed elsewhere under the PPP Contract (such as Force Majeure – [see Section 1, Force Majeure](#)) – if this is the case, the treatment of such events should conform to the same principles as far as practicable.

In some jurisdictions (e.g. in some EU countries and Australia), the Contracting Authority may not accept any liability when stepping in in a Private Partner breach or Private Partner risk scenario, except in the case of gross negligence in an emergency step-in, fraud or bad faith.

If the Contracting Authority accepts some liability under the PPP Contract, eligible costs, losses and other financial consequences (such as increased costs) should be clearly defined and limited to direct losses (such definition is likely also to apply in other provisions in the PPP Contract) and there should be no double-counting in respect of the Contracting Authority's liabilities.

4.2.7 Insurance

The Parties will want to ensure that the insurances maintained by the Private Partner will respond in respect of losses that could occur during the Contracting Authority's step-in. The Contracting Authority should protect its position by being a co-insured for its own interests (where it has an insurable interest) and requiring its interests to be noted as appropriate on the insurances taken out by the Private Partner. This is likely to be particularly the case for third party liability insurances. The Parties will also want

to ensure that the overall insurance arrangements are not prejudiced by step-in by the Contracting Authority (or its nominee), i.e. that the Contracting Authority actively intervening through step-in does not affect the insurance cover.

4.2.8 Step-in with no Private Partner breach or risk

The main points to note in relation to a step-in which is not triggered by a Private Partner breach or an event for which the Private Partner bears risk, are as follows:

Notice: Prior to stepping-in, the Contracting Authority should where reasonably practicable notify the Private Partner that it plans to step in and the extent and duration of such step-in. If it is not possible to give prior notice (e.g. in an emergency situation), the Contracting Authority should do so as soon as possible. The PPP Contract should set out the requirements for notice and where the Contracting Authority is permitted to step in without notice. *See Section 4.3, Sample Drafting 4, Clause XX.1(b).*

Relief from obligations: The contractual effect of the Contracting Authority stepping-in is typically for the Private Partner to be expressly relieved from performance of its affected obligations. In the Australian model, the Private Partner's rights, as well as its obligations, are usually expressly suspended to the extent necessary to permit the Contracting Authority to exercise its step-in rights. In all cases, no other rights or obligations of the Parties should be affected except those expressly contemplated under the step-in provisions. Any step-in due to a Force Majeure Event will be treated as a Force Majeure Event and relief determined accordingly (a similar approach would apply as regards any MAGA event step-in). *See Section 4.3, Sample Drafting 4, Clauses XX.2(a) and XX.1(e) and Section 1, Force Majeure.*

Compensation/Payment: Where the Contracting Authority steps in for reasons which are not due either to Private Partner breach or to a risk event for which the Private Partner is liable, the basic principle is that the Contracting Authority should compensate the Private Partner in respect of the effects of the step-in to leave the Private Partner in the same position that it would have been had no step-in occurred. As highlighted in *Section 4.2.6*, if the reason for step-in is attributable to events addressed elsewhere in the PPP Contract (such as Force Majeure – see *Section 1*) then the principles agreed in respect of such provisions should apply to the extent practicable and step-in rights should not bypass such provisions. *See Section 4.3, Sample Drafting 4, Clause XX.1(e).*

An example approach in a step-in scenario not triggered by a Private Partner risk event or default is as follows:

- when step-in occurs in the construction phase, the Private Partner is entitled to an extension of time and compensation in respect of its costs and losses;
- when step-in occurs in the operating phase, the Private Partner is entitled to payment in full (i.e. in a “government pays” model, the full availability payment) as if the service had been fully performed by the Private Partner, subject to:
 - deductions for operating cost savings the Private Partner makes during the step-in period;
 - unavailability or performance deductions to be made in respect of parts of the Service still provided by the Private Partner and unaffected by the Contracting Authority's step-in; and

- the Private Partner agreeing to provide reasonable assistance to the Contracting Authority during step-in (provided the Contracting Authority reimburses the Private Partner for any extra costs it incurs). *See Section 4.3, Sample Drafting 4, Clause XX.2(b).*

If the PPP Project involves a “user pays” model or other third party revenue generation, the Parties will need to consider how to calculate compensation in respect of this form of revenue, but this is an issue which will also arise in relation to other types of compensation event. Such compensation is likely to be based on the Original Base Case or revenue generated over a certain time period prior to the step-in.

The mechanics for determining compensation will be similar to those for other “no Private Partner fault” events. Where possible, compensation in these similar circumstances should be addressed under one overarching provision to ensure consistency and avoid unnecessary duplication (see similar point highlighted in [Section 3.1.3](#)). As any step-in due to a Force Majeure Event should be treated as a Force Majeure Event, again any consequences should be determined in accordance with the Force Majeure provisions (the same applies to any MAGA event step-in). *See Section 4.3, Sample Drafting 4, Clause XX.1(e) and Section 1, Force Majeure.*

Indemnity from Contracting Authority: Where step-in is not due to a Private Partner breach or risk event, the Private Partner will want the Contracting Authority to indemnify it for losses to the extent not addressed under the relevant compensation mechanic or other applicable provisions. An indemnity in respect of direct losses is proposed in the UK PF2 Guidance to the extent that the Contracting Authority fails to act in accordance with good industry practice. This is not unreasonable given the principle that the Private Partner should be kept whole as if the step-in had not occurred. Again, eligible costs, losses and other financial consequences should be clearly defined as set out in [Section 4.2.6](#) and the Contracting Authority and its advisers should take care to ensure that any losses it bears are appropriately limited. The Contracting Authority should consider carefully if, and to what extent, it is appropriate for it to accept any indemnity obligation in respect of any later interface costs as described in [Section 4.2.1](#).

Contracting Authority costs: The Contracting Authority should bear all its own costs incurred by stepping-in for reasons other than a Private Partner risk event or breach.

4.2.9 Step-in on Private Partner breach or Private Partner risk event

The main points to note in relation to a step-in due to Private Partner breach or a risk event for which the Private Partner is liable are set out below. Adjustments may be agreed to take into account circumstances where step-in is due to an event for which the Private Partner and the Contracting Authority share the risk (such as, in some projects, vandalism).

Notice: If the Private Partner is in breach of an obligation under the PPP Contract, the Contracting Authority should where feasible notify the Private Partner of such breach and the provisions relating to breach and rectification should first be followed before step-in occurs. *See Section 6.5.5, Termination Events and Section 4.3, Sample Drafting 4, Clause XX.1(b).*

Where this is not practicable in the circumstances, the Contracting Authority should have the right to step in without notice on the same basis as outlined in [Section 4.2.8, Notice](#). Alternatively, if the Private Partner has failed to remedy the breach within the agreed time period, the Authority should have the right to step-in by providing notice as outlined in [Section 4.2.8, Notice](#). See [Section 4.3, Sample Drafting 4, Clause XX.1\(b\)](#).

Relief from obligations: As described in [Section 4.2.8](#), the PPP Contract typically expressly relieves the Private Partner from performance of its affected contractual obligations on Contracting Authority step-in. However, any existing right of the Contracting Authority to terminate for breach by the Private Partner should not be affected. As mentioned in [Section 4.2.1](#) the Contracting Authority should not accept any obligation to rectify the relevant breach. See [Section 4.3, Sample Drafting 4, Clause XX.3\(a\)](#).

Compensation/Payment: To the extent step-in is due to a Private Partner breach or risk event for which the Private Partner is liable an example approach is as follows:

- when step-in occurs in the construction phase, the Private Partner will not be entitled to an extension of time or compensation in respect of its costs and losses (although in some Australian projects the Private Partner will receive time/costs if the event resulted from an act or omission which was in compliance with the PPP Contract).
- when step-in occurs in the operating phase, the Contracting Authority should consider whether the Private Partner ought to be entitled to payment:
 - (a) in full (i.e. in a “government pays” model, to the full availability payment) as if the service had been fully performed (this is the case typically in the UK PF2 Guidance); or
 - (b) in part (i.e. reflecting the Private Partner’s failure to perform the affected obligations) which may result in no payment being due (or a similar result if there are uncapped availability and performance deductions).

In each case, such payment should be subject to (without any double counting):

- deductions for any operating cost savings the Private Partner makes during the step-in period as reasonably estimated by the Contracting Authority;
- deductions for any costs and liabilities incurred by the Contracting Authority (see *Contracting Authority costs* below);
- unavailability or performance deductions to be made in respect of parts of the service still provided by the Private Partner and unaffected by the Contracting Authority’s step-in; and
- the Private Partner agreeing to provide reasonable assistance to the Contracting Authority during step-in at the Private Partner’s cost.

If in the operating phase the deductions applied to the availability payment result in a negative figure, this will be a debt due and payable by the Private Partner to the Contracting Authority (which may be set off against subsequent Availability Payments or other amounts owed to the Contracting Authority, if applicable). See [Section 4.3, Sample Drafting 4, Clause XX.3\(b\)](#).

If the PPP Project involves a “user pays” model or other third party revenue generation, the Parties will need to consider how to calculate payment in respect of this form of revenue. It is likely that this will follow a similar approach to that agreed for a no breach/risk step-in in respect of such revenue, with appropriate reductions/amendments to reflect the breach/risk scenario.

Contracting Authority costs: The Private Partner should be liable for any costs or liabilities the Contracting Authority incurs in stepping in on a Private Partner breach or risk event. Such costs should include the cost of carrying out the works or services, as well as time costs in running the PPP Project. These should be set off against the availability payment during the operating phase (to the extent not already abated), or where this results in a negative amount or step-in is in the construction phase, this will be a debt due and payable by the Private Partner (which may be set off against subsequent Availability Payments or other amounts owed to the Contracting Authority, if applicable). It may be appropriate for the Contracting Authority to require step-in costs to be covered by the Private Partner putting in place a bank guarantee or equivalent (this is seen in some French projects). *See Section 4.3, Sample Drafting 4, Clause XX.3(b).*

Indemnity/liability of Private Partner: In the case of step-in on Private Partner breach or risk event, the Contracting Authority will also want to ensure that any indemnities provided to it by the Private Partner in respect of third party liabilities continue to respond.

The PPP Contract should also address any later issues around interface between solutions implemented during step-in and the Private Partner’s planned delivery solution, as well as any other risks that are allocated to the Private Partner. *See Section 4.2.1.*

4.2.10 Step-out

Whatever the trigger is for stepping-in, the Contracting Authority should always be entitled to “step out” at any time on reasonable notice to the Private Partner and in respect of some or all of the PPP Project. Once the Contracting Authority has served such notice, it should step out in accordance with such notice. The notice period should be the minimum time reasonable for the Private Partner to re-mobilize to resume its contractual obligations. *See Section 4.3, Sample Drafting 4, Clause XX.4(a).*

Some jurisdictions (such as states in Australia) contractually require the Contracting Authority to step out where the relevant risk or event has ceased or has been remedied. Others do not expressly impose this obligation. In any event, where another risk or event has arisen before the Contracting Authority steps out which would otherwise entitle the Contracting Authority to step in, the Contracting Authority should not be obliged to step out.

The effect of step-out is that the Private Partner recommences performance of the affected obligations after the relevant notice period. The Contracting Authority should provide reasonable assistance to facilitate a smooth transition (at the Private Partner’s cost where step-in was for Private Partner breach or risk and otherwise as a Contracting Authority or shared cost). *See Section 4.3, Sample Drafting 4, Clause XX.4(b).*

If step-in was as a result of Private Partner breach and the breach is still subsisting on step-out, the procedure for default rectification and termination must be followed from the point that had been reached prior to step-in. If the Contracting Authority is now entitled to terminate for Private Partner default, this will usually be subject to any rights the Private Partner's Lenders may have under their Direct Agreement with the Contracting Authority. Where step-out leads to termination, it is important that the integrity of the carefully structured contractual termination arrangements is preserved. *See Section 6.1.4, Section 6.5, Private Partner Default Termination and Section 7, Lenders' Step-in Rights.*

In the case of step-in following a Force Majeure Event (or if applicable, MAGA event), the Parties will also have been discussing how best to continue with the PPP Project within the framework of the Force Majeure (or MAGA) provisions and the terms of the Contracting Authority step-in and step-out should reflect and form part of those discussions.

4.3 SAMPLE DRAFTING 4

Required Definitions

“Emergency” means an event causing or, in the reasonable opinion of the Contracting Authority, threatening to cause death or injury to any individual, or serious disruption to the lives of a number of people or extensive damage to property, or contamination of the environment, in each case which prevents:

- (a) the normal operation of the Facility; and/or
- (b) the Service *[to be defined]* operating under normal circumstances;

and, in each case, requires the mobilization of the emergency services.

“Good Industry Practice” means that degree of skill, care, prudence and foresight and operating practice which would reasonably and ordinarily be expected from time to time of a skilled and experienced operator (engaged in the same type of undertaking as that of the Private Partner) or facilities management contractor or building contractor or any Sub-contractor under the same or similar circumstances.

“Private Partner Risk Event” means an event, act or omission for which the Private Partner is wholly or partly responsible under this PPP Contract.

CLAUSE XX

STEP-IN – GENERAL

Contracting Authority Step-in

XX.1

- (a) If the Contracting Authority reasonably believes that it needs to take action in connection with the Service:
 - (i) because a serious risk exists to the health or safety of persons or property or to the environment; and/or
 - (ii) to discharge a statutory duty; and/or
 - (iii) because an Emergency has arisen; and/or
 - (iv) in any other instance where this is required for an [overriding public interest reason];

then the Contracting Authority shall be entitled to take action in accordance with Clauses XX.1(b) to (d) below.

- (b) If Clause XX.1(a) applies, the Contracting Authority may take such action and any consequential ancillary action as it reasonably believes is necessary (together, the “Required Action”) without prior notice to the Private Partner, provided that, where reasonably practicable, it shall notify the Private Partner in writing in advance and in any event as soon as practicable. Such notice shall include the following:

Other defined terms to conform with applicable defined terms used elsewhere in PPP Contract.

Consider defining these services and if includes the military.

Other considerations may be important in some projects, such as those involving national security.

- (i) the action the Contracting Authority wishes to take;
 - (ii) the reason for such action;
 - (iii) the date it wishes to commence such action;
 - (iv) the time period which it believes will be necessary for such action; and
 - (v) to the extent practicable, the effect on the Private Partner and its obligation to carry out the Works and/or provide the Service during the period such action is being taken.
- (c) The Private Partner shall give all reasonable assistance to the Contracting Authority while it is taking such Required Action, including:
- (i) granting such access rights as are necessary and take all action that is necessarily required by the Contracting Authority to assist the Contracting Authority in exercising its rights under Clause XX.1(b);
 - (i) providing sufficient resources, including personnel, to assist the State in exercising its rights under Clause XX.1(b); and
 - (i) not doing anything to hinder, disrupt or prevent the Contracting Authority in exercising its rights under Clause XX.1(b).
- (d) [The Contracting Authority shall use reasonable endeavors to undertake the Required Action in accordance with Good Industry Practice and will endeavor to inform and where possible involve the Private Partner.]
- (e) Where the Contracting Authority has exercised its rights under Clause XX.1(b) as a consequence of an event which is a Force Majeure [or MAGA][other] Event, the exercise by the Contracting Authority of those rights will be a Force Majeure [or MAGA][other] Event and Clause [Force Majeure] [MAGA] [other] shall apply.
- (f) The Private Partner acknowledges and agrees that the Contracting Authority is not obliged to exercise its rights under this Clause XX.1 and, if it exercises its rights under this Clause XX.1 it is not obliged to cure any breach, or to overcome or mitigate the event (or any of the consequences of the event) that gave rise to such exercise.

Reason may include failure to remedy breach.

Timing – see Section 4.2.3.

Consider whether the Contracting Authority should accept this and if so also any liability if it fails to act in this way on a no breach/ no Private Partner risk step in.

Add reference to any other applicable clauses (e.g. uninsurability, change in law) and ensure corresponding risk allocation is consistent. See Sections 4.1.3, 4.2.2, 4.2.6 and 4.2.8.

STEP-IN WITHOUT PRIVATE PARTNER BREACH OR PRIVATE PARTNER RISK EVENT

XX.2 [Subject to Clause XX.1(f)] If the Required Action is not taken as a result of a breach of any obligations of the Private Partner under the PPP Contract and or a Private Partner Risk Event, then for so long as and to the extent that the Required Action is taken and prevents the Private Partner from carrying out any parts of the Works and/or providing any part of the Service:

- (a) the Private Partner shall be relieved from its obligations to carry out such part of the Works and/or provide such part of the Service to the extent the Authority has expressly relieved it from its obligations; and

- (b) in the operating phase, in respect of the period in which the Contracting Authority is taking the Required Action, the [Availability Payment] due from the Contracting Authority to the Private Partner shall equal the amount the Private Partner would receive if it were satisfying all its obligations and carrying out such Works and/or providing the Service affected by the Required Action in full over that period; LESS (without double counting):
- (i) deductions for operating cost savings the Private Partner makes during the step-in period;
 - (ii) unavailability or performance deductions to be made in respect of parts of the Service still provided by the Private Partner and unaffected by the Contracting Authority's step-in;
- (c) in the construction phase, *[drafting to reflect Contracting Authority's agreed liabilities owed to the Private Partner and to cross-reference where applicable to other clauses in the PPP Contract dealing with compensation mechanics for Private Partner no fault events; plus ability to set off]*

The Parties will, to the extent relevant, need to consider how an appropriate forecast for any third party income can be made and any adjustments for a "user pays" project.

Drafting should ensure all applicable deductions and adjustments are addressed here or elsewhere in the PPP Contract as appropriate.

and provided that the Private Partner provides the Contracting Authority with reasonable assistance [in accordance with Clause XX.1(c) (such assistance to be at the expense of the Contracting Authority to the extent incremental costs are incurred that are not already taken into account)].

STEP-IN ON PRIVATE PARTNER BREACH OR RISK EVENT

XX.3 If the Required Action is taken as a result of a breach of any obligations of the Private Partner under the Contract or a Private Partner Risk Event, then for so long as and to the extent that the Required Action is taken, and prevents the Private Partner from carrying out any part of the Works and/or providing any part of the Service:

- (a) the Private Partner shall be relieved of its obligations to carry out such part of the Works and/or provide such part of the Service to the extent the Authority has expressly relieved it from its obligations; and EITHER
- (b) in the operating phase, in respect of the period in which the Contracting Authority is taking the Required Action, the [Availability Payment] due from the Contracting Authority to the Private Partner shall equal the amount the Private Partner would receive if it were satisfying [all its] [its affected] [its unaffected] obligations and providing the Service [affected][unaffected] by the Required Action in full over that period; LESS (without double counting):
 - (i) deductions for any operating cost savings the Private Partner makes during the step-in period as reasonably estimated by the Contracting Authority;
 - (ii) an amount equal to all the Contracting Authority's costs [and losses incurred] in taking the Required Action; and
 - (iii) unavailability or performance deductions to be made in respect of parts of the Service still provided by the Private Partner and unaffected by the Contracting Authority's step-in; OR

Drafting to reflect full/partial payment choice.

Drafting should ensure all applicable deductions and adjustments are addressed here or elsewhere in the PPP Contract as appropriate.

- (c) in the construction phase, *[drafting to reflect Private Partner's agreed liabilities owed to the Contracting Authority and any construction cost savings and to cross-reference where applicable to other clauses in the PPP Contract dealing with compensation on Private Partner fault events; plus ability to set off]*

and provided that the Private Partner provides the Contracting Authority with reasonable assistance [in accordance with Clause XX.1(c) (such assistance to be at the expense of the Private Partner)].

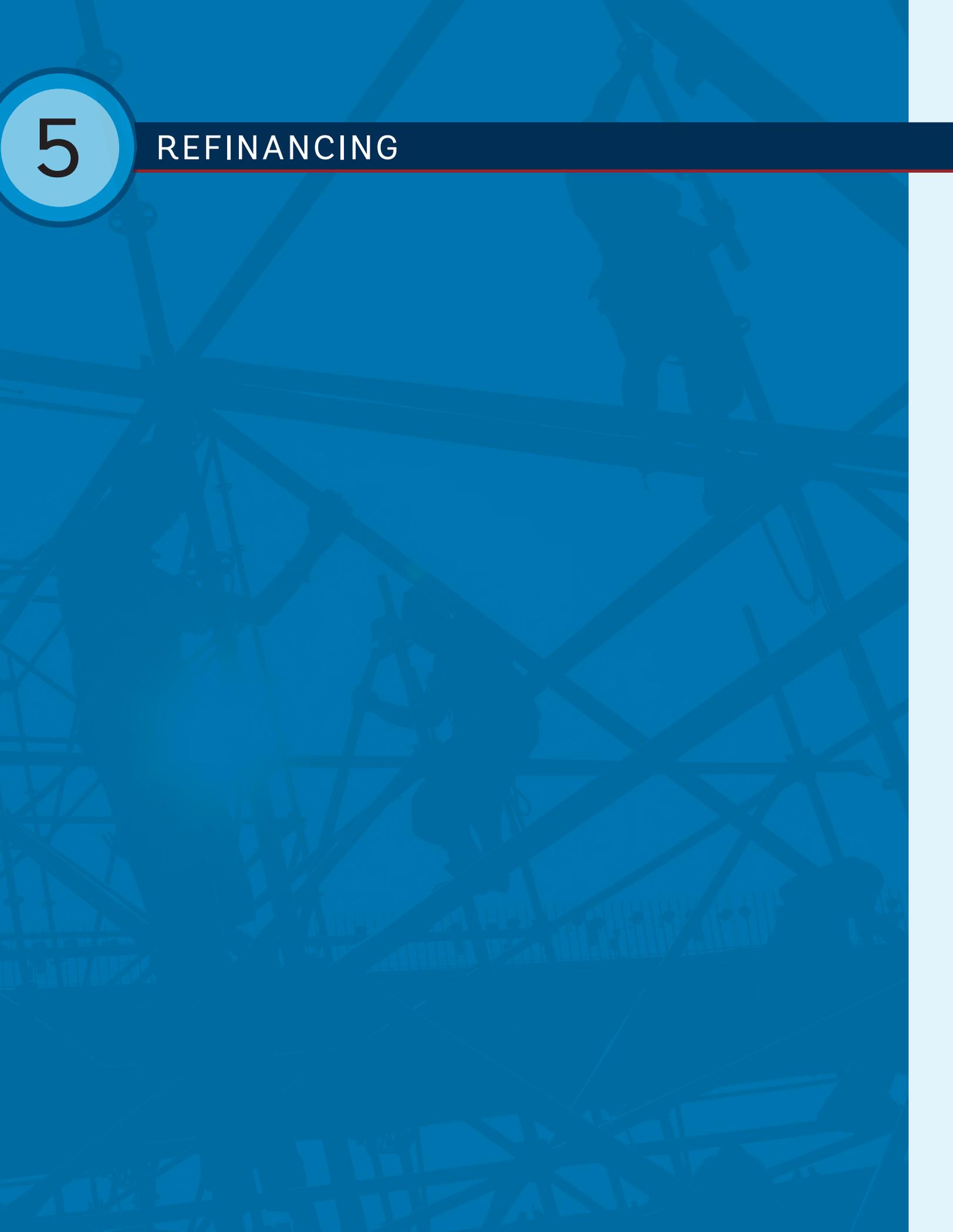
STEP-OUT AND NEXT STEPS

XX.4

- (a) The Contracting Authority may cease to exercise its rights under this Clause XX in whole or part upon giving a minimum of *[five (5)]* Business Days' notice to the Private Partner and shall use reasonable endeavors to provide as much advance notice as is reasonably practicable.
- (b) If the Contracting Authority ceases to exercise its rights under this Clause XX in accordance with Clause XX.4(a), the Private Partner must *[immediately] [within [x] working days]* recommence performing any obligations suspended due to the exercise by the Contracting Authority of those rights and the Contracting Authority must give reasonable assistance to the Private Partner to ensure that the transition is effected as smoothly as possible (at the Private Partner's cost and expense in the case of a step-in as a result of Private Partner breach [or risk event]).

The Parties will, to the extent relevant, need to consider how an appropriate forecast for any third party income can be made and any adjustments for a "user pays" project.

Notice could include details of the action taken or that the Contracting Authority still intends to take and, in the case of a breach that remains unremedied, whether the Contracting Authority intends to serve a rectification/ termination notice, in accordance with Clause [Private Partner default termination Notice and Rectification (see Section 6.6, Sample Drafting 6, Clause YY.1)].

The background of the page is a blue-tinted photograph of a construction site. It shows a complex network of steel beams forming a skeletal structure. Several workers are visible as dark silhouettes, positioned at various heights and working on the framework. The lighting is dramatic, highlighting the geometric patterns of the steel.

5

REFINANCING

5.1 KEY ASPECTS

5.1.1 *The concept of refinancing*

Refinancing means changing or replacing the existing terms on which debt obligations have been incurred. Borrowers may refinance existing debt obligations for a number of reasons and in a variety of ways.

5.1.2 *Why do PPP Contracts contain refinancing provisions?*

Financial terms are agreed between the Lenders, Equity Investors and the Private Partner prior to the PPP Contract becoming effective and will take into account market conditions at the time, as well as the risk profile of the project and applicable jurisdiction. The cost of financing the PPP Project will be passed directly through to the pricing offered to the Contracting Authority under the PPP Contract or the rates charged to users. Given the long-term nature of PPP Contracts, over time there will be changes in market conditions, as well as developments in the project itself, which will affect its risk profile, and the Private Partner may want to change the terms of or replace its financing accordingly. In some jurisdictions it may not even be feasible to put in place long-term financing at the outset and refinancing is therefore a necessity for the Private Partner after the initial funding period.

The result of a refinancing may be that the Private Partner's debt costs are reduced, resulting in greater revenue and in turn a higher equity return – this is typically called “refinancing gain”. The PPP market has increasingly acknowledged that it would not be fair for the Private Partner to enjoy the entire benefit of refinancing gain where it is not entirely responsible for the availability of the improved financing terms. This is particularly important from the Contracting Authority's perspective given the use of public funds to pay for PPP Projects. Any change in financing terms may also impact other provisions in the PPP Contract that reference the financing terms, such as termination payments for which the Contracting Authority may be liable.

Without specific provisions in the PPP Contract, the Contracting Authority will have limited or no ability to share in any refinancing gain received by the Private Partner and the position as regards other contractual terms (such as termination payments) may be unclear. Not all refinancings lead to gains that should be shared, however, and refinancing provisions also typically clarify the circumstances which are exempt.

5.1.3 *Refinancing grounds*

The circumstances in which a refinancing of the PPP Project may be sought by the Private Partner are described below and the differing grounds are likely to necessitate different treatment under the PPP Contract.

Rescue Refinancing – In adverse circumstances a refinancing may be sought to rescue the PPP Project from default. The Private Partner may be in a distressed situation requiring

an increase and/or a rescheduling of their debt repayment obligations. Generally, it will be in the Contracting Authority's and the Private Partner's interests for this form of refinancing to be implemented so that service provision under the PPP Contract can continue and default termination consequences avoided. The Contracting Authority will want to ensure any changes to the financing terms do not adversely affect its contractual position but it should not anticipate any immediate financial benefit.

Mini perm refinancing – In markets where it is not possible (or desirable) to obtain long-term financing, the Private Partner may put in place what is sometimes known as a “mini perm” financing. The loan will have a short tenor (e.g. five or seven years), and there is an incentive on the Private Partner and its Shareholders to refinance because the loan terms may provide that the Lenders will sweep all available cash (after reserve account funding) if no refinancing has occurred by the relevant maturity date (and the Lenders may require gradually increasing cost sweeps (e.g. 25%, 50%, 75%) in the years prior to maturity), or (in the case of a “hard” mini perm) that there will be an event of default⁷². The common position in Australia, for example, is to put in place five to seven-year debt funding, with assumed refinancings every five years through the life of the PPP Project. Given the nature of this financing and that replacement will be a necessity envisaged at the start of the PPP Contract, it will be in both Parties' interests to facilitate a refinancing on acceptable terms and it is unlikely to be driven by or to deliver any significant additional financial benefit. On the other hand, such mini perm arrangements are often sub-optimal from a budget and public spending perspective as the Contracting Authority will not be able to assess the overall whole-life project cost. The availability of long-term committed finding is an important element in the initial assessment as regards opting for PPP or another procurement method.

Bridge to bond financing – Where it is envisaged that initial bank debt financing will be replaced by bond finance, normally after completion of the construction or development phase, this is known as ‘bridge to bond’ financing. Generally, the bridge financing will contain incentives to refinance, such as progressive increases to the margin and a relatively short tenor. [See Section 12, Bond Financing.](#)

Realising Value Refinancing – In other circumstances (which are the focus of this [Section 5](#)), the effect of changed market conditions and PPP Project developments may be positive and the Private Partner may seek to obtain more favorable financing terms to realize more equity return for its Shareholders. Such terms may be available for a number of reasons, such as:

- the market may have greater liquidity and the price of debt may have declined (e.g. after a period of financial crisis or where new lenders want to enter the PPP market);
- as significant risks are considered to arise during the construction period, once the income-generating asset is built and the PPP Project is successfully operational, the risk profile is reduced and the corresponding risk of inability to service debt repayment obligation is perceived to be lower;

⁷² “Hard” mini perm financing structures are not permitted by Contracting Authorities in the Netherlands on the basis that they effectively introduce refinancing risk.

- general market conditions have improved (e.g. the jurisdiction concerned may have established a good track record in successful PPP Projects and/or the regulatory and political framework may be considered more stable); and
- for “user pays” PPP Projects (*see Section G, PPP Contracts in Context*), demand may be stronger than anticipated and revenues therefore higher, resulting in an opportunity to increase leverage.

It is this type of refinancing which is more likely to yield a financial benefit for the Contracting Authority if the PPP Contract is correctly drafted and the Contracting Authority will also want to ensure any changes to the documentation do not adversely affect its contractual position.⁷³

5.2 KEY CONSIDERATIONS FOR THE CONTRACTING AUTHORITY

Refinancing provisions can be complex and will differ between PPP Projects, according to the different financing structures used. Some PPP Contracts will contain detailed drafting (particularly in Developed Markets), whereas others include a much shorter provision designed to bring the Parties together to discuss the implications of a refinancing. In either case, key points to bear in mind are set out below.

5.2.1 Defining “Refinancing”

Establishing a definition which captures all types of potential refinancing can be difficult and the Contracting Authority should aim for a definition which minimizes the potential for circumvention through sophisticated structurings. The recommended approach is to be as generic as possible by reference to the senior finance documents, with a catch-all provision. *See Section 5.3, Sample Drafting 5, Required Definitions, definition of “Refinancing”.*

A definition of “Exempt Refinancing” is sometimes requested by the Private Partner to clarify that certain dealings are not intended to be caught by the relevant refinancing provisions. Again, the Contracting Authority should carefully consider what might be included on a case-by-case basis. For example, in the case of a mini perm financing and a bridge to bond financing, Contracting Authorities should recognize that refinancing is virtually a given so the PPP Contract should envisage this occurrence.

5.2.2 Refinancing gain

The question for the Contracting Authority is what qualifies as refinancing gain and whether all refinancing gain should be shared. As with defining “Refinancing”, care needs to be taken in drafting gain calculation and sharing provisions to minimize the Private Partner’s ability to circumvent the provisions. It is increasingly common, particularly in Developed Markets, for a Private Partner to factor in the benefit of a future refinancing into its Original Base Case so that it can offer a more competitive price to the Contracting Authority in its bid. In this instance, the Private Partner

⁷³ It is also possible to include a provision entitling the Contracting Authority to request the Private Partner to seek terms for a potential refinancing if it feels better financing terms are available (see the *Infra Australia Guidelines*).

would argue that the Contracting Authority is already benefiting from any potential refinancing gain and should therefore not be entitled to a further share of such gain when the refinancing actually happens. While this argument has some merit, the precise basis of any refinancing envisaged by the Original Base Case would need to be clearly agreed upfront to limit the risk of disputes. *See Section 5.3, Sample Drafting 5, Required Definitions, definition of “Refinancing Gain”.*

Similarly, in a rescue or mini perm refinancing the overall effect may not lead to any increase in equity return compared to the Base Case Equity IRR.

In all cases it is generally considered to be fair for the Contracting Authority only to share in gain over and above the Original Base Case. The rationale in a rescue refinancing is that due to the distressed scenario, Lenders are unlikely to agree to any refinancing debt being paid to the Contracting Authority. However, this may not always be justifiable where the Contracting Authority has concerns that the Base Case Equity IRR may have been artificially inflated (e.g. due to weak competition during the bidding process).

EMERGING AND DEVELOPED MARKET DIFFERENCES

In Emerging Markets, particularly for “user pays” PPP Projects (*see Section G, PPP Contracts in Context*), there may be limited scope for the Contracting Authority to negotiate refinancing gain sharing if such gain is a key incentive for potential bidders. This dynamic has been evident in the Philippines, for example, where refinancing provisions are not typically included in the PPP Contract.

5.2.3 Right to consent

The Contracting Authority’s right to consent is important as it is what will bring the Private Partner to the negotiating table. As mentioned above, if a particular refinancing is already factored into, or is as contemplated by, the Original Base Case, then it is reasonable for Contracting Authority consent not to be required or to be subject to fewer constraints than other refinancings.⁷⁴ However, its right to consent should be exercised reasonably. The Contracting Authority should bear in mind that a refinancing resulting in gain is likely to benefit it financially and even a rescue refinancing will help save the PPP Project. Nevertheless, the Contracting Authority should only consent if it is confident that the refinancing will not have a negative impact on the PPP Project or on its own liabilities without providing it with sufficient commensurate benefit. This will include assessing any increase in any termination payments for which it is liable as described in *Section 8, Termination Payments. See Section 5.3, Sample Drafting 5, Clause (3).*

⁷⁴ In some markets in the United States, rescue refinancings that do not result in an increase in the Private Partner’s outstanding debt above a certain percentage threshold may be permitted without the consent of the Contracting Authority, as may refinancings where the Private Partner provides satisfactory evidence that its aggregate debt is no less than a specified percentage of the fair market value of the PPP Contract.

5.2.4 Calculating refinancing gain

A full understanding and sight of existing and proposed financing structures and documentation is needed for the Contracting Authority to be in a position to calculate any refinancing gain and enforce its rights effectively. Expert legal and financial advice should be obtained (to match the advice the Private Partner is likely to be receiving) to ensure the Contracting Authority is not at any disadvantage in analysing the effect of any refinancing proposal. External expenses incurred by the Contracting Authority when considering a refinancing proposal should be borne by the Private Partner and if the refinancing is implemented they should be deducted from the total refinancing gain amount prior to sharing. *See Section 5.3, Sample Drafting 5, Clause (7).*

5.2.5 Share of refinancing gain

The Contracting Authority should consider what an appropriate sharing mechanism is. Equal sharing is one option, or staged sharing depending on the amount of the gain and/or how it arises. The basic premise under the Infra Australia PPP Guidelines is a 50% sharing (as it is in the South Africa PPP Guidelines), but recognizing that more detailed arrangements and greater proportions may be appropriate.⁷⁵ *See Section 5.3, Sample Drafting 5, Clause (4).*

5.2.6 Method of payment

The Contracting Authority should typically have the right to choose the method of payment of its share of the refinancing gain and this will depend on the nature of the refinancing and discussions at the time. Options include the Contracting Authority being paid (a) in a lump sum upon the refinancing to the extent the Private Partner receives such amounts at the time of the refinancing, (b) in a lump sum or periodically at the time of receipt of the relevant payments, or the receipt of the projected benefit (in the case of the “user pays” model), (c) via a reduced availability payment (in the case of the “government pays” model), (d) by reduced user fees (in the case of the “user pays” model) or (e) by a combination of the above (in accordance with the applicable payment model). *See Section 5.3, Sample Drafting 5, Clause (6).*

⁷⁵ The UK PF2 Guidance draws a distinction between gains arising from a reduction in margin under the senior finance documents (where the Contracting Authority expects 90% of the gain) and other gains (where the Contracting Authority shares on a staged basis between 50%-70% according to the size of the gain). A staged sharing percentage of 50%-70% has also become the norm in the Netherlands.

5.3 SAMPLE DRAFTING 5

The principle of sharing refinancing gain has developed over time out of the experience of early PPP markets such as the UK. For a detailed approach see the UK PF2 Guidance and the Infra Australia PPP Guidelines. Sample Drafting 5 is broadly based on concepts they define.

Required Definitions

"Base Case Equity IRR"	means the Equity IRR set out in the Original Base Case.
"Distribution"	means whether in cash or in kind, any: <ul style="list-style-type: none"> (a) dividend or other distribution in respect of share capital; (b) reduction of capital, redemption or purchase of shares or any other reorganization or variation to share capital; (c) payments under any Subordinated Finance Documents; and (d) the receipt of any payment, contractual arrangement, transfer of asset and other benefit which is not received in the ordinary course of business and on reasonable commercial terms.
"Equity IRR"	means the projected blended internal rate of return to the Shareholders and any of their affiliates over the entire PPP Contract period, having regard to Distributions made and projected to be made.
"Exempt Refinancing"	<ul style="list-style-type: none"> (a) any Refinancing fully contemplated in the Original Base Case; (b) a change in taxation or in accounting treatment; (c) the exercise of rights, waivers, consents and similar actions which relate to day-to-day administrative and supervisory matters, and which are in respect of: <ul style="list-style-type: none"> (i) breach of representations and warranties or undertakings; (ii) movement of monies between the project accounts in accordance with the terms of the Senior Finance Documents; (iii) late or non-provision of information, consents or licenses; (iv) approval of revised technical and economic assumptions in relation to the Original Base Case; (v) failure by the Private Partner to obtain any consent by statutory bodies required by the Senior Finance Documents; or (vi) voting by the Lenders and the voting arrangements between the Lenders in respect of the levels of approval required by them under the Senior Finance Documents; (d) any sale of shares in the Private Partner by the Shareholders. (e) [any ordinary market dealings in bonds.]
"Financial Model"	<i>[Or delete and use definition of Original Base Case in Section 8, Sample Drafting 8.7. See definition of Base Case Equity IRR above and where Original Base Case already used in this clause.]</i>

The Private Partner may wish to extend this definition to clarify that changes to certain documents or other types of circumstance will be exempt (e.g. a mini perm refinancing scenario). This should be considered on a case-by-case basis to reflect the particular circumstances of the PPP Project.

"Net Present Value"	means the aggregate of the discounted values, calculated as of the estimated date of the Refinancing, of each of the relevant projected Distributions, in each case discounted using the Base Case Equity IRR.
"Pre-Refinancing Equity IRR"	means the Equity IRR calculated immediately prior to any Refinancing, but without taking into account the effect of such Refinancing and using the Original Base Case as updated (including as to the performance of the PPP Project).
"Qualifying Refinancing"	means any Refinancing that will give rise to a Refinancing Gain greater than zero that is not an Exempt Refinancing.
"Refinancing"	means: <ul style="list-style-type: none"> (a) any amendment, variation, novation, supplement or replacement of any Senior Finance Documents; (b) the grant of any waiver or consent, or the exercise of any similar right under any Senior Finance Documents; (c) the creation of or granting of any form of benefit or interest in the Senior Finance Documents, or the creation or granting of any rights or interest in any contracts, revenues or assets of the Private Partner whether by way of security or otherwise; and (d) any other arrangement having been put in place by any person which has an effect similar to any of (a) to (c) above or which has the effect of limiting the Private Partner's ability to carry out any of (a) to (c) above.
"Refinancing Gain"	<p>means a positive amount equal to $(A-B) - C$, where:</p> <p>A = the Net Present Value of Distributions, as projected immediately prior to the Refinancing (taking into account the effect of the Refinancing and using the Original Base Case as updated (including as to the actual past performance of the PPP Project) so as to be current immediately prior to the Refinancing) to be made to each Shareholder or affiliate over the remaining term of the PPP Contract following the Refinancing;</p> <p>B = the Net Present Value of Distributions, as projected immediately prior to the Refinancing (but without taking into account the effect of the Refinancing and using the Original Base Case as updated (including as to the actual past performance of the PPP Project) so as to be current immediately prior to the Refinancing) to be made to each Shareholder or affiliate over the remaining term of this PPP Contract following the Refinancing; and</p> <p>C = any adjustment required to raise the Pre-Refinancing Equity IRR to the Base Case Equity IRR.</p>
"Subordinated Finance Documents"	means any agreements under which the Private Partner's Shareholders make subordinated debt available to the Private Partner.

Delete "C" if there are reasons not to agree this – see Section 5.2.2.

Refinancing

- (1) The Private Partner shall promptly provide the Contracting Authority with full details in relation to any contemplated Refinancing, which shall include the proposed changes to the Original Base Case, a justification of the assumptions on which it is based, the proposed contractual documentation and any other information that the Contracting Authority may reasonably request in relation to that Refinancing.
- (2) The Contracting Authority shall, at all time, have unrestricted rights to audit the Original Base Case used (or proposed to be used) in relation to a Refinancing.
- (3) The Private Partner shall obtain the Contracting Authority's prior written consent in relation to any Qualifying Refinancing.
- (4) The Contracting Authority shall be entitled to receive a [fifty per cent (50%)] share of any Refinancing Gain in a Qualifying Refinancing. *[Adapt in accordance with agreed sharing mechanism]*
- (5) *[The Parties shall act in good faith in relation to any Refinancing or proposed Refinancing (including the manner of calculation of the Refinancing Gain and of payment of the Contracting Authority's share of the Refinancing Gain in a Qualifying Refinancing)].*
- (6) The Contracting Authority shall have the right to elect to receive its share of any Refinancing Gain in a Qualifying Refinancing as:
 - (a) a lump-sum payment which amount shall not exceed the relevant Distribution made on or about the date of the Refinancing and shall be due on the date immediately after the date of the relevant Distribution; or
 - (b) *[an increase of any fee payable by the Private Partner to the Contracting Authority over the remaining PPP Contract period/or a reduction of the availability payment to be paid by the Contracting Authority to the Private Partner over the remaining PPP Contract period][by reduced user fees];* or
 - (c) *a combination of [both].*
- (7) The Private Partner shall pay, on behalf of the Contracting Authority, all reasonable costs of external advisers appointed by the Contracting Authority in relation to a Refinancing or potential refinancing and the calculation of a Refinancing Gain *[drafting also to reflect deduction of costs from any Refinancing Gain prior to calculating the amount to be shared if not already factored into the Refinancing Gain formula].*

The Contracting Authority should approve these agreements and the Original Base Case as a condition precedent to the entry into effect of the PPP Contract and any subsequent amendment and/or additional document which would fall under this definition. See definition of "Original Base Case" in Section 8.7, Sample Drafting 8.

This will not be required in most civil law-governed PPP Contracts as good faith obligations are implied.

Drafting to be adjusted to fit the payment structure. See also Section 5.2.6.

6

TERMINATION EVENTS



6.1 KEY ASPECTS

6.1.1 *The concept of contractual termination*

In commercial contracts, where termination rights are not expressly included, the parties will need to rely on rights available under applicable governing laws to determine whether termination is permitted and what its consequences will be. This can create uncertainty and could involve a costly process if the matter is contentious and the legal position is unclear. While parties from some (typically, but not exclusively, civil law) jurisdictions may be used to contracting in this way, parties from other jurisdictions (typically, but again not exclusively, common law) will expect to see termination rights set out expressly in the contract. This is especially likely to be the case the more valuable and long-term the contract is and where termination has a potentially huge commercial impact on one or more of the contract parties. PPP Contracts fall into this category and the guidance below explains how they typically address termination events.

6.1.2 *Why do PPP Contracts contain termination event provisions?*

When Contracting Authorities and Private Partners enter into PPP Contracts, the goal is for these contracts to run their course and for rights and obligations to remain valid throughout the duration of the contract, often for multiple decades. However, as with any contract – and particularly for a long-term contract of this nature – there may be exceptional cases where one or both Parties may want or need to terminate the PPP Contract early. Typically this would be following events which have a very serious impact on the project or the Parties and which are not remedied or otherwise resolved to enable the project to continue, such as (a) material Contracting Authority default, change in law or MAGA event, (b) material Private Partner default, and (c) instances of prolonged Force Majeure or unavailability of key project insurances. The Contracting Authority may also require a unilateral right to terminate for public policy or other reasons. These events are described in detail in [Section 6.2.3](#) and [Sections 6.3-6.5](#).

In some civil and common law jurisdictions there may be underlying laws addressing certain termination rights and consequences which apply without the PPP Contract having to make express provision. In practice, however, the complexity and individual characteristics of PPP Contracts and the various potential termination circumstances that need to be addressed have resulted in Parties almost always seeking to include express contractual mechanisms setting out comprehensively what circumstances may give rise to termination, who may terminate and what the consequences of termination will be for the Contracting Authority and the Private Partner, as well as for lenders or other key third parties.

The reason why almost all PPP Contracts contain detailed termination regimes lies in the nature of PPP. Elements that have led to best practice and standards around termination events and compensation include:

- contract duration – these are long-term agreements and it is difficult to predict what circumstances may fundamentally affect the agreement or the Parties over 30 years;
- the public interest that drives the Contracting Authority – changes in public interest or policy may affect its need for the contract;
- the amounts at stake – the private sector and the public sector Parties need to be able to protect their investment and public funds, respectively;
- the financial model that lies at the heart of most PPP Contracts – the Private Partner and its Lenders effectively finance the works and services and only recover the investment over time, so any early termination provisions need to take this into account;
- the nature of the asset – this will rarely have a market value and is usually not “marketable” by the Private Partner, and is also – in some jurisdictions – owned by the Contracting Authority regardless of whether it has been paid for; and
- the need for certainty – as PPPs are typically structured as non or limited recourse financings (*see Section C, PPP Contracts in Context*), the Private Partner will have limited funds and so certainty – and a quick resolution – of disputes relating to termination provisions are key to avoid the project company running out of cash and potentially going bankrupt. The Contracting Authority also needs certainty so that it can make informed decisions in respect of early termination.

In the absence of appropriate contractual termination provisions, the Contracting Authority may not be able to terminate the PPP Contract or may be exposed to disproportionate claims for damages. It may even be unable to attract the desired level of competition to bid for the PPP Project in the first place as private sector Parties may feel unable to enter into a PPP Contract without express termination provisions. This is because market practice has shown that, on the private sector side, professional, prudent equity investors are not willing to enter into PPP Projects, and Lenders are not prepared to lend, without reasonable assurance that the Private Partner’s rights under the PPP Contract – and their investment (both equity and debt) – have reasonable protection from any unexpected or early termination of the PPP Contract and will be fairly compensated if early termination occurs. It is in both Parties’ interests that termination should only occur in expressly defined – and exceptional – circumstances and that comprehensive consequential provisions should also apply, including a clear compensation mechanism.

By way of example, in a recent Western European social infrastructure PPP, bidders were asked to bid on the basis of a contract that did not include clear, market-standard termination provisions and compensation, and were told they had to rely on general (civil) law principles and local courts for disputes relating to termination and termination compensation. Bidders challenged this approach to no avail; which led to several pre-qualified bidders withdrawing from the tender process and the remaining bidders putting in such margins (and the few interested lenders a risk premium) that ultimately the tender process was cancelled.

CIVIL AND COMMON LAW DIFFERENCES

While relying on underlying law rather than express contractual provisions is an approach less likely to be seen in common law jurisdictions, there can be certain exceptions, however, for example in respect of Contracting Authority default termination, as is the case in Australia. [See Section 6.3.1](#). Conversely, some civil law jurisdictions always include express termination grounds and corresponding termination compensation mechanics (e.g. the Netherlands).

6.1.3 Types of termination event

Termination provisions are a key element of the risk allocation in a PPP Contract across both Developed and Emerging Markets and in both common and civil law jurisdictions. The list of events which can lead to termination, and the precise terms, will vary from one PPP Contract to another and should be tailored to take account of the specific risks and obligations involved in the relevant PPP Project and the position under the applicable law of the relevant jurisdiction.⁷⁶

Typical early termination events expressly addressed in PPP Contracts can be summarized as follows (these are explained in detail in the sections noted below):

- (a) **Contracting Authority default termination** – The Private Partner will usually require the express right to terminate the PPP Contract itself (and be compensated) for breaches by the Contracting Authority which have a material adverse effect on the project or the Private Partner (such as failure to pay when the Private Partner is not in breach). This may not be possible in some jurisdictions as discussed further below. [See Section 6.3](#).

Specific action or inaction by the Contracting Authority (such as failure to build essential connecting infrastructure), or the occurrence of certain events for which responsibility lies with the Contracting Authority under the PPP Contract (such as a change in law ([See Section 3, Change in Law](#)) or other events referred to in [Section 2, Material Adverse Government Action](#)), which in each case have a material adverse effect on the project or the Private Partner, may sometimes be addressed in separate specific provisions which also give rise to similar Private Partner termination rights. Whether this approach is appropriate or expedient in a particular project will depend on the specifics of the project and jurisdiction concerned. [See Section 2, Material Adverse Government Action and Section 3, Change in Law](#).

- (b) **Voluntary termination** – The Contracting Authority will commonly seek a right to terminate the PPP Contract, at its discretion, for convenience or for public policy reasons. This termination right can have various names, including unilateral termination, termination at will, or termination for convenience or for public policy. The Private Partner does not have a reciprocal right. [See Section 6.4](#).
- (c) **Private Partner default termination** – The Contracting Authority will wish to protect itself against being tied into a long-term contract which is not being performed to the agreed contractual standard by the Private Partner. It will typically have

⁷⁶ See the Global Infrastructure Hub's *PPP Risk Allocation Tool 2019 Edition* – e.g. the early termination (including any compensation) entries in its risk matrices. [See link in Appendix A, Additional PPP Resources](#).

the right to terminate where the Private Partner fails to comply with its material obligations (often including cumulative minor breaches), ranging from performance to breach of change of control restrictions. Specific failures may in some PPP Contracts be addressed in separate specific provisions, such as breaches relating to bribery and corruption offences or breach of refinancing gain-sharing provisions. Some jurisdictions may have a separate termination provision for specified Private Partner defaults which entitle the Contracting Authority to terminate immediately with no remedy period (e.g. the Netherlands). [See Section 6.5.](#)

- (d) *Prolonged Force Majeure or Uninsurability* – Both the Private Partner and the Contracting Authority will also want to protect against being tied in to a long-term contract which is incapable of being fully performed due to a particular occurrence which is typically neither Party’s fault and where no solution has been agreed to continue with the PPP Contract (e.g. due to a prolonged Force Majeure situation or unavailability of a key insurance ([see Section 1.3.3](#)). Similarly, if the Contracting Authority is acting as insurer of last resort and the uninsurable risk occurs, it should have the option to terminate as described in [Section 1.3.4](#). Termination in these circumstances is addressed in the relevant section of this Guidance. [See Section 1, Force Majeure and Section 1.3, Uninsurability.](#)

Some jurisdictions may also have a similar termination event in respect of other specified types of prolonged delay which are a shared risk (e.g. in the Netherlands, where the scheduled availability date is delayed by a certain period, due to zoning or permitting issues – [see Section 1.2.4](#)). [See Section 8.5, Termination Payments.](#)

6.1.4 Relationship to other provisions

As mentioned above, provisions relating to the grounds and mechanics of termination events are closely linked to consequential termination provisions, such as those addressing compensation payments and return of the project assets to the Contracting Authority. [See Section 8, Termination Payments and Section 9, Handback of Assets at End of Contract.](#)

The interplay of provisions entitling the Contracting Authority to step in and take over responsibility for the PPP Project in certain circumstances will also need to be considered, depending on the grounds potentially giving rise to termination rights. For example, if the trigger for step-in is a Private Partner default then the PPP Contract will need to address how these provisions operate together – for example, see [Sections 4.2.9 and 4.2.10](#). If a Force Majeure Event is the trigger, the Contracting Authority step-in should form part of the Parties’ discussions as to how to manage the event and the risk allocation in the Force Majeure clause should apply. [See Section 1, Force Majeure, Sample Drafting 1A, Clause \(4\) and Section 1.2.2 and Section 4, Contracting Authority Step-in Rights.](#)

Events which may also give rise to termination rights but which are treated separately under the PPP Contract will need to dovetail with other termination provisions to ensure consistency in approach in terms of process and consequences and to avoid unnecessary duplication of drafting. As indicated in [Section 6.1.3](#), these may include events of Material Adverse Government Action, Force Majeure, Uninsurability and change in law. [See Section 1, Force Majeure and Section 1.3, Uninsurability, Section 2, Material Adverse Government Action and Section 3, Change in Law.](#)

6.1.5 Related Project Agreements

The Contracting Authority's right to terminate for Private Partner default is subject to the terms agreed between the Contracting Authority and the lenders under the Direct Agreement. The Contracting Authority will want to ensure that it and its advisers have carefully reviewed how the provisions of the PPP Contract, Direct Agreement and Project Agreements (e.g. the main Sub-contracts) work together – including how the timeframes of the successive cure regimes in each contract interplay with each other.

Direct Agreements often postpone the rights of a Contracting Authority to terminate to allow the Lenders a period of time to step in to rectify a default (provided they are actively doing so). It is important that a Contracting Authority retains the right to terminate the PPP Contract if, for example, amounts remain outstanding from the Private Partner to the Contracting Authority after the Lenders' rectification period or if the Lenders fail to rectify poor performance within the specified period. [See Section 7, Lenders' Step-in Rights and Section 6.1.2.](#)

6.2 KEY CONSIDERATIONS FOR THE CONTRACTING AUTHORITY

6.2.1 Effect of applicable laws

Where the underlying law of the relevant jurisdiction provides for early termination rights (e.g. through civil code or legislation or established common law), the Parties should ensure they fully understand how such rights may arise in the context of the PPP Contract, and their consequences, and the extent to which such rights can be expressly written into, derogated from and/or sign-posted in the PPP Contract. This will be key to ensuring the required level of certainty. Particular examples are described further in the relevant sections below. [See Sections 6.3 and 6.4.](#)

CIVIL AND COMMON LAW DIFFERENCES

Underlying law may apply to certain termination scenarios and affect how they are treated under the PPP Contract. For instance, in some jurisdictions (more typically civil law) the Contracting Authority may be entitled to terminate the PPP Contract on the grounds of public interest even without an express contractual right. However, in some civil law jurisdictions the Parties will still want the PPP Contract to expressly cater for such public interest termination, to ensure all relevant scenarios and the applicable process and compensation are captured as comprehensively as possible. [See Section 6.4.](#)

6.2.2 Certainty

As mentioned above, all Parties will want to avoid having to rely on lengthy and potentially costly and uncertain legal proceedings to determine whether termination is permitted and how any compensation may be calculated. Express provisions in the PPP Contract setting out rights to terminate will mitigate these concerns. It is the level of certainty provided by such provisions which is key for Lenders in agreeing to commit funding to the PPP Project – it also enables them to price their debt based on a lower risk profile as regards repayment risk, which in turn feeds through into the price bid by the Private Partner for the PPP Contract.

EMERGING AND DEVELOPED MARKET DIFFERENCES

Underlying Lenders' analysis of their likely debt repayment will be an assessment of the likelihood of early termination, as well as the strength of the Contracting Authority's covenant to pay (*see Section 8.6, Method and timing of payment*). In less mature markets, or projects in areas where there is less precedent, Lenders may therefore wish to see more protection from early termination (in terms of both scope of rights, as well as termination consequences) than they might in more Developed Markets. Lenders will also take comfort from the ability to mitigate Private Partner default termination risk through entry into a direct agreement with the Contracting Authority. *See Section 6.1.5 above and Section 7, Lenders' Step-in Rights and Section 8.1.2.*

The inclusion of express termination provisions will not necessarily result in any greater rights or obligations on either Party than would be the case if the Parties relied on the underlying law applying to such early termination rights. However, the certainty provided is key to attracting long-term finance and ensures both Parties understand the circumstances in which termination may be permitted.

EMERGING AND DEVELOPED MARKET DIFFERENCES

The difference between mature and less mature markets is minimal as regards the need for express contractual termination provisions. This is preferred market practice even in jurisdictions where it may be justifiable to have no or limited express contractual arrangements in place (which in itself will depend on the nature and maturity of the applicable legal system, the expertise of local courts, the predictability of the outcome of disputes around termination and termination compensation and sufficient legal certainty and/or underpinning legislation regarding entitlements to terminate and termination consequences).

6.2.3 Framework for negotiation

As mentioned in *Section 8.2.4, Termination Payments*, it is important to note that, in practice, termination provisions provide a backdrop for the Parties (and the Lenders) to initiate discussions about how to continue the PPP Contract where there is a risk of termination. It is usually in all Parties' interests to find a way to continue the PPP Project and avoid termination. From the Contracting Authority's perspective, although it needs to protect the use of public funds, it also has a duty to provide public services. Negotiating a way to continue the PPP Contract which works for all Parties may be the best way to achieve this and avoids triggering a termination payment liability. Express provisions are key in providing a clear framework for the Parties to try, where applicable, to resolve any project issues before the exercise of any termination rights.

In some jurisdictions, the scope for negotiations will be limited by public procurement or competitive tender rules forbidding substantial amendments to existing agreements, unless detailed, precise and unequivocal amendment clauses are incorporated into the contract. If such legislation applies, the Contracting Authority should ensure that the PPP Contract contains appropriate revision clauses.

6.2.4 Consideration of termination consequences

As explained in [Section 8, Termination Payments](#), it is market practice that the Contracting Authority makes some level of compensation payment to the Private Partner (subject to relevant deductions) whatever the reason for termination. When considering exercising its termination rights, the Contracting Authority should therefore bear in mind its ability to meet its obligations as regards method and timing of such payment ([see Section 8.6 Termination Payments](#)).

Both Parties should also be aware of contractual provisions addressing other consequences of termination in addition to compensation provisions, such as transfer by the Private Partner of the project assets and handover obligations and arrangements to facilitate continuing to operate or construct the PPP Project. These should form part of any assessment regarding exercise of termination rights and will need to be considered in a timely manner and in accordance with the timeframes specified in the relevant provisions. [See Section 9, Handback of Assets at End of Contract](#).

6.3 TERMINATION ON CONTRACTING AUTHORITY DEFAULT

6.3.1 Market practice

The Private Partner should have the right to terminate the PPP Contract in certain circumstances where the Contracting Authority is in breach of its obligations. Although such rights may exist under general law in both civil and common law jurisdictions, it is common to see this as an express contractual right. The UK PF2 Guidance describes this right as arising where the Contracting Authority or government acts in a way which “renders their contractual relationship untenable or completely frustrates the Private Partner’s ability to deliver the PPP Project (including due to the effect on its financial status)”. Minor breaches will by their nature typically not fall into this category and even a material breach may not give rise to a contractual termination right if the Contracting Authority’s (or government’s) actions do not have those consequences. For example, a partial denial of access to the project assets may not be sufficient to reach the “frustration” threshold and non-payment will normally be the subject of minimum thresholds and rectification periods. [See Section 6.6, Sample Drafting 6, Clause XX](#).

In some jurisdictions (both civil law and common law), the Private Partner may have rights to terminate under applicable law and may be expected to rely on such rights without an express contractual right. The extent to which private sector Parties are able to bid for a PPP Contract on this basis will depend on the level of legal certainty and precedent in the relevant jurisdiction.

CIVIL AND COMMON LAW DIFFERENCES

As described in the Infra Australia PPP Guidelines, there are jurisdictions where the Private Partner is expected to rely on its common law rights to terminate for Contracting Authority default instead of having an express right. This may be because termination for Contracting Authority default is such a fundamental step with enormous business and other ramifications for the Private Partner that the Private Partner's focus is instead on the enforceability of the contractual payment and time/cost compensation provisions applicable to breaches by the Contracting Authority. Similarly, in civil law France⁷⁷, the Private Partner would typically apply to an administrative court to request contract termination in such circumstances and a contractual right to terminate would be rare. Relying on underlying law is likely to deter bidders in markets where there is insufficient legal precedent and certainty.

6.3.2 Default events

Key defaults: In jurisdictions where termination for Contracting Authority default is contractually envisaged, the key Contracting Authority defaults which typically entitle the Private Partner to terminate the PPP Contract are:

- a failure by the Contracting Authority to pay the Private Partner;
- an expropriation or similar of a material part of the project assets or shares of the Private Partner; and
- a breach of an obligation which makes it impossible (in whole or substantial part) for the Private Partner to perform the PPP Contract for a specific period.

Most Contracting Authority breaches that allow the Private Partner to terminate the PPP Contract will typically be captured under the scope of these default events. See [Section 6.6, Sample Drafting 6, Clause XX, Required Definition, Contracting Authority Default](#).

Other defaults: Any other circumstances in which the Private Partner is permitted to terminate for Contracting Authority default must be considered on a project-specific basis. Any additional specific termination events must be justifiable by reference to the particular nature of the project and must meet the threshold above (i.e. making it impossible for the Private Partner to perform the PPP Contract or making the continued relationship untenable).

EMERGING AND DEVELOPED MARKET DIFFERENCES

As the identity of the Contracting Authority and the strength of its financial (and other key covenants) will be key to the Private Partner's decision to enter into the PPP Contract, the Private Partner may want to retain a specific termination right if the Contracting Authority breaches any restrictions on its ability to assign or transfer its contractual rights, or its ownership changes. This will depend on the Contracting Authority and jurisdiction concerned and may be more common in markets which are less politically and legally stable.

⁷⁷ In France, in most cases, the PPP Contract is silent and the Private Partner would typically be expected to apply to court for the right to terminate the PPP Contract.

As the obligations of the Contracting Authority tend to be principally payment obligations and approval rights, it is typically not appropriate to replicate a long list of default events as is the case for Private Partner default. Most failures by the Contracting Authority to comply with the provisions of the PPP Contract before service commencement (for example, issuing approvals) and – to an extent during the operating phase – can be adequately addressed through contractual regimes granting time and/or cost relief. *See Section 6.6, Sample Drafting 6, Clause XX, Required Definition, Contracting Authority Default (d) and (f).*

Grace periods: The Contracting Authority should ensure that grace periods are built in for non-payment or other defaults by it under the PPP Contract to reduce the risk of a termination right arising in the first place. For example, a right to terminate for non-payment should only arise when the payment is overdue by a certain period (e.g. a few months) and then only after a specified period has elapsed following a formal demand by the Private Partner. This is key for the Contracting Authority to at least mitigate, if not eliminate, the possibility of termination arising from, for example, purely administrative error. *See Section 6.6, Sample Drafting 6, Clause XX, Required Definition, Contracting Authority Default (b) and (c).*

Material Adverse Government Action: As highlighted in *Section 2, Material Adverse Government Action*, some PPP Contracts may contain specific MAGA provisions which provide the Private Partner with relief if a MAGA event occurs and may entitle the Parties to terminate the PPP Contract if there is a protracted MAGA event. The type of political risk events addressed by a MAGA provision may include the type of Contracting Authority defaults outlined above (and vice versa). This could mean that a PPP Contract (i) only has a MAGA provision, (ii) only has a Contracting Authority default provision, or (iii) has a combination of the two and/or separate provisions addressing specific political risk matters such as changes in law (*see Section 3, Change in Law*). As indicated in *Section 2, Material Adverse Government Action*, one approach could be to have a separate MAGA clause, with a protracted MAGA event defined as a Contracting Authority default event. Some jurisdictions may only allow the Contracting Authority to terminate for protracted MAGA-style events by implementing a voluntary termination (*see Section 2.2.3*). The key consideration is that the chosen approach works for the project in question and is consistent with the principles outlined in this Guidance in respect of such matters. *See Section 6.6, Sample Drafting 6, Clause XX, Required Definition, Contracting Authority Default (e).*

EMERGING AND DEVELOPED MARKET DIFFERENCES

Markets which are politically and legally stable are less likely to have separate Material Adverse Government Action termination provisions (*see Section 2, Material Adverse Government Action*) as the Private Partner and its lenders will be comfortable relying on a Contracting Authority default termination provision, combined with a shared risk Force Majeure provision and other contractual provisions which provide time and/or money relief to the Private Partner in relevant circumstances of Contracting Authority responsibility.

6.3.3 Notice and Rectification

Where contractual termination for Contracting Authority default is available in the relevant jurisdiction, the PPP Contract should set out when and how the Private Partner is entitled to serve a termination notice and what it should contain. Termination should be the Private Partner's last resort. Due to the effect termination would have on the provision of the relevant services and the substantial financial liability it would impose on the Contracting Authority, the PPP Contract typically gives the Contracting Authority the opportunity to rectify (where remediable) its failure and its effects within a specified period. The termination notice should specify how long the rectification period is and when the PPP Contract will terminate if rectification is not achieved. There is often no formal rectification process expressly set out in the PPP Contract unlike for Private Partner default. *See Section 6.6, Sample Drafting 6, Clause XX and Section 7.5.5.*

EMERGING AND DEVELOPED MARKET DIFFERENCES

In a mature market where the Contracting Authority default termination events are limited and likely to be primarily linked to non payment, it is less common to include a formal rectification process in the PPP Contract following service of a termination notice. In less mature markets where the Contracting Authority default termination events may be more extensive, it may be in all Parties' interests to introduce a more formal mechanic (*this is not included in the Sample Drafting*).

The Parties will need to consider the practical consequences of the exercise by the Private Partner of a termination right under the PPP Contract. In particular, there should be an orderly plan or at least sufficient time for the Contracting Authority to take back the project. In practice, this means the Contracting Authority ensuring that the notice period for termination is sufficient for it to mobilize its resources in relation to the project. *See Section 6.6, Sample Drafting 6, Clause XX(c) and Section 9, Handback of Assets at End of Contract.*

6.4 VOLUNTARY TERMINATION

6.4.1 Market Practice

Although the intention of all Parties to a PPP Contract should be that it will run its full course, there may be circumstances where the Contracting Authority is no longer able to continue the relationship it has with the Private Partner under the PPP Contract. For example, there may be a policy change which makes further provision of the services provided through the PPP Project redundant or no longer politically acceptable through PPP. In order to cater for such circumstances, the Contracting Authority may wish to retain the flexibility to terminate the PPP Contract unilaterally. The Private Partner should not object to the Contracting Authority having this right, provided that it is compensated in full if such right is exercised (i.e. so that it is left in the position it would have been in had the PPP Contract run its full course). *See Section 6.6, Sample Drafting 6, Clause XY.*

This type of right is known by various terms, depending on its scope and the relevant jurisdiction; these include: voluntary termination, unilateral termination, termination for convenience, termination at will and – as described below – termination for public interest or policy. In common law jurisdictions the PPP Contract does not usually fetter the Contracting Authority as to the reason for voluntary termination and none needs to be given if the right is exercised. However, in other jurisdictions where the right is tied to public interest, the Contracting Authority may be required to substantiate the validity of the public interest ground. [See Section 6.3.1.](#)

In some jurisdictions (more typically civil law) the Contracting Authority may be entitled to terminate the PPP Contract on the grounds of public interest even without an express contractual right. This inalienable right is rarely invoked but the private sector (Private Partner, Sub-contractors and Lenders) will still require the PPP Contract to cater for this low probability but high risk event as comprehensively as possible. In some jurisdictions it is not possible to contractually waive the right to unilaterally terminate in the public interest, but it is possible for Parties to agree in advance the procedure and consequences of such termination. In practice, the compensation and process is usually identical to voluntary termination, or even a Contracting Authority default scenario. This is because the Private Partner is not responsible for, nor capable of mitigating, a public policy-driven decision to terminate unilaterally. The voluntary termination regime usually means that the Contracting Authority indemnifies the Private Partner, Equity Investors and Lenders. [See Section 6.6, Sample Drafting 6, Clause XY\(a\).](#)

As highlighted in [Section 2, Material Adverse Government Action](#), some PPP Contracts may only allow the Contracting Authority to terminate for protracted MAGA-style events by implementing a voluntary termination.

6.4.2 Notice

The PPP Contract should set out when and how the Contracting Authority is entitled to serve a termination notice and what such notice should contain. The PPP Contract will terminate on the date specified in the notice. [See Section 6.5.5 and Section 6.6, Sample Drafting 6, Clause XY\(c\).](#)

The Contracting Authority should ensure that the minimum notice period for termination is sufficient for both Parties to make appropriate arrangements in respect of the handback of the project and to facilitate compliance with handback obligations. From its own perspective, it should have already fully considered and prepared for this in deciding to exercise its right to terminate unilaterally. From the Private Partner's perspective, its prime concern will be to ensure it is fully compensated for such early termination and able to comply with its handover obligations. [See Section 9, Handback of Assets at End of Contract and Section 6.6, Sample Drafting 6, Clause XY\(c\)\(ii\).](#)

6.5 PRIVATE PARTNER DEFAULT TERMINATION

6.5.1 *Market Practice*

It is market practice that the Contracting Authority has the right to terminate the PPP Contract for serious failures by the Private Partner in, or connected to, delivering the PPP Project. Termination is not, however, triggered by minor breaches alone and, where practicable, the Private Partner is given the opportunity to remedy any breach. This is because the financial and reputational consequences of termination for default are likely to be severe for the Private Partner. The Contracting Authority's aim is to find a balance which enables it to terminate for poor performance and protect public services (by finding a replacement service provider), but only in respect of serious breaches which are not remediable by the Private Partner, or by its Lenders under the Direct Agreement. [See Section 6.6, Sample Drafting 6, Clause YY.1.](#)

The Contracting Authority will typically be monitoring the Private Partner's performance under the availability and performance regimes linked to the availability payment mechanism in a "government pays" model. In "user pays" models it should similarly stay aware of Private Partner performance and one measure of this may be user demand and satisfaction levels (e.g. in a toll road project). PPP Contracts generally provide for bespoke regimes to calibrate performance, whether in "government pays" or "user pays" models and specific performance levels should be specified to provide certainty to the Contracting Authority of when its rights to terminate arise.

6.5.2 *Default events*

Private Partner default events should be defined clearly and objectively. Where practicable, given the nature of the default, they should have reasonable in-built tolerance levels so that an appropriate threshold of poor performance has to be reached before termination rights arise. For example, for less significant obligations, this could be by requiring a certain level of performance points to be accrued in respect of certain obligations before a termination right arises in respect of such failures, or by the termination right only arising in respect of a particular failure if it has happened more than once. [See Section 6.6, Sample Drafting 6, Clause YY.1, Required Definitions, Private Partner Default \(b\) and \(k\).](#)

While Private Partner default events typically follow a similar pattern, they should be tailored to the specific nature of the PPP Project in question; for example, if vandalism is a particular concern due to the nature of the project, it might be appropriate to have a separate cumulative performance point default event specifically related to vandalism. This is more likely to be the case in a school or prison project, for example, than a road project, as the potential for – and impact of – vandalism damage on the core service in a school or prison is likely to be much greater than in a road project (where, for example, graffiti on a bridge will not typically affect use of the road). [See Section 6.6, Sample Drafting 6, Clause YY.1, Required Definitions, Private Partner Default \(p\).](#)

Termination events may be performance-related or relate more specifically to the financial status and corporate activity of the Private Partner. While typically the drafting of a Private Partner default provision will contain a list of various types of default, as mentioned in [Section 6.1.3](#), particular defaults are sometimes given their

own specific (and sometimes separate) termination provision. For example, breaches of bribery and corruption laws in South Africa and the UK fall under a “corrupt gifts” provision which is typically required in all government contracts and closely reflects specific legislation. *See Section 6.6, Sample Drafting 6, Clause YY.1, Required Definitions, Private Partner Default (o).*

EMERGING AND DEVELOPED MARKET DIFFERENCES

In more Developed Markets where it is more likely that Private Partners seek to optimize their returns through refinancing the debt incurred for the project, the Contracting Authority may seek to share in any gains realized. Breach of provisions requiring such gain-sharing are typically specific defaults in markets such as the UK, the Netherlands and Australia. *See Section 6.6, Sample Drafting 6, Clause YY.1, Required Definitions, Private Partner Default (n) and Section 5, Refinancing.*

Typical performance type defaults that may give the Contracting Authority the right to terminate the PPP Contract include:

- ***Breach having a material adverse effect on performance:*** by definition this is a serious occurrence (rather than a cumulative series of smaller failings) which has a material adverse effect on the Private Partner’s delivery of the project. Defining “material” can be challenging and this can make material breach an uncertain termination ground to rely on from the Contracting Authority’s perspective. However, there may be legal precedent in the relevant jurisdiction for what “material” typically means. The advantage of having a default event with this scope is that the Contracting Authority does not have to identify before contract signature every specific failing which might have a material adverse effect on the project over its life (which would then be included as specific material breach default events in their own right, as outlined below). *See Section 6.6, Sample Drafting 6, Clause YY.1, Required Definitions, Private Partner Default (a).*

It may also be possible to define this type of breach by reference to a failure to provide a particular aspect or portion of the project or a particular outcome. For example, in a prison project, this could include a failure which results in the Contracting Authority being able to provide custodial services at the project site, or in a hospital project, being unable to provide clinical services. *See Sector-specific breach below.*

- ***Unavailability:*** in a “government pays” model, payment is based on availability of key aspects of the PPP Contract at the required standard, such as classrooms in schools projects or prison cells in prisons projects. Although unavailability will be reflected in payment deductions, if it occurs to such an extent that the Contracting Authority is not receiving the public services it needs, this could have serious repercussions for the Contracting Authority and be indicative of a serious underlying problem with the Private Partner. The right to terminate in specified circumstances will be an additional incentive for the Private Partner and its Lenders to ensure unavailability is minimized. As mentioned above, this type of event is an example of a material breach which can be expressly defined. *See Section 6.6, Sample Drafting 6, Clause YY.1, Required Definitions, Private Partner Default (j).*

In a “user pays” model, while the main incentive for the Private Partner to perform is to receive third party revenue, the threat of losing the PPP Project for poor service provision will act as an incentive to perform. In order to provide an empirical basis for assessing Private Partner performance, a default event can be included based on the Contracting Authority’s monitoring of the service (e.g. a termination right could arise in toll road projects if a certain number of lanes are out of operation for a particular length of time within a specified period, or in a PPP Project where vital services are not delivered to users for a period of time (e.g. water services under a concession)).

- **Performance points accrual:** typically, in a “government pays” model, the PPP Contract will contain a performance regime designed to incentivize the Private Partner to perform more minor obligations by linking minor failings to performance points. Accruing performance points leads to deductions from the availability payment. Giving the Contracting Authority the additional right to terminate if a certain level of performance points is accrued in a specified period will act as a strong incentive for the Private Partner to carry out its minor obligations. In some jurisdictions (e.g. the UK), Contracting Authorities may also have a termination event based on a combination of unavailability and performance points accrual over a specified period. No additional rectification period is typically allowed if a termination notice is served, but the Lenders will be able to exercise their step-in rights under the Direct Agreement. *See Section 6.6, Sample Drafting 6, Clause YY.1, Required Definitions, Private Partner Default (k) and (l) and Section 7, Lenders’ Step-in Rights.*
- **Persistent breach:** this default event is aimed at recurrent defaults of the same type which by themselves are not serious enough to entitle the Contracting Authority to terminate and which would not otherwise be caught under another default event. If the performance regime is all-encompassing then this default event may not be needed. However, it has the advantage of giving the Contracting Authority the ability to take action over repeated failings which were not expressly identified before contract signature, and which do not have a financial impact on the Private Partner to act as an incentive for it to perform. This type of default event is a common feature in the Australia, UK and Philippines markets, for example. *See Section 6.6, Sample Drafting 6, Clause YY.1, Required Definitions, Private Partner Default (b).*

If included, the drafting should set out a clear and fair warning notice regime for notifying the Private Partner when a particular failing has occurred and what will happen if it re-occurs. Typically, the mechanism provides for a first warning once the breach has occurred a specified number of times, followed by a final warning if the same breach re-occurs within a specified period (allowing also for a short rectification period). If it occurs again within a further specified period after the final warning, then the Contracting Authority has the right to terminate the PPP Contract. No additional rectification period is typically allowed if a termination notice is served, but the Lenders will be able to exercise their step-in rights under the Direct Agreement. *See Section 7, Lenders’ Step-in Rights.*

- **Construction-related breach:** the key construction-related defaults during the construction phase which typically give rise to the Contracting Authority’s right to terminate are the Private Partner:
 - (a) abandoning the construction works; and

- (b) failing to achieve the scheduled date for service commencement by a specified long-stop date (which can be set by reference to a date a number of years after the scheduled commencement date of the PPP Project (as adjusted by permitted extensions of time)).

Failure by the Private Partner to commence construction or to obtain relevant administrative authorisations needed for construction is also sometimes seen. [See Section 6.6, Sample Drafting 6, Clause YY.1, Required Definitions, Private Partner Default \(g\)–\(i\)](#) for more detail.

The Contracting Authority will want to consider the particular circumstances of its PPP Project to assess if there are any other key construction-specific defaults to include. For example, it might be critical for works in a schools project to commence on an existing site by a specific date in order not to disrupt term-time, or in other PPP Projects it might be vital to start works by a particular date in order to avoid extreme seasonal weather which would then impact on the whole PPP Project delivery.

- ***Insolvency-related breach:*** the financial health of the Private Partner is key to its ability to perform the PPP Contract and the Contracting Authority should aim to monitor the financial indicators of the Private Partner (and its main Sub-contractors) so that it can make contingency plans to minimize the impact of any adverse financial situation on delivery of the PPP Project. Critical to this is the ability to terminate the PPP Contract if insolvency-related steps are taken in respect of the Private Partner. The type of events that will be relevant will depend on the jurisdiction of the PPP Project and applicable insolvency laws. Typically, this type of default event does not apply to Sub-contractors because the Private Partner is already incentivized to replace them if they are in financial difficulty. However, if any Parties owe significant obligations to the Contracting Authority which cannot be set off against an availability payment owed by it, it would be sensible to include a specific insolvency-related default event in respect of them. This will depend on the particular PPP Project. In some jurisdictions there are restrictions on termination rights in the pre-insolvency phase, and in addition exercising relevant rights may be difficult in the event an insolvency practitioner is appointed. [See Section 6.6, Sample Drafting 6, Clause YY.1, Required Definitions, Private Partner Default \(c\)](#).

CIVIL AND COMMON LAW DIFFERENCES

In some civil law jurisdictions, insolvency laws may have an impact on the right to terminate the PPP in the event of insolvency of the Private Partner (or its Shareholders).

In the context of default events which relate to the financial health of the Private Partner, Contracting Authorities should note that it is not usual to include non-payment by the Private Partner as a default event as it has limited payment obligations and in a “government pays” model these should be capable of being set off against amounts payable by the Contracting Authority. If this is not the case (e.g. in a “user pays” model), the Contracting Authority should consider including a specific default event.

- **Strategic breach:** there may be certain restrictions that the Contracting Authority wants to place on the Private Partner in respect of corporate matters. For example, it may want to prevent a change of ownership of the Private Partner or an assignment of any of the Private Partner's rights, or prohibit a change in a key Sub-contractor without its consent.⁷⁸ Where these restrictions are of significant importance to the Contracting Authority, it may be appropriate to include them as individual termination events. *See Section 6.6, Sample Drafting 6, Clause YY.1, Required Definitions, Private Partner Default (d)-(f).*
- **Sector-specific breach:** in some sectors, there may be a need to require specific compliance with certain procedures such as security clearance (e.g. in a prison) or national security (e.g. in a defense project). It may consequently be appropriate to include a corresponding default event. Similarly, compliance with health and safety matters or child safeguarding may be particularly key in certain sectors (e.g. in a hospital or school) and a breach may warrant its own termination event. As these matters are sector-specific, sample drafting is not included although a place-holder has been included to indicate where a bespoke breach event could be inserted. *See Section 6.6, Sample Drafting 6, Clause YY.1, Required Definitions, Private Partner Default (p).*
- **Social/environmental breach:** if there are particular obligations relating to social/environmental matters, for example, decontamination of specific real estate assets, relocation or employment of a specified number of local people or people of a particular gender, or failure to comply with a climate change-specific obligation, it may be appropriate to include corresponding default events. Again, these matters are project-specific and accordingly, sample drafting is not included although a place-holder has been included to indicate where a bespoke breach event could be inserted. *See Section 6.6, Sample Drafting 6, Clause YY.1, Required Definitions, Private Partner Default (q).*
- **Insurance breach:** placing and maintaining key insurances in accordance with the insurance provisions is key to the financial viability of the PPP Project and to protecting the Contracting Authority's interests. A failure to do so by the Private Partner should be included as an individual default event, subject to provisions on unavailability of insurance. *See Section 1.3 and Section 6.6, Sample Drafting 6, Clause YY.1, Required Definitions, Private Partner Default (m).*
- **Other breach:** failure to provide or to renew performance guarantees is also common in some jurisdictions.

6.5.3 Relationship between Private Partner default events

From the Contracting Authority's perspective, these Private Partner default events should not be mutually exclusive. An unavailability default could also be a material breach, for example, if the unavailability threshold was reached through a one-off failing, and failings which attract performance points leading to a performance point accrual termination event might also be capable of being a persistent breach termination event. Contracting Authorities should ensure that wording is not included in the PPP Contract which specifically provides that defaults are mutually exclusive. *Section 6.6, Sample Drafting 6, Clause YY.1* avoids this issue.

⁷⁸ These provisions are covered briefly in *Section D, PPP Contracts in Context*. For more information, see the resources in *Appendix A*.

6.5.4 Application of default events across project phases

The Contracting Authority may be asked by the Private Partner to consider limiting some of the default events so that they only apply in the operating phase – this is usually on the basis that until the asset is operational the Private Partner should not be at risk of termination for any events which are not specific construction defaults (such as those in [Section 6.6, Sample Drafting 6, Clause YY.1, Required Definitions, Private Partner Default \(g\)-\(i\)](#)). Broadly speaking, the Private Partner’s main obligation during the construction phase is to build the asset and it is highly incentivized to reach completion so that its revenue stream will begin. However, the strategic and insolvency-related failures could occur in either phase, a failure to obtain required insurances is critical in the construction phase and there may also be other types of material or persistent failures (e.g. to obtain relevant consents or provide information) which from the Contracting Authority’s perspective should be capable of giving rise to a termination event in any phase of the project. The Contracting Authority would need to consider any such request on a project-specific basis and typically the defaults referred to in the previous sentence should not be limited to the operating phase.

6.5.5 Notices and Rectification

The PPP Contract should set out when and how the Contracting Authority is entitled to serve a termination notice and what it should contain. As termination should be the Contracting Authority’s last resort given the effect this would have on the provision of the relevant services, the Private Partner is typically given the opportunity to rectify termination event failures where they are remediable and/or to financially compensate the Authority for the effects of the breach. The PPP Contract should set out a clear rectification procedure and the termination notice should specify if the rectification process applies. [See Section 6.6, Sample Drafting 6, Clause YY.1\(b\)-\(e\)](#).

Rectification will not be appropriate in respect of all types of breach. Some breaches may not be capable of remedy (for example, failure to achieve service commencement by the long-stop date) and some events may only qualify as termination events after a built-in rectification or grace period has already been given (e.g. after the accrual of a specified level of performance points or due to the steps leading to a persistent breach). As mentioned in [Section 6.1.3](#), some jurisdictions (such as the Netherlands) may have a separate termination provision for specified Private Partner breaches which cannot be rectified and which entitle the Contracting Authority to terminate immediately. [See Section 6.6, Sample Drafting 6, Clause YY.1\(b\)\(iii\)](#).

Following service of the termination notice, the rectification process should allow the Private Partner to propose a rectification program in respect of certain remediable breaches ([see Section 6.6, Sample Drafting 6, Clause YY.1\(b\)\(ii\)\(A\)](#)) which the Contracting Authority may comment on and approve. A typical example of this is where poor service has resulted in unavailability for a specified period, and the rectification plan would deal with how this could be remedied (e.g. in the case of unavailability of rooms due to low temperatures caused by a defective boiler, by requiring a replacement piece of heating equipment). The contractual mechanism will usually specify a fixed period

for the program to be carried out although it may be appropriate to agree a different, reasonable, period depending on the nature of the specific breach.

Failure to propose an acceptable rectification program or to rectify the default will result in termination in accordance with the terms of the termination notice (*see Section 6.6, Sample Drafting 6, Clause YY.1(d)(i)*). Failure to rectify the default within the timeframe set under the agreed rectification program or in accordance with its terms will also lead to termination: typically the Contracting Authority will serve a further notice stating that the failure has not been remedied in accordance with the agreed program and that the PPP Contract will terminate on a subsequent specified date, subject to any step-in rights of the Lenders under the Direct Agreement. *See Section 6.6, Sample Drafting 6, Clause YY.1(d)(ii) and (e) and Section 7, Lenders' Step-in Rights.*

As mentioned in *Section 6.1.4*, provisions in respect of Contracting Authority step-in rights should also tie in with the Private Partner default termination process where the trigger for such step-in is a Private Partner default event. *See Section 4, Contracting Authority Step-in Rights.*

6.6 SAMPLE DRAFTING 6

CONTRACTING AUTHORITY DEFAULT TERMINATION

Required Definitions

“Contracting Authority Default” means:

- (a) an expropriation, sequestration or requisition of a material part of the assets [*consider defining assets*] and/or shares of the Private Partner [or the Sub-contractors] [or its/their holding company] by the Contracting Authority [or other governmental entity];
- (b) a failure by the Contracting Authority to make payment of any amount of money exceeding [XXX] (indexed) that is due and payable by the Contracting Authority under this PPP Contract within 30 days of service of a formal written demand by the Private Partner, where that amount fell due and payable [two] (or more) months prior to the date of service of the written demand;
- (c) a breach by the Contracting Authority of its obligations under this PPP Contract which substantially frustrates or renders it impossible for the Private Partner to perform its obligations under this PPP Contract for a continuous period of [two] months;
- (d) [*other project-specific key failures*];
- (e) [*protracted MAGA event/other termination event for which Contracting Authority bears same risk/responsibility*]; or
- (f) [*a breach by the Contracting Authority of Clause [] (Assignment) or Clause [] (Change of Ownership)*].

Clause XX

- (a) If a Contracting Authority Default has occurred and the Private Partner wishes to terminate the PPP Contract, it must serve a termination notice on the Contracting Authority within [45] days of becoming aware of the Contracting Authority Default.
- (b) The termination notice must specify the type of Contracting Authority Default which has occurred entitling the Private Partner to terminate.
- (c) The PPP Contract will terminate [45] days after the date the Contracting Authority receives the termination notice, unless the Contracting Authority rectifies the Contracting Authority Default within [30] days of receipt of the termination notice. *The Parties will comply with Clause [●] [Compensation on Contracting Authority Default Termination] and Clause [●] [Handback].*

This termination right is not available in some jurisdictions.

Interest on late payment should be addressed in the PPP Contract.

Time periods subject to further rectification period following termination notice.

Time periods subject to further rectification period following termination notice.

See Section 6.3.2 and Section 2.2.3 – ensure drafting ties in with any other termination clauses on an equivalent basis.

Add further details if applicable.

Add drafting to evidence rectification etc. if considered necessary.

Drafting to tie in with notice terms, related clauses and obligations on handback.

CONTRACTING AUTHORITY VOLUNTARY TERMINATION

Clause XY

- (a) The Contracting Authority may terminate this PPP Contract at any time on or before its Expiry Date [define] in accordance with this Clause [XY].
- (b) On termination, the Contracting Authority shall *[have the option to]* require the Private Partner to transfer its right, title and interest in and to the [Assets] *[define]* to the Contracting Authority or as directed by the Contracting Authority.
- (c) If the Contracting Authority wishes to terminate this PPP Contract under this Clause [XY], it must give notice to the Private Partner stating:
- (i) it is terminating the PPP Contract under Clause [XY] (Contracting Authority voluntary termination);
 - (ii) the date on which the PPP Contract will terminate, which must be a minimum of [30] days after the date of receipt of the notice; and
 - (iii) *[whether it elects to exercise its option under Clause [XY](b) and, if so,]* to whom any relevant transfer(s) are to be made *[and any other requirements]* in accordance with Clause [●] *[Handback]* *[and Clause XY(b)]*.
- (d) If the Contracting Authority gives notice in accordance with Clause XY(c), this PPP Contract will terminate on the date specified in, and in accordance with, that notice, the Contracting Authority will pay the Private Partner an amount in accordance with Clause [●] *[Compensation on voluntary termination]* and the Private Partner/Parties will comply with Clause *[Handback]* *[and the Contracting Authority's requirements under this Clause XY]*.

This includes termination in the public interest; where applicable, include reference to underpinning public law principle and legal basis and clarify this clause covers all consequences of termination in the public interest.

Include option wording if appropriate. This may not be viable in jurisdictions such as France if handback is automatic. See Section 9.2.7.

See also Sections 6.2.3, 6.4 and 2.2.3 in relation to MAGA style events.

Drafting to tie in with notice terms, related clauses and obligations on handback.

PRIVATE PARTNER DEFAULT TERMINATION

Required Definitions

“Abandonment” means not carrying out any Works contemplated by the [Construction Program] at the Site for twenty (20) consecutive Business Days or during sixty (60) Business Days (whether consecutive or not) in any twelve (12)-month period.

“Information Breach” means a breach of any of the provisions of Clauses [●] [in respect of Private Partner’s records and provision of information] or [●] (in respect of personal data)].

“Persistent Breach” means a breach which has given rise to the Contracting Authority’s right to terminate in accordance with Clause [YY.2(b)(iii)].

“Private Partner Default” means one of the following events:

- (a) breach by the Private Partner of any of its obligations under this PPP Contract which materially and adversely affects the performance of the Service;
- (b) Persistent Breach;
- (c) [insolvency-related events relevant to the Private Partner/Holdco/key Parties];

- (d) breach by the Private Partner of Clause [●] (Replacement of Sub-contractors);
- (e) breach by the Private Partner of Clause [●] (Assignment);
- (f) breach of Clause [●] (Change in Ownership);
- (g) Abandonment of the Works by the Private Partner at any time;
- (h) [failure by the Private Partner to commence the Works [at XX Site] by [specified date]];
- (i) failure by the Private Partner to achieve the [Service Commencement Date] by the [Longstop Date];
- (j) failure by the Private Partner to provide [x] Available [places/areas/beds/cells] for [x] period;
- (k) the accumulation by the Private Partner of [x] or more [performance points] in any [specified period];
- (l) failure by the Private Partner to provide [x] Available [places/areas] for [x] period [and accumulation of [x] [performance points] in respect of the same period];
- (m) subject to Clause [●] (Risks that become uninsurable), a breach by the Private Partner of its obligation to take out and maintain [Required Insurances];
- (n) breach of Clause [●] (Refinancing Gains);
- (o) [breach of Clause [●] (Bribery and corruption)/commission of a [prohibited act] by the Private Partner (or Sub-contractor) or their employees acting independently;]
- (p) [Sector-specific breaches];
- (q) [Social/environmental breaches]; or
- (r) [material breach by the Private Partner of its [Health and Safety] obligations under Clause [●]/this PPP Contract which results in the criminal investigation, prosecution and conviction of the Private Partner or any Private Partner Related Party or the Contracting Authority under [applicable Health and Safety Regime] (an “H&S Conviction”) provided that an H&S Conviction of a Private Partner Related Party or the Contracting Authority shall not constitute a Private Partner Default if, within ninety (90) Business Days from the date of the H&S Conviction (whether or not the H&S Conviction is subject to an appeal or any further judicial process), the involvement in the project of each relevant Private Partner Related Party (which in the case of an individual director, officer or employee shall be deemed to include the Private Partner Related Party of which that person is a director, officer or employee) is terminated and a replacement is appointed by the Private Partner in accordance with Clause [●] (Restrictions on the Private Partner) provided always that in determining whether to exercise any right of termination or right to require the termination of the engagement of a Private Partner Related Party under this Clause [●], the Contracting Authority shall:

An Available Place/Area/Bed/Cell will be specifically defined.

This default may be treated in a separate provision. In either case, this (and any separate operative provision) should reflect applicable bribery and corruption legislation and may draw a distinction between employee acts which are independent of the employer and those which are not.

Other than as a consequence of a breach by the Contracting Authority of its obligations under this Agreement.

- (i) act in a reasonable and proportionate manner having regard to such matters as the gravity of any offense and the identity of the person committing it; and
- (ii) give all due consideration, where appropriate, to action other than termination of this PPP Contract.

“Private Partner Related Party” means:

- (a) an officer, servant or agent of the Private Partner, or any Affiliate [define] of the Private Partner and any officer, servant or agent of such a person;
- (b) any Sub-contractor or Sub-contractor of the Private Partner of any tier and any of their officers, servants or agents; and any person on or at the Site at the express or implied invitation of the Private Partner (other than a Contracting Authority Related Party).

Private Partner Default Termination Notice and Rectification

Clause YY.1

- (a) If a Private Partner Default has occurred and the Contracting Authority wishes to terminate the PPP Contract, it must serve a termination notice on the Private Partner.
- (b) The termination notice must specify:
 - (i) the type and nature of Private Partner Default that has occurred, giving reasonable details; and
 - (ii) that in the case of any Private Partner Default under limb [*material breach, Sub-contractor assignment, change of ownership, insurance*] of the definition of Private Partner Default this Agreement will terminate [sixty (60)] days after the date the Private Partner received the termination notice, unless:
 - (A) in the case of a breach under limb (a) [*material breach*] of the definition of Private Partner Default the Private Partner puts forward an acceptable rectification program within [thirty (30)] days after the date it receives the termination notice (and implements such program in accordance with its terms and rectifies the Private Partner Default in accordance with the program); or
 - (B) the Private Partner rectifies the Private Partner Default within [sixty (60)] days after the date it receives the Termination Notice; or
 - (iii) that in the case of any other Private Partner Default (not referred to in Clause [YY.1](b)(ii)), the PPP Contract will terminate on the date falling [thirty (30)] days after the date the Private Partner receives the termination notice.
- (c) If the Private Partner either rectifies the Private Partner Default within the time period specified in the termination notice, or implements the accepted rectification program, if applicable, in accordance with its terms, the termination notice will be deemed to be revoked and the PPP Contract will continue.

Remediable events
– adapt according
to project-specific
events included.

Irremediable
events.

- (d) If:
- (i) no acceptable rectification program has been put forward pursuant to Clause [YY.1](b)(ii)(A) and the Private Partner fails to rectify the Private Partner Default within the time period specified in the termination notice; or
 - (ii) the Private Partner fails to rectify the Private Partner Default within the time period specified in the termination notice pursuant to Clause [YY.1](b)(ii)(B),
- the Contracting Authority may give notice stating that the Contract will, subject to the terms of the Direct Agreement, terminate on the date falling [seven (7)] days after the date of service of such notice.
- (e) If the Private Partner fails to implement any rectification program in accordance with its terms, the Contract will, subject to the terms of the Direct Agreement, terminate on the date falling [seven (7)] days after the date of notice from the Contracting Authority to the Private Partner of such failure.

Drafting to tie in with notice terms, related clauses and obligations on handback.

PERSISTENT BREACH

Clause YY.2

- (a) If an Information Breach, or any other breach other than any breach for which performance point deductions could have been awarded and/or availability deductions could have been made, has continued for more than [x] days or occurred more than [x] times in any [x] month period then the Contracting Authority may serve a notice on the Private Partner:
- (i) specifying that it is a formal warning notice;
 - (ii) giving reasonable details of the breach; and
 - (iii) stating that such breach is a breach which, if it recurs frequently or continues, may result in a termination of this PPP Contract.
- (b) If, following service of such a warning notice, the breach specified has continued beyond thirty (30) days or recurred in [x] or more months within the [x] month period after the date of service, then the Contracting Authority may serve another notice on the Private Partner:
- (i) specifying that it is a final warning notice;
 - (ii) stating that the breach specified has been the subject of a warning notice served within the [twelve (12)]-month period prior to the date of service of the final warning notice; and
 - (iii) stating that if such breach continues for more than [x] days or recurs in [x] or more months within the [six (6)]-month period after the date of service of the final warning notice, the PPP Contract may be terminated.
- (c) A warning notice may not be served in respect of any breach which has previously been counted in the making of a separate warning notice.

7

LENDERS' STEP-IN RIGHTS



7.1 KEY ASPECTS

7.1.1 *The concept of step-in*

As described in [Section 4.1.1](#), “step-in” to a contract commonly means the ability of one party to take over certain rights and (in some cases) obligations of another party to that contract in specified circumstances. In the context of lenders who are not themselves party to the relevant contract, step-in typically means the ability to step into the shoes of their borrower if the borrower is defaulting under the relevant contract. This is usually for a limited timeframe and the aim is to give the lenders stepping in the opportunity to rectify the default and prevent termination of the contract. Lenders’ step-in rights under the PPP Contract are different to the Contracting Authority’s rights to step-in which are described in [Section 4, Contracting Authority Step-in Rights](#).

7.1.2 *Why do Lenders have step-in rights in respect of PPP Contracts?*

Most PPP Projects are financed on a “limited recourse” basis ([see Section C, PPP Contracts in Context](#)) under which third party lenders loan funds to the Private Partner based on an analysis of the projected cash flows generated under the PPP Contract.

As the PPP Contract is usually the sole source of revenue (or basis for revenue in the case of “user pay” PPP Contracts) for debt repayment, the prospect of the Contracting Authority terminating for Private Partner default is of significant concern for Lenders, particularly if the termination occurs before the asset has been completed and the service commenced. This is because even where a termination payment will be made by the Contracting Authority, the amount may not cover the entire debt amount and so Lenders are incentivized to get the PPP Contract back on track so that debt can be repaid as scheduled and in full.

One way Lenders seek to protect themselves against termination of the PPP Contract following Private Partner default is to negotiate step-in rights. Step-in rights are typically enshrined in an agreement between the Lenders and the Contracting Authority, often called a “Direct Agreement” or, in some jurisdictions, a “Consent Agreement.” The Direct Agreement will entitle the Lenders to be alerted to a potential termination and to take steps to prevent it by rectifying the problem. From the Contracting Authority’s perspective, its interest in completing the infrastructure and ensuring adequate service provision and the Lenders’ interests in achieving the same outcome are aligned. Direct Agreements enable Lenders to engage directly to try to save the PPP Contract before the Contracting Authority has to deal with termination and its consequences.

In a PPP context, direct agreements are executed not only in relation to the PPP Contract but also in relation to the Project Agreements. In the latter case, both the Lenders and the Contracting Authority may have separate direct agreements with the Private Partner’s Project Agreement counterparties (i.e. its main Sub-contractors) to ensure that the counterparties grant them similar opportunities to rectify defaults

by the Private Partner under the Project Agreements before the counterparties may terminate and also to ensure the counterparties' continued performance.⁷⁹ This [Section 7](#) focuses on Lenders' step-in rights in respect of the PPP Contract.

7.2 KEY CONSIDERATIONS FOR THE CONTRACTING AUTHORITY

7.2.1 Authority to execute Direct Agreement

In certain jurisdictions, there may be mandatory laws preventing the granting or enforcement of Lender step-in rights (in particular, under public policy rules applicable to insolvency procedures and/or public procurement regulations applicable to Contracting Authorities that have not been tailored to PPP Projects). Well-drafted PPP laws typically authorize entry by a Contracting Authority into both PPP Contracts and the Direct Agreements that usually accompany them. Accordingly, this should be carefully analyzed and addressed by Contracting Authorities before commencing the procurement of its PPP Contract.

CIVIL AND COMMON LAW DIFFERENCES

The validity and enforceability of step-in rights have rarely (if ever) been properly tested in court in any jurisdiction. Their formal existence gives Lenders comfort in terms of bankability and provides a framework within which the Parties can come together to negotiate solutions in a default/termination scenario, subject to the impact of mandatory law (for example with regard to receivership, bankruptcy and public procurement rules).

7.2.2 Form of Direct Agreement

Some jurisdictions have developed standard template provisions which must be used by Contracting Authorities and Lenders (e.g. the Dutch Model, the South Africa PPP Guidelines and the UK PF2 Guidance). The Direct Agreement is usually executed on the same date as the PPP Contract. In some instances it may be signed at a later date on financial close (as is the case in the Netherlands or the United States). Where this is the case, the Direct Agreement will have been virtually finalized at the time the PPP Contract was signed and such agreed form will be attached as an exhibit to the PPP Contract. Lenders typically will require an executed Direct Agreement as a condition precedent to drawdown under the Senior Finance Documents. From the Contracting Authority's perspective, it is preferable to have agreed on the form of the Direct Agreement in advance at the time of bid and under competitive tension, so that it is not introduced or re-negotiated post award of the PPP Contract.

7.2.3 Scope of Direct Agreement/governing law

The Contracting Authority should recognize that the Direct Agreement may be used as a vehicle for the Lenders to alter, clarify or add provisions which go beyond step-in arrangements. While it may in limited circumstances be helpful to include other provisions, the Contracting Authority should beware that this does not undermine the underlying risk transfer position agreed in the PPP Contract unless this is specifically agreed.

⁷⁹ In terms of order of exercise, the Lenders' rights under their Direct Agreement with a Sub-contractor will typically take priority over the Contracting Authority's rights under its Direct Agreement with the same Sub-contractor.

Given that the operation of the Direct Agreement can affect the Private Partner's rights and obligations under the PPP Contract as well as the Contracting Authority's, it is recommended that the Private Partner should also be party to the Direct Agreement to acknowledge and consent to its terms. It is also advisable for the governing law of the Direct Agreement and the PPP Contract to be consistent.

The scope of the Direct Agreement will vary between jurisdictions. In Australia, for example, there is not a formal step-in/step-out regime as in the UK, and there is generally an acknowledgement of the Lenders' right to rectify defaults without having to 'step in' and assume any obligations under the PPP Contract. Practically speaking, this would happen when an event of default occurs under the finance documents and the Lenders appoint a receiver to the Private Partner.

7.2.4 Main issues

Timing and duration of step-in – When the Contracting Authority serves a termination notice on the Private Partner it typically agrees to serve the same on the Lenders who then have a certain period to decide whether or not to step in. Lenders will also request this right when they have called a default under their financing agreements and accelerated their debt (in this circumstance the Private Partner will have to be replaced if the PPP Contract is to continue). The step-in period is usually agreed to be a reasonable length of time for the Lenders to try to rectify the problem or find a new Private Partner and will end when the agreed step-in period expires, the Lenders formally step out, a new Private Partner is appointed or termination occurs due to new default events. The Contracting Authority and its advisers should ensure that the time periods under the relevant agreements are correctly aligned so that the whole process can work effectively and, where applicable, to take into account any user impact.

Assumption of liabilities – The Contracting Authority should consider the extent to which it will require the Lenders to assume any liabilities which the Private Partner has already incurred or will incur in return for their step-in right.

It is generally accepted market practice that Lenders are required to pay any known liabilities outstanding at step-in, but the position as regards ongoing liabilities can vary. Where Lenders are required to agree to meet future liabilities in order to step in, they will want a capped amount so that they can quantify their exposure. This approach is seen in some jurisdictions (particularly in earlier PPP Projects in the UK) but there has been some movement away from this requirement in recent years (e.g. because the termination amount may in any event take account of liabilities owed to the Contracting Authority and if, conversely, the PPP Contract is not terminated, such liabilities will still be payable). One approach is that the Contracting Authority can notify the Lenders of subsequent liabilities and if the Lenders choose not to meet them then the Contracting Authority can proceed to terminate the PPP Contract (and the liabilities will again be taken into account in the termination payment).

Rectification rights – It is in the Contracting Authority's interests for breaches to be rectified but it also needs to protect itself against failures to remedy and new breaches by ensuring it still has a right to terminate in respect of these new failures that arise during the step-in period.

Other protections – The Contracting Authority may want to try to include certain provisions which restrict the Lenders’ exercise of certain rights under the financing documents (e.g. in relation to set-off) and to regulate priority of security enforcement between the Contracting Authority and the Lenders (this is the case, for example, in Australia).

7.3 SUMMARY OF MAIN PROVISIONS

A Direct Agreement should typically contain a clear and unequivocal step-in regime including the following main provisions (or their equivalent under the laws of the relevant jurisdiction):

- (1) mutual obligations on the Parties to notify each other, respectively, of (a) a Private Partner default under the PPP Contract which could allow the Contracting Authority to terminate the PPP Contract and (b) key events under the senior finance documents which could impact the Contracting Authority (e.g. such as an event of default or acceleration of debt);
- (2) a standstill period, pursuant to which the Contracting Authority will undertake to notify the Lenders of its intention to terminate the PPP Contract, and will commit not to terminate the PPP Contract for a given period of time (nor to terminate any related agreements);
- (3) appointment of the Lenders’ nominee to “step in” and become jointly liable with the Private Partner to perform the PPP Contract and cure any breaches which gave rise to the Contracting Authority’s right to terminate (and to “step out”). Approving the identity of a nominee at contract signature is not usually advisable as they may no longer subsist at the relevant time. It is more usual instead to agree any criteria that a nominee will need to satisfy to be acceptable to the Contracting Authority;
- (4) consent to the assignment of the PPP Contract and related receivables to the Lenders, as well as consent to assignments to insurers and guarantors upon payment of claims;
- (5) provision for relevant payments (such as termination payments) to be made direct to the Lenders by the Contracting Authority (*see also Section 8.6, Termination Payments*);
- (6) Lenders’ right to novate the Private Partner’s rights and obligations under the PPP Contract to a substitute private partner of their choice (subject to the consent of the Contracting Authority and/or to any reasonable and objective criteria) and the Contracting Authority’s obligation to enter into a new direct agreement with the Lenders to the new Private Partner on substantially equivalent terms; and
- (7) a clear statement as regards whose step-in right takes priority, where both the Contracting Authority and the Lenders have contractual rights to step into the PPP Contract. Typically the Lenders will have first step-in right.

7.4 SAMPLE DRAFTING 7

As indicated above, the terms of the Direct Agreement are normally not outlined in the PPP Contract (although the agreed form may be appended to the PPP Contract) which is why this Guidance does not include proposed drafting.⁸⁰

⁸⁰ For further information and sample drafting from a more Developed Market, please see the South Africa PPP Guidelines and the UK PF2 Guidance.

8

TERMINATION PAYMENTS



8.1 KEY ASPECTS

8.1.1 *The concept of a termination payment*

In commercial contracts where compensation on termination for specific reasons is not addressed specifically, the parties will rely on the chosen dispute resolution method for determining the amount of any damages should termination occur. This may involve bringing a court action. Generally speaking, where there is an innocent party, they will be the party seeking damages. However, even a defaulting party may be entitled to compensation under general law to fairly reflect the value of any works or services it has carried out. In certain contracts, rather than relying on general law, there may be a need to agree upfront the level of compensation payable if termination events occur for specific reasons.

8.1.2 *Why do PPP Contracts contain termination payment provisions?*

Market practice has shown that Lenders are not prepared to lend to PPP Projects without reasonable assurance that they will be repaid. In carrying out their detailed due diligence, Lenders are keen to ensure that their debt is protected on any early termination of the PPP Contract, regardless of fault and without having to rely on lengthy and potentially uncertain legal proceedings to determine the level of compensation. Equity Investors, similarly, will want to expressly protect their equity investment in circumstances where termination occurs through no fault of their own or of the Private Partner.

Although legal proceedings may ultimately result in termination compensation being payable by the Contracting Authority, it is the level of certainty provided by express contractual provisions which is key for Lenders in agreeing to commit funding to the PPP Project. Termination payments are a key element of the risk allocation in a PPP Contract and are essential in achieving a bankable PPP Project. This applies across both established and less Developed Markets in both common and civil law jurisdictions, although the precise terms will vary according to the particular PPP Project circumstances.⁸¹

The grounds for termination and the consequent payments can be complex. They are included in the PPP Contract to give both Parties certainty as to the mechanics and effects of termination. This in turn enables the Lenders to price their debt based on a lower risk profile as regards repayment risk, which in turn feeds though into the price bid by the Private Partner for the PPP Contract.

⁸¹ See the Global Infrastructure Hub's *PPP Risk Allocation Tool 2019 Edition* – e.g. the early termination (including any compensation) entries in its risk matrices. [See link in Appendix A, Additional PPP Resources.](#)

EMERGING AND DEVELOPED MARKET DIFFERENCES

Underlying the Lenders' analysis of their likely debt repayment will be an assessment of the strength of the Contracting Authority's covenant to pay (i.e. its ability to pay any termination payment), including the scope and nature of their rights under the Direct Agreement, and the enforceability of such payment obligations (*see Section 11, Governing Law and Dispute Resolution*). Where there is no alternative, Lenders may accept reliance on underlying law to determine termination and compensation rights, but this is likely only to be viable in stable and established legal regimes and in limited circumstances.

A key concern for Lenders in some jurisdictions relates to the requirement for parliamentary approval of appropriations in respect of contingent liabilities under project contracts (*see Section 8.6, Termination Payments*).

In cases of weak or uncertain Contracting Authority credit, additional credit support may be sought by the Private Partner and its Lenders. This may be the case, for example, in less stable regimes or Emerging Markets or where the Contracting Authority is not part of central government. Support may be available via multilateral or export credit agencies or central government.

8.1.3 Types of termination event

The list of events which can lead to termination will vary from one PPP Contract to another and should be tailored to take account of the specific risks and obligations involved in the relevant PPP Project.

CIVIL AND COMMON LAW DIFFERENCES

Each Party should make sure it understands how underlying law may affect certain termination scenarios under the PPP Contract. For instance, in some jurisdictions (more typically civil law) the Contracting Authority may be entitled to terminate the PPP Contract for convenience or on the grounds of public interest even without an express contractual right. Similarly, the Private Partner may be expected to rely on its rights at general law to terminate for Contracting Authority default instead of having an express right (as has been the case in some PPP Projects in civil law France⁸² and jurisdictions in common law Australia). *See Section 6.3.1.*

Early termination events which may be expected to lead to termination compensation are described in *Section 6.1.3* and include:

Contracting Authority default termination – by the Private Partner where the Contracting Authority fails to comply with its material obligations (which are primarily payment obligations if under the availability payment model).

⁸² In France, in most cases, the PPP Contract is silent and the Private Partner would typically be expected to apply to court for the right to terminate the PPP Contract.

- (a) Voluntary termination – by the Contracting Authority at its discretion for convenience or for public policy reasons (also known as termination for public policy).
- (b) Private Partner default termination – by the Contracting Authority where the Private Partner fails to comply with its material obligations.
- (c) Specific events such as MAGA and change in law will typically have similar compensation consequences where no solution has been agreed to continue with the PPP Contract and termination occurs. Typically both Parties have the right to terminate. *See Section 2, Material Adverse Government Action and Section 3, Change in Law.*
- (d) Prolonged Force Majeure or Uninsurability (and certain other prolonged delay events as described in *Section 6.1.3(d)*) – by either Party where no solution has been agreed to continue with the PPP Contract. *See Section 1, Force Majeure, Section 2, Material Adverse Government Action and Section 3, Change in Law.*

8.2 KEY CONSIDERATIONS FOR THE CONTRACTING AUTHORITY

8.2.1 Certainty

Simple and objective calculation methods will provide greater certainty for all Parties, minimizing the risk of disputes and enabling less risk premium to be costed into the Private Partner’s price. Equity and debt elements to be compensated must be clearly defined and understood by all Parties, including any financing breakage costs (e.g. under interest rate hedging arrangements), any “make-whole” payments (e.g. in respect of fixed rate loans⁸³ or bonds) and any default interest. As mentioned above, the inclusion of an express termination payment provision in the PPP Contract will not necessarily result in any greater liability on the Contracting Authority than would be the case if there was no express provision and the matter was determined under applicable law through the contractual dispute resolution process, but the certainty provided is key to bankability.

8.2.2 Understanding relevant agreements

Where termination compensation provisions are defined by reference to Lenders’ financing agreements (including any hedging arrangements and the financial model), equity agreements (e.g. subordinated loan documents) or the Project Agreements, the Contracting Authority and its advisers must review and approve the agreements and arrangements involved. The Contracting Authority should also require approval rights in relation to changes to such agreements and arrangements which could affect its liability (or the PPP Contract must be clear that any unapproved adverse changes will not be taken into account in calculating the Contracting Authority’s liability). The Contracting Authority and its advisers should only need to review the parts of the documentation which are relevant to the PPP Contract and suitably redacted copies may suffice for their review.

⁸³ Fixed rate debt provided by institutional and non-institutional lenders has become increasingly common over the past five years in Developed Markets such as the Netherlands, although even in Developed Markets generally, fixed rate PPP loans from bank lenders remain rare.

An additional approach is to set out financial figures in the PPP Contract based on the Original Base Case to represent a cap on the Contracting Authority's liability. The actual sums involved on a termination should still be reviewed but this approach can give the Contracting Authority comfort as regards its maximum exposure. The debt figures should however be adjusted on a realising value refinancing (*see Section 5.1.3*), for example, to reflect a reduced liability for the Contracting Authority.

8.2.3 Deductions

The Private Partner may have cash standing in certain bank accounts (e.g. its current account, debt service reserve account, maintenance retention/reserve or lifecycle fund accounts or any collateral account into which e.g. bond proceeds are drawn). The Contracting Authority should consider how these cash balances should be treated and whether they should be set off against any compensation due to the Party which ultimately receives such cash. Consideration also needs to be given to how to treat insurance proceeds (*see Section 1.2.1.4*) and any net payments the Private Partner might receive as a result of closing hedging arrangements early, as well as any outstanding claims against, or amounts owed to it by, its counterparties under the Project Agreements. Deductions in respect of the handback condition of the asset should where possible also be factored into any calculations to the extent the Private Partner has not complied with its remediation obligations in this regard. *See Section 8.7, Sample Drafting 8, Schedule, definition of "Outstanding Senior Debt" and Section 9, Handback of Assets at End of Contract.*

8.2.4 Framework for negotiation

It is important to note that, in practice, termination provisions provide a backdrop for the Parties (and the Lenders) to initiate discussions about how to continue the PPP Contract where there is a risk of termination. It is usually in all parties' interests to find a way to continue the PPP Project and avoid termination and from the Contracting Authority's perspective, although it needs to protect the use of public funds, it also has a duty to provide public services. Negotiating a way to continue the PPP Contract which works for all parties may be the best way to achieve this and avoids triggering a termination payment liability.

8.2.5 Other termination consequences

In addition to the termination payment itself, the Contracting Authority will want to ensure the PPP Contract contains adequate provisions addressing other consequences of termination, such as transfer by the Private Partner of the PPP Project asset, handover arrangements and access to information necessary for continuing to operate or construct the PPP Project. *See Section 9, Handback of Assets at End of Contract.*

8.2.6 Principles for the calculation of termination payments

The amount payable to the Private Partner upon early termination of the PPP Contract will depend on the grounds on which the PPP Contract is terminated, so it is important for the Contracting Authority to understand the different rationale in each case. *Section 8.7, Sample Drafting 8* is based on the principles set out below in *Sections 8.3–8.6*.

8.3 COMPENSATION ON CONTRACTING AUTHORITY DEFAULT, MAGA, CHANGE IN LAW OR VOLUNTARY TERMINATION

8.3.1 Market practice

If the PPP Contract is terminated on the grounds of Contracting Authority default, MAGA, change in law or voluntary termination, market practice is that the Private Partner should be fully compensated by the Contracting Authority as if the PPP Contract had run its full course. This reflects the principle that these categories of termination event are considered a Contracting Authority risk and responsibility. It also reflects the likely position should the Private Partner instead have to sue for damages on these grounds under general law.

In these circumstances, the Private Partner will expect an amount which repays the sums used to finance the PPP Project (equity and debt), as well as compensates for the equity return it had forecast (for a specified number of years to be negotiated between the Parties but typically for (and limited to) the remaining term of the PPP Contract). In order to be left in the same position as if the PPP Contract had not been terminated, the Private Partner will also expect the amount to include compensation for costs payable as a result of the early termination of specified financing agreements and Project Agreements, as well as related employee redundancy payments incurred. If the PPP Project has been funded in the bond markets or by fixed rate loans, a “make-whole” payment may be payable to the bondholders or relevant fixed rate lenders in these circumstances to compensate them for the early repayment of their investment. [See Section 12.4.2, Bond Financing.](#)

As mentioned in [Section 2, Material Adverse Government Action](#), there may be scope for the Contracting Authority to negotiate a slightly reduced level of termination compensation for MAGA events which are less directly within its control (this payment would still cover at least outstanding debt and contributed equity).

CIVIL AND COMMON LAW DIFFERENCES

The Contracting Authority should not be “unjustly enriched” by receiving an asset for which it has not paid the expected contractual price. Some jurisdictions (typically civil law) have an underlying unjust enrichment principle and this might affect the drafting of any termination provisions in its PPP Contract.

8.3.2 Compensation approach

There are two “full” compensation methods which the Contracting Authority will need to consider in the case of compensation on Termination on Contracting Authority default, MAGA, change in law and voluntary termination:

- (a) **Book value compensation:** this is based on the investment costs the Private Partner incurs in building the PPP Project. Third party costs as described in [Section 8.3.3.3](#) would be added on top of such book value. This method is not as commonly used and although it is relatively clear and simple, it is generally not recommended as it is not guaranteed to compensate the Private Partner fairly. There is a risk of underpayment (which would create bankability issues for Lenders) or overpayment

(which may wrongly incentivize the Private Partner). There may also be problems if accounting rules change during the life of the PPP Contract. It should be noted that the book value of the PPP Project assets is unlikely to take into account their physical state.⁸⁴

- (b) **Financing-based compensation:** this is based on the financing for the PPP Project (e.g. senior debt (whether in the form of bank or bond finance), subordinated debt and equity), again with third party costs (as described in [Section 8.3.3.3](#)) added on top. This approach is more common across the PPP market and is the recommended approach in this Guidance. *See further detail in Section 8.3.3 and Section 8.7, Sample Drafting 8, Schedule, Clause (1).*

8.3.3 Components of Financing-based compensation

As mentioned in [Section 8.3.2](#), this type of termination payment is made up of compensation in respect of senior debt (*see Section 8.3.3.1*), equity (*see Section 8.3.3.2*) and third party costs (*see Section 8.3.3.3*). These components are explained more fully below. Applicable deductions should always be taken into account (*see Section 8.2.3*).

8.3.3.1 Compensation in respect of outstanding senior debt

This payment will typically consist of:

- (i) principal outstanding under the senior finance documents (whether bank or bond financing) (which may be capped by reference to forecast amounts in the Original Base Case); plus
- (ii) interest, penalties and fees (and make-whole payments on any bond or fixed rate loan); plus
- (iii) breakage costs arising under applicable hedging agreements or floating rate loans;

LESS certain amounts, such as:

- (a) amounts credited to the bank accounts of the Private Partner (which are secured to the benefit of the Lenders);
- (b) net payments received as a result of the termination of the hedging agreements and, in some cases, profits from pre-paying fixed rate loans;
- (c) insurance proceeds received or due to be received before the termination payment date; and
- (d) generally any other sums recovered by the Lenders before the termination payment date.

See Section 8.2.3 and Section 8.7, Sample Drafting 8, Schedule, Clause (1)(a) and relevant definitions.

⁸⁴ This approach is not in [Section 8.7, Sample Drafting 8](#).

8.3.3.2 Compensation in respect of equity

There are essentially three different options the Contracting Authority should consider in respect of equity compensation. These are all likely to lead to different outcomes so the Contracting Authority should be guided by the key considerations in [Section 9.2, Handback of Assets at End of Contract](#), as well as by the circumstances of the PPP Project. *See Section 8.7, Sample Drafting 8, Schedule, Clause (1)(d).*

- (a) **Original Base Case Approach (Option 1(a)):** in this approach, the amount payable is determined by reference to the Original Base Case. The Contracting Authority pays a sum which, when taken together with all amounts already paid to the Equity Investors before the date on which the PPP Contract is terminated, will ensure that the Equity Investors recover Base Case Equity IRR.

The key benefit of this approach lies in its easy implementation and certainty and the fact that it leaves less room for dispute than other approaches.

A material drawback, however, is that this option assumes that the Private Partner has been performing as planned in the Original Base Case – it does not take into account the actual performance of the Private Partner under the PPP Contract. From the Contracting Authority’s perspective, this may over-compensate the Private Partner if it has been performing worse than expected in the Original Base Case and arguably there may be a stronger incentive on the Private Partner to ensure the PPP Project is terminated. Conversely, if the Private Partner has been performing better than expected it will be undercompensated and arguably may be concerned that this might incentivize, or result in political pressure on, the Contracting Authority to terminate the PPP Contract early. *See Section 8.7, Sample Drafting 8, Schedule, Clause (1)(d), (a).*

- (b) **Market Value Approach (Option 1(b)):** in this approach, the amount payable is determined by assessing the price which third party investors would be willing to pay for (i) the shares in the Private Partner and (ii) the receivables arising under subordinated debt, subject to certain assumptions (including that the event giving rise to the early termination had not occurred).

Compared to the Original Base Case Approach (Option 1(a)), this option takes full account of the actual performance of the Private Partner under the PPP Contract so is fairer on that front.

However, this method is complex to implement in practice and the result could be undesirable on both sides – the Contracting Authority could pay more than expected under the Original Base Case and the Private Partner’s Equity Investors may feel their interests are not sufficiently protected in circumstances that are largely beyond their control. It may be difficult to establish a market value (particularly if no market exists) and this could lead to disputes. *See Section 8.7, Sample Drafting 8, Schedule, Clause (1)(d), (b).*

- (c) **Adjusted Base Case Approach (Option 1(c)):** under this approach, the amount payable is determined by reference to the distributions which Equity Investors would have expected to receive under the Original Base Case, but only from the termination date. The amount payable will be the aggregate amount of distributions forecast in the Original Base Case to be made after the termination date, discounted using the Base Case Equity IRR.

This approach takes into account the performance of the Private Partner under the PPP Contract up to the termination date. It also provides greater certainty as it does not require a market valuation mechanism and is easier to implement.

However, it does not take into account likely actual performance in respect of the period after the termination date, so (as highlighted under the Original Base Case Approach (Option 1(a)) the Contracting Authority may be over or under-compensating the Private Partner for that period. This will have a greater impact the earlier termination occurs. *See Section 8.7, Sample Drafting 8, Schedule, Clause (1)(d), (c).*

8.3.3.3 Compensation in respect of third party costs

The Private Partner is likely to incur certain other costs as a result of early termination of the PPP Contract, including employee redundancy costs, as well as other costs payable to its Sub-contractors in accordance with the terms of the relevant Project Agreements. The general principle is that the Private Partner and its Sub-contractors should be no worse nor better off as a result of the early termination. While market practice is for these costs to be included in the compensation payment for this category of termination, the scope may vary depending on the jurisdiction. Key points for the Contracting Authority to bear in mind include:

- **Reviewing the Project Agreements** – as with the financing agreements, before PPP Contract signature the Contracting Authority and its advisers should review the Project Agreements to assess any early termination provisions which may give rise to third party cost compensation. In particular, the Contracting Authority will want to ensure there are no excessive termination payments included in contracts with parties who hold shares in the Private Partner and are sub-contracted to it.
- **Defining and capping liabilities** – as far as possible the PPP Contract should set out the precise scope of compensation for third party costs. As third party costs can be significant and fluctuate over time, the Contracting Authority may wish to seek to cap its liability in this respect, although typically this is achieved by defining the eligible items as opposed to setting a monetary cap. The Contracting Authority should also oblige the Private Partner to mitigate costs. Both liability caps and mitigation obligations should be reflected in the Project Agreements themselves.
- **Compensating for loss of profit** – one of the key commercial issues the Contracting Authority will also need to address is the extent to which compensation should cover the loss of future profits for the Sub-contractors – this may be achieved by limiting the number of years.
- **Redundancy costs** – careful consideration needs to be given to compensation for redundancy of staff employed by the Private Partner and/or its Sub-contractors. Such compensation will likely depend on applicable law and the ability to redeploy affected staff.

See Section 8.7, Sample Drafting 8, Schedule, Clauses (1)(b) and (c).

8.4 COMPENSATION ON PRIVATE PARTNER DEFAULT TERMINATION

8.4.1 Market Practice

In the case of termination by the Contracting Authority on the grounds of Private Partner default, market practice is that the PPP Contract should expressly provide for some amount of compensation. While this may at first seem at odds with the reason for termination, there is in fact some strong justification:

- (a) the Contracting Authority could otherwise benefit from a Private Partner default by unjust enrichment (e.g. taking a built asset without having paid for it) and could in theory be incentivized to terminate the PPP Contract. This could result in legal proceedings being brought by the Private Partner which may ultimately result in the Contracting Authority being liable to pay compensation, as well as legal costs incurred;
- (b) without the certainty of an express provision, the Private Partner will likely have to price more risk into its bid and therefore the Contracting Authority will be paying more in the ordinary course of the PPP Contract even though termination on these grounds may never happen;
- (c) market practice shows that Lenders have typically been reluctant to agree to finance a PPP Project constructed and operated by an SPV where no compensation is expressly payable to them in these circumstances (i.e. the PPP Project will not be bankable). While there is an argument that the risk of no compensation will encourage Lenders to step in and rescue a troubled PPP Project, the market has in general moved away from this for the reasons above. There are some examples of the no compensation approach in some early PPP Contracts in the UK and it is also seen in some projects in the U.S. market, for example, but this approach is resisted by Lenders in projects where the risks in respect of project failure and of the ability to rescue it are considered high (e.g. from a technical or resourcing perspective, or because the market is untested), and the overall security package available to Lenders is otherwise insufficient to cover their debt; and
- (d) the Private Partner still usually loses its equity investment and the return on its equity which is its main driver for undertaking the PPP Project in the first place. [See Section 8.7, Sample Drafting 8, Schedule, Clause \(2\).](#)

The Contracting Authority will want to weigh up the likelihood of the termination payment arising against the benefit of procuring private finance. In doing so, the following factors are relevant:

- (i) the Contracting Authority has control over serving the termination notice that triggers such payment – this will also be a factor in its favor in bringing all parties to the negotiating table in a potential termination scenario; and
- (ii) the Contracting Authority has the ability to mitigate against the risk of Private Partner default even before the PPP Contract is signed, by selecting the Private Partner after a thorough and fair procurement process and evaluation of the soundness of all elements of its bid.

8.4.2 Compensation approach

Although market practice is to pay compensation on Private Partner default termination, the Contracting Authority needs to choose a method which does not result in overly generous compensation. This would not properly incentivize the Private Partner to perform (nor its Lenders to due diligence the PPP Project thoroughly or exercise their rights to monitor and step into the PPP Project); it would also raise value-for-money concerns. The options are outlined below. Applicable deductions should always be taken into account (*see Section 8.2.3*).

- (a) **Debt-based compensation:** under this approach, the Private Partner (or in reality the Lenders) is compensated based on the amounts payable under the Senior Finance Documents (whether bank or bond) (i.e. an amount based on the formula under *Section 8.3.3.1* or which may alternatively be set out and capped in the PPP Contract as described in *Section 8.2.2*). The PPP Contract must clearly define the debt elements to be compensated and also applicable deductions of amounts available to Lenders (such as proceeds received on close-out of the hedging arrangements, insurance proceeds and amounts in bank accounts which may include e.g. maintenance reserves and bond proceeds held in a collateral account).

EMERGING AND DEVELOPED MARKET DIFFERENCES

This debt-based compensation method is the most common approach in Emerging Markets.

As the main or only beneficiary of compensation upon termination for Private Partner default, Lenders will tend to look for the highest possible recovery rate for their loan and the simplest/most objective solution possible. As a result, debt-driven approaches are likely to be more satisfactory to them. Whether the amount reflects the value of the PPP Project is less clear and the Contracting Authority will need to consider this in its value-for-money analysis.

One major drawback of this method is that Lenders have limited incentive to ensure that the project performs or to step in to save it. To counter this risk and ensure Lenders have an incentive to conduct proper due diligence and exercise their monitoring and step-in rights, Contracting Authorities may be able to specify that the level of compensation is a percentage of the total outstanding debt (and not the full amount), in addition to making appropriate deductions as described in *Section 8.2.3*. This is commonly referred to as a “haircut”. It should be noted that Lenders may not accept the risk of a haircut in all circumstances and this will depend on a variety of factors (such as the specific country and sector in which the PPP Project is conducted, the likelihood of project failure and of the ability to rescue it, and the overall security package available to the Lenders). If Lenders are unable to accept a haircut, there is a risk that this will result in insufficient interested bidders or even none for the project. The exact percentage of a haircut (if any) should be assessed on a project-by-project basis. In projects where a haircut has been agreed, this has typically ranged from 5-20% (the upper end of the range seen in some U.S. projects). In addition, in the context of a bond financing, consideration should be given as to whether make-whole payments should be included. *See Section 8.7, Sample Drafting 8, Schedule, Clause (2)*.

An alternative (or addition) could be to refer to an amount of outstanding senior debt minus unfunded equity contributions if these are required under the relevant financing documents – the Lenders would then look to recover that amount from the Private Partner/Equity Investors through its project security arrangements.

- (b) **Market value:** where the PPP market is sufficiently liquid and there is a reasonable prospect of the PPP Contract being re-tendered, the fairest approach is to calculate the compensation payable to the Private Partner by reference to the market value of the PPP Contract, as determined by a tendering procedure. This ensures, in theory, that the Contracting Authority will not pay the Private Partner more than the remaining value of the PPP Contract. As a result, this calculation protects the Contracting Authority's interests while ensuring that the Contracting Authority does not unfairly benefit from the Private Partner's default.

The fall-back position if there is no liquid market, or if the Authority chooses not to go down this route for any reason, is that the compensation payment is calculated on the basis of the estimated value that would have been obtained in a re-tendering, as determined by an independent, third party appraiser. While seemingly straightforward to implement, setting the parameters may require some negotiation, and it may not reflect the true market value of the PPP Contract. This approach is seen in countries with Developed Markets (such as Belgium, Australia⁸⁵, the Netherlands and also South Africa).

EMERGING AND DEVELOPED MARKET DIFFERENCES

The market value approach is likely to be more suitable for a Developed Market where there are likely to be a number of potentially interested purchasers in the relevant sector. Lenders to PPP Projects in certain jurisdictions or in relation to certain assets may be reluctant to rely on a market-based valuation method for fear of undervaluation or underpayment. This is particularly likely to be the case in Emerging Markets where there is a limited PPP track record and a limited market. The South Africa PPP Guidelines acknowledge this and provide for an additional payment to be made by the Contracting Authority to the extent the market value approach does not yield a certain percentage of outstanding debt.

Contracting Authorities should take a view as to whether market-based termination compensation is a viable option on a project-by-project basis.⁸⁶

- (c) **Book Value:** although seen in some European jurisdictions, the calculation of compensation payments based on book value is not the recommended approach in this Guidance as the result may not accurately reflect the reality of the sums owed.⁸⁷ *See discussion under Section 8.3.2(a).*

⁸⁵ See the Infra Australia PPP Guidelines (for Social Infrastructure).

⁸⁶ This option is not in [Section 8.7, Sample Drafting 4](#) – for more detail see the South Africa PPP Guidelines, Infra Australia PPP Guidelines (for Social Infrastructure) and the UK PF2 Guidance.

⁸⁷ A “hybrid” approach may also be considered in some cases e.g. where termination compensation is equal to the lesser of the appraised market value and outstanding senior debt. This approach has been taken by some State authorities in the United States.

8.5 COMPENSATION ON FORCE MAJEURE TERMINATION

As discussed in [Section 1, Force Majeure](#), each Party should have the right to terminate the PPP Contract as a result of prolonged Force Majeure and compensation is calculated to reflect the principle that Force Majeure is considered a shared risk. In this case, the risk is shared by virtue of the Contracting Authority being liable for a less than full compensation payment and having the right to take over the relevant asset, while the Private Partner loses any return on its equity investment (i.e. the profit element which will have been at the heart of its decision to bid for and undertake the PPP Project in the first place) and possibly some of its invested equity. The potential consequences will incentivize both Parties to find a solution to a prolonged Force Majeure before termination occurs.

Subject to adjustments on a case-by-case basis, the principle is that the Private Partner is paid an amount representing:

- (i) the amount of outstanding senior debt (based on the formula in [Section 8.3.3.1](#) but probably not including a make-whole payment on any bonds); plus
- (ii) the amount of equity invested (taking into account any distributions already paid), but not loss of profit (in some cases, for example in Australia, a haircut may also be applied to further reflect the shared risk principle); plus
- (iii) an amount in respect of redundancy and Sub-contractor break costs (based on the principles set out in [Section 8.3.3.3](#)).

A similar approach is usually followed in any termination for uninsurability and, for example, in respect of the Dutch prolonged delay event referred to in [Section 6.1.3\(d\)](#) (although in the latter case, the compensation terms are slightly enhanced with, for example, a small element of equity return included). In each case, applicable deductions should always be taken into account ([see Section 8.2.3](#)). [See Section 8.7, Sample Drafting 8, Schedule, Clause \(3\)](#). It may also be possible for the Contracting Authority to negotiate no or reduced compensation in specific circumstances. [See Section 1.2.5, Force Majeure](#).

While it may seem that the Lenders' exposure is more limited, this comes back to the issue of bankability, and the decision facing Lenders as to where to put their funds to best advantage. The Contracting Authority will want to weigh up the risk of a Force Majeure termination occurring (again why close attention to the definition of Force Majeure is so important) against the benefit of achieving the private finance it wants, at a reasonable price, having chosen PPP as its procurement method.

8.6 METHOD AND TIMING OF PAYMENT

The method of payment of the termination compensation will also need to be considered by the Contracting Authority. Generally speaking, providing for payment by lump sum in the PPP Contract seems more typical market practice, but there are a number of factors to take into account, including the grounds for termination:⁸⁸

- **Payment capacity** – the Contracting Authority will need to assess whether it will be able to pay a lump sum if such a large payment may not be budgeted for or have backing from its government treasury department. Payment over time may be preferable and the Contracting Authority should in any event try to negotiate a reasonable period of grace long enough to raise the necessary funds (e.g. including, where applicable, factoring in the time needed to go through any applicable parliamentary legislative or appropriations processes). In the Philippines, for example, the government requires a two-year grace period for the payment of termination compensation as this is the maximum period of time for the parliamentary appropriation process.
- **Private Partner/Lender perspective** – it is likely that the Private Partner and its Lenders will favor a lump sum payment. This is particularly the case on Contracting Authority default termination as the most likely cause is failure to pay. The Private Partner and its Lenders will typically want to close off their exposure to a terminated PPP Project and avoid Contracting Authority credit risk as soon as possible. As flagged in [Section 8.1.2](#), Lenders may be concerned if parliamentary approval of appropriation in respect of termination payments is a necessary and potentially lengthy process, as is the case in some jurisdictions (e.g. the Philippines).

On Private Partner default termination Lenders are again likely to resist payments over time (and are likely to be the only Party receiving compensation). They are also likely to resist payments over a period longer than the remaining life of the loan or bond, especially if to receive such payments on a longer schedule would cause additional break costs (particularly to non-bank funders).

- **Interest** – payment over time will incur interest costs for the Contracting Authority, usually from the date the payment is recognized as due until the final payment. If the Contracting Authority does select this method, it will need to consider an appropriate interest rate.
- **Asset transfer** – Lenders may be reluctant to release security interests held over the PPP Project assets until compensation payments have been made in full. This may make the transfer of relevant assets back to the Contracting Authority difficult. In certain circumstances, the Contracting Authority may be able to negotiate an interim solution at the time of the termination, such as an arrangement pursuant to which the Contracting Authority has a right to access the PPP Project assets during the period from the termination date until all termination compensation is paid, so long as the Contracting Authority complies with the payment terms with respect to such compensation. This approach is unlikely to be agreed at contract signature and certain issues will need to be clearly addressed (such as liability

⁸⁸ See [Section 6, Termination Events](#).

for damage to the asset while in the Contracting Authority's use). In jurisdictions where Lenders typically take security over the Private Partner as opposed to the project assets, this will not be an issue (see [Section 9.2.8](#)).

- **Set-off rights** – the Contracting Authority should try to negotiate the right to set off any amounts due to it from the Private Partner under the PPP Contract against any compensation it pays (unless these are already taken into account in the relevant formula). Lenders, however, will in general be reluctant to give the Contracting Authority any set-off rights, particularly where compensation is debt-based.
- **Payments to other parties** – the PPP Contract is entered into by the Contracting Authority and the Private Partner and termination payment provisions should be drafted to reflect the payments that are owed by one Party to the other, even where elements of the payment are essentially to be passed on to third parties (such as Lenders or Sub-contractors). Obligations on the Contracting Authority to make direct payment to those third parties of such amounts will typically be included in direct agreements with those parties, which the Private Partner will acknowledge by being party to such agreements or through mandatory clauses included in Sub-contracts between the Private Partner and its Sub-contractors.

8.7 SAMPLE DRAFTING 8

The provisions relating to the calculation of termination payments are generally set out in a Schedule to the PPP Contract.

Schedule [insert number] – Termination Payments

Required Definitions

"Bonds"	means the [●] bonds due [●] of the Issuer, issued at [Financial Close], in the aggregate principal amount of [●].
"Distribution"	means: <ul style="list-style-type: none"> (a) the payment of a distribution by the Private Partner (whether directly or indirectly) to its Shareholders; (b) any dividend, charge, fee or other distribution (or interest on any unpaid dividend, charge, fee or other distribution) (whether in cash or in kind) declared, paid or made on or in respect of share capital (or any class of share capital) in the Private Partner; (c) the redemption, repurchase, defeasance, retirement or repayment of any share capital of the Private Partner, including in connection with any merger or consolidation, or any resolution to do so.
"Initial Equity"	means, as at the Termination Date, the initial equity investment disbursed by the Shareholders plus any such other equity contributions approved by the Contracting Authority, less the Distributions paid by the [Private Partner] to its Shareholders as at the Termination Date.
"Issuer"	means [insert company name, registered number and country of registration]. [assuming Issuer is different entity to Private Partner]
"IRR"	means internal rate of return.
"Losses"	means all damages, losses, liabilities, costs, expenses (including legal and other professional charges and expenses), and charges whether arising under statute, contract or otherwise, internal costs or demands.
"Make-Whole Payment"	means: <ul style="list-style-type: none"> (a) in relation to termination of the PPP Contract under Clause [●] (Termination on Contracting Authority Default) [Change in Law] [MAGA], the Make-Whole Payment to be made pursuant to and in accordance with Condition [●] of the Bonds; (b) in relation to termination of the PPP Contract under Clause [●] (voluntary termination), the modified Make-Whole Payment to be made pursuant to and in accordance with Condition [●] of the Bonds; and (c) in relation to termination of the PPP Contract in any other circumstances, zero.
"NPV"	means net present value.

NB see Section 12.4.2 in respect of Emerging Markets.

"Original Base Case"

means the financial model agreed between the Parties dated [] for the purpose of, amongst other things, calculating [*insert defined term of availability payment in a "user pays" model /Equity IRR etc.*] [as attached at [Schedule [●]], as updated from time to time in accordance with the terms of this PPP Contract.

Contracting Authority should approve changes to the model; otherwise such changes should not affect its potential liabilities on termination or otherwise. See also Section F, PPP Contracts in Context and Section 5, Refinancing.

"Outstanding Senior Debt"

means the sum of: [*See Section 8.2.3, Deductions and Section 8.4.2(a)*]

- (a) the total amount outstanding at the Termination Date to the Lenders under any Senior Finance Documents and accrued but unpaid interest and including default interest; plus
- (b) any winding-up costs, prepayment charges [(including any Make-Whole Payments)] [except on termination for Force Majeure or Private Partner Default], costs of terminating any hedging arrangements or other breakage costs, payable by the Private Partner [or the Issuer] to the Lenders as a result of a prepayment of sums due under the Senior Finance Documents, or, in the case of early termination of interest rate hedging arrangement, as a result of termination of the PPP Contract, subject to the Private Partner[, the Issuer] and the Lenders mitigating all such costs [unless the amount, or the formula for determining the amount of such costs is fixed in advance under the terms of the relevant Senior Finance Documents];

less (without double counting): [*See Section 8.2.3, Deductions*]

- (aa) all credit balances held on any bank accounts held by or on behalf of the Private Partner [and/or the Issuer] on the Termination Date;
- (bb) all amounts (including net hedge termination payments) payable by the Lenders to the Private Partner as a result of a prepayment of amounts outstanding under the Senior Finance Documents or termination of the PPP Contract; and
- (cc) all other amounts received or due to be received by the Lenders on or after the Termination Date and before the date on which compensation is payable by the Contracting Authority to the Private Partner as a result of enforcing any other rights that they may have.

This may include, inter alia, insurance proceeds pledged or assigned to the Lenders.

Consider also deductions in respect of unfulfilled handback condition obligations where appropriate.

"Senior Finance Documents"

means the finance documents entered into between the Lenders and the Private Partner for the purpose of financing the PPP Project, including [*insert defined terms for relevant [loan agreements] [bond financing documents to include bond trust deed, subscription agreement (terms and conditions of the bond) and security documents]*].

"Sub-contractor Breakage Costs"

means the value of Losses that have been or will be reasonably and properly incurred by the Private Partner as a direct result of the termination of the PPP Contract, but only to the extent that:

- (a) the Losses are incurred in connection with the PPP Project and in respect of the provision of services or the completion of works, including:
 - (i) any materials or goods ordered or Sub-contracts placed that cannot be cancelled without such Losses being incurred;
 - (ii) any expenditure incurred in anticipation of the provision of services or the completion of works in the future;
 - (iii) the cost of demobilization including the cost of any relocation of equipment used in connection with the PPP Project; and
 - (iv) redundancy payments;
- (b) the Losses are incurred under arrangements and/or agreements that are consistent with terms that have been entered into in the ordinary course of business and on reasonable commercial terms, excluding loss of profits calculated over a period which is longer than [*one (1) year*] after the Termination Date; and
- (c) the Private Partner and the relevant Sub-contractor have each used their reasonable endeavors to mitigate the Losses.

"Subordinated Finance Documents"

means any agreements under which the Shareholders make subordinated debt available to the Private Partner. [See Section 8.2.2.](#)

"Termination Date"

means the date on which the PPP Contract terminates in accordance with Clause [*insert relevant clause number*].

Compensation on Contracting Authority Default, Material Adverse Government Action, Change in Law or Voluntary Termination

- (1) If this PPP Contract is terminated for (i) Contracting Authority Default in accordance with Clause [*insert*], (ii) Material Adverse Government Action in accordance with Clause [*insert*], (iii) Change in Law in accordance with Clause [*insert*] or (iv) voluntary termination in accordance with Clause [*insert*], the Contracting Authority shall pay the Private Partner an amount equal to the sum of:
 - (a) Outstanding Senior Debt; plus
 - (b) redundancy payments for employees of the Private Partner that have been or will be reasonably incurred by the Private Partner as a direct result of termination of this PPP Contract; plus

Delete (ii), (iii) and/or (iv) if not contemplated in the PPP Contract.
See Sections 2, 3, 6 and 8.

Drafting to include any applicable deductions (see Section 8.2.3) if not included in definition of Outstanding Senior Debt.

- (c) any Sub-contractor Breakage Costs; plus
- (d) [select from Option 1(a), 1(b), or 1(c) below depending on the required valuation method for the payments due to the equity Party]
 - **Option 1(a):** an amount which, when taken together with any Distributions paid, interest paid and principal repaid under the Subordinated Finance Documents on or before the Termination Date, taking account of the actual timing of such payments, results in a real IRR on the share capital subscribed and amounts advanced to the Private Partner under the Subordinated Finance Documents equal to the Base Case Equity IRR; or
 - **Option 1(b):** the aggregate amount for which the share capital of the Private Partner and the receivables arising under Subordinated Finance Documents could have been sold on an open market basis, under the assumption that there is no default by the Contracting Authority, that no Material Adverse Government Action or Qualifying Change in Law has occurred, that the sale is on a going-concern basis and that no restrictions exist on the transfer of the share capital; or
 - **Option 1(c):** the NPV of forecast Distributions and interest to be paid and principal to be repaid under the Subordinated Finance Documents as at the Termination Date, based on the Original Base Case, each amount discounted back at the Base Case Equity IRR from the date on which it is shown to be payable in the Original Base Case to the Termination Date.]

Compensation on Private Partner Default Termination

- (2) If the Contracting Authority terminates this PPP Contract for Private Partner Default in accordance with Clause [insert], the Contracting Authority shall pay to the Private Partner a compensation amount equal to [●] % of Outstanding Senior Debt.

Compensation on Force Majeure [and Uninsurability] Termination

- (3) If this PPP Contract is terminated for Force Majeure in accordance with Clause [insert], the Contracting Authority shall pay the Private Partner an amount equal to the sum of:
 - (a) Outstanding Senior Debt, if any; plus
 - (b) Initial Equity and any outstanding principal under the Subordinated Finance Documents as at the Termination Date [less any Distributions or subordinated debt interest payments already made]; plus
 - (c) redundancy payments for employees of the Private Partner that have been or will be reasonably incurred by the Private Partner as a direct result of termination of this PPP Contract; plus
 - (d) any Sub-contractor Breakage Costs.

See Sections 6 and 8 and Section 8.4.2(a) as regards % haircut.

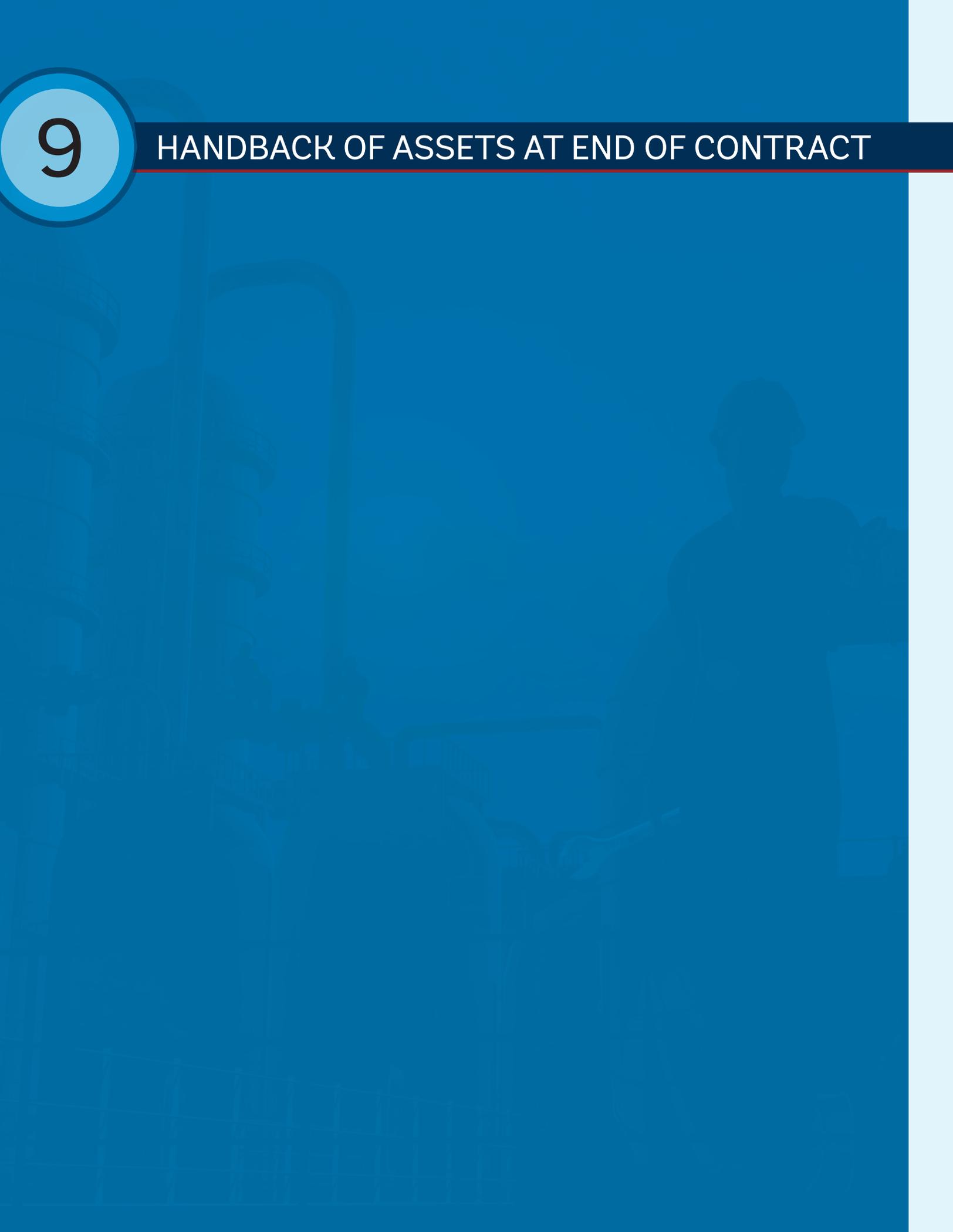
Drafting to include any applicable deductions (see Section 8.2.3) if not included in definition of Outstanding Senior Debt.

See Sections 1 and 8.

Drafting to include any applicable deductions (see Section 8.2.3) if not included in definition of Outstanding Senior Debt.

9

HANDBACK OF ASSETS AT END OF CONTRACT



9.1 KEY ASPECTS

9.1.1 *The concept of handback*

In a general commercial context, a contract involving the provision of important assets, operation of services or other complex cooperation typically contains provisions addressing what happens on expiry or early termination in terms of any on-going business and remaining assets. This might include provisions in relation to the sale, division or handover of ownership of physical assets, as well as ancillary aspects such as intellectual property and other rights necessary for a party continuing to run the business or use the assets.

9.1.2 *Why do PPP Contracts contain handback provisions?*

In a PPP context, handback is a key aspect because PPP Contracts typically involve the provision of a service through a major infrastructure asset (such as a hospital or road or transmission network), which in most cases is constructed as part of the PPP Contract (although some PPP Contracts involve an existing asset). The remaining life of the infrastructure asset often exceeds the contract term and the Contracting Authority wants the asset to be handed back to it in a good state (together with necessary ancillary matters and in some cases personnel) when the PPP Contract expires or terminates, so that the asset can continue to be operated and/or relevant service provided. In the majority of PPP Projects:

- (a) the Private Partner is paid for the construction of the relevant asset and the delivery of the relevant service over the life of the PPP Contract. The expectation of the Private Partner is that on expiry of the full term of the PPP Contract the Private Partner and its Lenders will have been repaid and the asset fully paid for.

Termination payments following early termination of those PPP Contracts are based on this principle. [See Section 8, Termination Payments.](#)

- (b) the Contracting Authority will expect to take back the asset/land at the end of the PPP Contract because it has paid for it and:
 - (i) the asset/land is necessary for the continued provision of the essential service (either by the Contracting Authority itself or through another Party which may involve a re-tender); or
 - (ii) it has other plans for the site/land; or
 - (iii) the asset/land has no value to the Private Partner and leaving it with the Private Partner is not a viable option (see [Section 9.3, Alternative use/Residual value risk](#) for further reasons).

Where the Contracting Authority wishes to continue to use the asset to deliver the service, it will want to ensure that the asset is returned to it in the condition and with the remaining useful life that the Contracting Authority assumed when the PPP Contract was entered into. The Contracting Authority's output specification for the PPP Contract should make clear what continuing condition is expected for all key assets. Economically, the pricing and payments made under the PPP Contract (or by users) will be based on the Private Partner's financial offer, which the Private Partner should size to provide for proper maintenance (both general operational and lifecycle capital replacement). This will be the case whether the PPP Contract ends by natural expiry or early termination.

The PPP Contract needs to ensure that:

- the condition of the project asset is as expected – at whatever stage termination occurs; *See Section 9.5, Sample Drafting 9, Clause ZZ(a)(iv) and Section 9.6, Sample Drafting 9A, Clause 2(1)(a).*
- the Contracting Authority has the necessary rights and, in many cases, operational personnel, to take over and use the asset (and/or the land) at the end of the PPP Contract; *See Section 9.5, Sample Drafting 9A, Clause AA(b)(i) and (c) and Section 9.6, Sample Drafting 9A, Clause 2(1) and (4). and*
- sufficient time is allowed under the PPP Contract to ensure that an orderly transition can take place. *See Section 9.5, Sample Drafting 9A, Clause AA(d) and Section 9.6, Sample Drafting 9A, Clause 2(1)(b)-(c).*

Although these matters concern the end of the PPP Contract, they need to be considered before contract signature, as the agreed treatment for handback will impact the design, maintenance, pricing and other matters during the life of the PPP Contract (e.g. as regards maintenance standards and costs). For example, if the PPP Contract has an operating period of 25 years, a need to replace a roof or lift system in year 26 (one year after handback) would produce a lower priced bid than one where the roof or lift system were to be replaced in year 24). The Contracting Authority needs to decide whether it wants the PPP Contract to require the roof to be replaced before the end of the contract term or not, weighing up the additional cost that the Private Partner would factor into its price for such replacement against not having to replace the roof itself after handback. It is also key for the Contracting Authority that such matters are specifically dealt with in the PPP Contract, as at the time of contract termination, the Private Partner is unlikely to accept additional obligations to facilitate handover unless it is contractually required to do so.

The circumstances around handback will vary from one PPP Contract to another and will depend on the Contracting Authority's intentions with regard to post-PPP usage, the nature of the asset (e.g. roads and most buildings are usable for much longer than the initial PPP Project duration), the stage at which the PPP Contract comes to an end (early or on natural expiry) and whether termination occurs during construction or operation. Ultimately, the PPP Contract provisions should be tailored to take account of the specific nature of the relevant PPP Project and any requirements under underlying laws in the relevant jurisdiction (as described in the 'civil and common law differences' box below).

Exceptions to the principles above are discussed briefly in [Section 9.3, Alternative use/Residual value risk](#) below and, as explained, will not be relevant for the vast majority of PPP Contracts.

CIVIL AND COMMON LAW DIFFERENCES

In civil law jurisdictions, assets built on publicly owned land and/or used for a public service will often be subject to particular restrictions. For example, mandatory handback at termination may be embedded in underpinning administrative law principles or legislation and there may be mandatory access or rights of use for third parties. In some countries (such as France), ownership will remain with the Contracting Authority throughout the duration of the PPP Contract, with assets built on such land automatically becoming Contracting Authority property as soon as they are built and handed back for free at natural expiry⁸⁹. The PPP Contract will set out the specific accompanying detail about asset condition and cooperation obligations, taking into account the underlying mandatory law provisions. Parties will want to set out the requirements and process regarding handback to ensure clarity and avoid unexpected consequences. For example, not specifying the contractual regime applicable to PPP assets may in some jurisdictions result in the Contracting Authority having a discretionary right to require demolition of all infrastructure (with costs being borne by the Private Partner).

9.1.3 Relationship to other provisions

There are a number of provisions in a PPP Contract which relate to handback but also to the operation of the PPP Contract during its life. These include contractual terms dealing with access to and inspection of the PPP Project and provision of certain information. These should dovetail with specific handback provisions to ensure that the Contracting Authority has all the rights it needs at the end of the PPP Contract.

Provisions relating to maintenance and surveys of the condition of the asset are closely related to handback. They are intended to ensure that the asset is maintained to the standard required under the PPP Contract and, as applicable, to ensure a remaining useful life of a particular length after the end of the PPP Contract. Contractual terms in respect of maintenance funds, guarantees and insurance proceeds are also relevant as these cash flows may need to be shared with the Contracting Authority in some handback circumstances. *See Section 9.2.2.*

As the handback provisions may be triggered on early termination as well as natural expiry of the PPP Contract, they should also dovetail with provisions in respect of termination mechanics and compensation to ensure, for example, that the Private Partner does not unfairly benefit from such termination payments where the handback condition is unsatisfactory. *See Section 6, Termination Events and Section 8, Termination Payments and Section 9.2.8.*

⁸⁹ Under French administrative law, assets are built on state-owned land and qualify as “returned assets” (“biens de retour”).

9.1.4 Related Project Agreements

The Private Partner must ensure that the handback provisions in the PPP Contract flow down into the Project Agreements so that the Private Partner can comply with its obligations under the PPP Contract regarding both the condition of the asset at handback and relevant rights to enable whoever is taking over the service provision to do so effectively. This will include ensuring that Sub-contractors are obliged to carry out relevant condition surveys and rectification and also provide relevant cooperation and assistance (including ensuring any unexpired equipment warranties or guarantees relating to the PPP Project can be transferred to the Contracting Authority (or its nominee)). It may also include ensuring the Contracting Authority can take over unexpired contracts necessary for delivering the service, such as supply or technical assistance contracts.

The Parties must ensure that all other contractual arrangements and documentation regarding the PPP Project land are structured so that the handback provisions under the PPP Contract work as intended, for example, in terms of timing and ownership transfer. This will depend on the real estate laws and procedures in the relevant jurisdiction and it is important that the Contracting Authority and its advisers consider this carefully.

CIVIL AND COMMON LAW DIFFERENCES

Typically, in a common law jurisdiction, the Private Partner leases the PPP Project land from the Contracting Authority (and may have been permitted to sub-lease it to the relevant Sub-contractors). The head-lease to the Private Partner is usually coterminous with the PPP Contract, so the land will revert to the Contracting Authority at the same time as the PPP Project asset. In civil law jurisdictions, the PPP Project land may have been made available through an administrative contract such as a “land concession” or other precarious right of use and because it is land within the public domain, assets may automatically have become the Contracting Authority’s property on construction completion and/or may transfer automatically at the end of the PPP Contract. As mentioned above, the Parties should ensure that the contractual handback provisions are compatible with the applicable real estate legal processes.

9.2 KEY CONSIDERATIONS FOR THE CONTRACTING AUTHORITY

9.2.1 Asset maintenance during the PPP Contract

Maintenance of the assets during the life of the PPP Contract is integrally linked to their condition at the end of the PPP Contract and to whether they will meet any handback conditions required by the Contracting Authority such as remaining asset life. In considering handback it is important to understand the nature of the Private Partner’s maintenance obligations under the PPP Contract. As these obligations are key to the Private Partner’s performance of the PPP Contract generally, these are addressed separately in [Section 9.4, Asset maintenance during the PPP Contract](#).

9.2.2 Condition of assets on natural expiry

Asset condition: The condition of the PPP Project assets is key to how the Contracting Authority will be able to use them after the PPP Contract ends.

The Contracting Authority should ensure that the PPP Contract:

- sets out the Private Partner's obligations as regards the condition it must hand the assets back in on natural expiry of the contract term and any required remaining useful life;
- provides for a termination survey to be carried out – either jointly by the Contracting Authority and the Private Partner, or by an independent assessor agreed upon by the Parties – to determine whether the obligations are likely to be met and what remediation works are needed; *See Section 9.5, Sample Drafting 9, Clause Y and Section 9.6, Sample Drafting 9A, Clause 2(2);*
- provides a mechanism for recovering from the Private Partner the cost of any remediation works needed to bring the asset up to the required condition; *See Section 9.5, Sample Drafting 9, Clause Y(e) and Section 9.6, Sample Drafting 9A, Clause 2(3) and*
- requires a follow-up survey to confirm that the remediation has been satisfactorily implemented. *See Section 9.5, Sample Drafting 9, Clause Y and Section 9.6, Sample Drafting 9A, Clause 2(3).*

Handback condition and useful life: As described in [Section 9.2.1](#) above, the baseline handback requirement is typically that the asset is handed back having met the maintenance obligations. If the Contracting Authority wishes to continue to provide the service seamlessly from expiry of the PPP Contract then it is essential that there is some useful life required to be left in the key project assets⁹⁰ (unless the Contracting Authority has agreed that the asset will have no residual life by the end of the PPP Contract and it has taken steps to procure a replacement). Some assets (or parts of assets) will have varying design lives and the Contracting Authority will want to take specialist advice in this regard when setting the project requirements and to be aware of the corresponding pricing implications.

For example, if the Contracting Authority requires the asset (or a particular part of it, such as the heating system) to have a further ten years of useful life after natural expiry and this means the Private Partner has to buy an expensive replacement piece of technical equipment (e.g. a heating boiler) which it would otherwise not have needed to replace, the Private Partner will cost the anticipated cost into the price its bids for the PPP Contract. The Contracting Authority should consider whether paying for that through the PPP Contract is value for money, especially when technology may have changed by the time the end of the PPP Contract arrives and a cheaper solution may be available. *See Section 9.6, Sample Drafting 9A, Clause 1(1) and 2(1)(a).*

⁹⁰ See APMG PPP Guide, Chapter 8: Operations and Hand-back, Section 11.2 Prepare for Continuity of Operations after Asset hand-over. [See links in Appendix A, Additional PPP Resources.](#)

Importance of survey: Although the risk of payment deductions is the Private Partner’s incentive to comply with its maintenance obligations, this incentive may weaken over time as the Private Partner seeks to maximize its return over the remaining life of the PPP Contract by “sweating assets” (i.e. making cost savings where possible – for example, by not replacing an asset or carrying out major maintenance if the existing asset is able to last until expiry). At this stage, the Contracting Authority will also no longer have the comfort that the Private Partner’s Lenders are overseeing its compliance with its maintenance obligations because they will most likely have been fully or almost fully repaid. A termination survey is therefore important for ensuring that the Contracting Authority receives the asset in the condition that it has paid for it to be in and also for identifying the scale of any necessary remedial works so that the Contracting Authority can ensure a retention fund or other cost security is put in place by the Private Partner to fund the works (see below). *See Section 9.5, Sample Drafting 9, Clause Y.* In some PPP Contracts in some jurisdictions (e.g. Belgium), PPP Contracts may include detailed transfer requirements including certification that the requirements are satisfied. *See Section 9.6, Sample Drafting 9A, Clause 2(4).*

Timing of survey: The termination survey should take place sufficiently in advance of the PPP Contract expiry date to allow for any remediation to be carried out and verified. The recommended time period will depend on the nature of the particular PPP Project and whether the PPP Contract is terminating early or on natural expiry. It will also be influenced by the way in which remediation cost security (described further below) is to be provided – e.g. because a certain period may be required to allow for sufficient fund build-up. In the case of natural expiry, the survey is likely to be at least one to two years prior to the contract end and in some cases may be far sooner (e.g. seven years for a French motorway and six years for rail projects). In some jurisdictions (such as some states in Australia, the Netherlands and Belgium), successive termination surveys before expiry are recommended to ensure that asset condition is closely monitored on a regular basis (e.g. from two years, one year, six months before, and then, finally, on expiry). *See Section 9.5, Sample Drafting 9, Clause Y(a) and Section 9.6, Sample Drafting 9A, Clause 2(2)(b).*

Costs of survey and remediation: The initial cost of the termination survey may be borne by either Party or shared, and may be borne directly or indirectly depending on whether an independent assessor is appointed or whether the Parties carry out the survey themselves. PPP Contracts in some jurisdictions provide that the cost falls on the Private Partner where the need for remedial works is revealed. In any event, the cost of any required remediation costs will be for the Private Partner’s account and it is typically also responsible for any subsequent surveys to review the remediation works. *See Section 9.5, Sample Drafting 9, Clauses Y(c) and (d)(iii) and Section 9.6, Sample Drafting 9A, Clause 2(2)(a) and (c).*

In order to ensure that there are sufficient funds to pay for any such works and to reduce the risk of the Private Partner losing the incentive to maintain the asset to the standard required as the end of the contract approaches, it is market practice for the PPP Contract to provide a mechanism to secure the funding of such costs as described below.

Maintenance retention fund: In both “government pays” and “user pays” models, a maintenance retention fund (i.e. a separate bank account) is typically set up in the last few years of the PPP Contract to cover the cost of any remedial maintenance works

required to bring the asset up to the contractually required condition. In a “government pays” model, the Contracting Authority will pay a specified amount of the availability payment (which would otherwise be paid to the Private Partner) into the account. In a “user pays” model, the Private Partner (or the Contracting Authority, depending who receives the fees directly) will similarly pay a certain amount into the account. The amount and timeframe will vary according to the particular PPP Project and assets concerned and should be determined according to the type of rectification that might be needed. In some jurisdictions a set amount may be paid into the fund, whereas in other jurisdictions (such as some states in Australia), the amount will be determined by reference to the remediation works identified by an independent assessor in the termination survey (or surveys) which take place at specified intervals prior to contract expiry. The amount may be paid into the account over successive payment periods or a single payment period, depending on the circumstances. *See Section 9.5, Sample Drafting 9, Clause Y(e) and Section 9.6, Sample Drafting 9A, Clause 2(3).*

The Private Partner is reimbursed from the fund if it carries out the remediation work satisfactorily, and similarly the Contracting Authority can draw on the fund if it carries out the work itself. If the level of the fund is insufficient to cover the cost of the required work then the Private Partner will receive no reimbursement for the unrecovered amount. If the Contracting Authority has paid the costs, it should ensure that it is entitled to set off the unrecovered amount against the remaining availability payments due to the Private Partner in a “government pays” payment model and/or to otherwise recover the cost from the Private Partner as a debt. *See Section 9.5, Sample Drafting 9, Clause Y(f)–(h).*

Release of maintenance retention fund: The Contracting Authority should retain any remaining balance in this fund for a certain period after the end of the PPP Contract until it, or as applicable, the independent assessor has confirmed that all remediation has been carried out satisfactorily. It is in the Private Partner’s interests to ensure that such remediation is actioned swiftly and before expiry so that any remaining amount in the fund can be released as soon as practicable following expiry. It is usual that, to the extent funds are released to the Private Partner, any interest that has accrued on the account is also released to the Private Partner (on the basis that the account has been funded by amounts otherwise due to the Private Partner). *See Section 9.5, Sample Drafting 9, Clause Y(i).*

Alternative cost security: An alternative to the maintenance retention fund is for the Private Partner to provide the Contracting Authority with a form of performance bond, bank guarantee or equivalent security equal to the target fund amount. This can be called on by the Contracting Authority if necessary to carry out required works and can be reduced over the period prior to contract expiry to the extent that the Contracting Authority, or as applicable, the independent assessor confirms, completion of any necessary works and the satisfactory condition of the asset. This is typically put in place by reference to the cost of works identified as necessary in the surveys leading up to expiry. *See Section 9.6, Sample Drafting 9A, Clause 2(3) and 4(g).*

Warranties: Depending on the defect in condition and the age of the relevant part of the asset, there may also be construction or maintenance warranties which are still in force which will cover the remediation cost. As highlighted above, the Contracting Authority will want to ensure that it has the benefit of any such warranties when the asset is handed over to it.

Other maintenance/lifecycle funds: As indicated in [Section 9.2.1](#), it may be that certain savings can be made when reviews show that lifecycle assets have a longer useful life than originally expected. Where savings are identified in scheduled inspections within a certain period before the end of the PPP Contract (for example, two years), the Contracting Authority should ensure that it receives a share of such savings on contract expiry (for example, by retaining unused maintenance retention fund amounts). Some jurisdictions, such as the UK, propose that – in addition to the maintenance retention fund – the Contracting Authority should also withhold a proportion of the availability payment to ensure it receives its expected share of any lifecycle savings. An alternative is that savings (at least the Private Partner’s share) are added to the maintenance retention fund. The appropriate approach will depend on the individual PPP Project circumstances. The [Sample Drafting](#) does not include drafting for this.

Any savings at early termination should be factored into the calculation of any termination payments, taking into account the reason and timing of termination and the asset condition. [See Section 8, Termination Payments and Section 9.5, Sample Drafting 9, Clause Y\(e\)](#).

9.2.3 Private Partner obligations to facilitate handback/continued operation

In addition to the aspects mentioned in [Section 9.1.4](#) and [Section 9.2.2](#) above, in summary the Contracting Authority will want to ensure that the Private Partner is contractually obliged to:

- (a) hand back the PPP Project works, assets and site to the Contracting Authority free of any encumbrances and surrender all rights, title and interest in them except for any express exceptions; [See Section 9.5, Sample Drafting 9, Clause AA\(b\)\(i\) and \(c\) and Section 9.6, Sample Drafting 9A, Clause 4](#).
- (b) take all steps in the period leading up to contract expiry to cooperate with the Contracting Authority in preparing for handover and efficient continuity of service – this may include meeting with the Contracting Authority and any nominee (e.g. who may have won a re-tendering process) and providing access to operations, information and personnel so that the Contracting Authority and/or its nominee can familiarize themselves with the PPP Project; [See Section 9.5, Sample Drafting 9, Clause AA\(b\)–\(e\) and Section 9.6, Sample Drafting 9A, Clause 2\(1\)](#).
- (c) facilitate and provide all aspects of the handover arrangements as specified in the PPP Contract – this will include implementing arrangements relating to personnel ([see Section 9.2.4](#)), ensuring the Contracting Authority (or its nominee) has all necessary contractual and other rights (including intellectual property rights and rights to insurance), providing access to insurance proceeds received but not yet applied in repair and reinstatement, and supplying construction and operating manuals and historical data, as-built drawings, warranties and systems information etc. as well as all other necessary physical materials and equipment⁹¹; and [See references in Section 9.2.3\(a\) and \(b\)](#).

⁹¹ For examples of detailed lists, see Partnerships Victoria PPP Policy, Guidance and Templates (Standard Form Project Deed). [See links in Appendix A, Additional PPP Resources](#).

- (d) generally take all reasonable action to cooperate with the Contracting Authority (or its nominee) to enable the service to be continued (where applicable) with the minimum disruption. *See references in Section 9.2.3(a) and (b).*

The Contracting Authority should bear in mind that this cooperation is likely to have a price implication so it should ensure that its expectations are reasonable and value for money. For example, in some states in Australia, the PPP Contract requires the Private Partner to provide a nominated representative to be responsible for handover arrangements for a specified period (e.g. six months) and to train the Contracting Authority's nominated personnel in operating the project. In France, on the other hand, it may be more usual for the obligation to focus more on requiring the Private Partner to provide detailed written information.

This may also include the Private Partner appointing the Contracting Authority as its attorney to carry out all such necessary actions, which, as described in *Section 6, Termination Events and Section 9.2.4, Private Partner obligations on step-in*, will be contained in the security that the Private Partner typically grants the Contracting Authority to secure its end of contract obligations.

9.2.4 Personnel transfers

As mentioned in *Section 9.1.2*, the Contracting Authority (or its nominee) may need to take on personnel employed by the Private Partner/its Sub-contractors in order to continue to operate the asset/deliver the service. As with other handback provisions, this needs careful consideration before contract signature to ensure the Contracting Authority has the appropriate contractual rights in place. For example, the Contracting Authority will want to know the terms of the relevant employment contracts and ensure that the PPP Contract prohibits the Private Partner from making any significant changes to them in the last year or two of the PPP Contract that might adversely affect and bind the Contracting Authority under applicable employment legislation in the PPP Project jurisdiction. Similarly, the Contracting Authority may wish to restrict the Private Partner from significantly altering the number of employees as the PPP Contract nears its expiry. *See Section 9.6, Sample Drafting 9A, Clause 2(1)(c).*

If large numbers of employees are concerned, the process of transferring can involve significant work and specific procedures and legislation to be followed. It is essential that the Private Partner is required to cooperate with the Contracting Authority in a timely manner so that the necessary steps can be taken prior to the end of the PPP Contract. The precise drafting of employment-related provisions will depend on the legal position in the specific jurisdiction and so the *Sample Drafting* does not address these provisions.

9.2.5 Framework for negotiation

As mentioned, handback provisions are matters which must be considered prior to contract signature. Given the long-term nature of the PPP Contract, however, it is possible that the Parties may wish to adjust some of the handback requirements as priorities change or the useful life of certain assets is proven to be different. In this instance, the handback provisions will provide an essential framework within which

such negotiations can take place as the end of the contract term approaches. For example, the Parties may agree that certain remediation works highlighted by the termination survey need not take place, but the Contracting Authority should ensure that it is compensated appropriately for such reduction in standards (for example, by reducing the availability payment accordingly). Depending on tender laws, this may need to be set out in a clear, unequivocal and detailed way in the PPP Contract, as is the case in jurisdictions where EU public procurement rules apply. In some jurisdictions it may not need to be provided for in such detail in advance in the PPP Contract and could, if applicable, be discussed during the termination survey process (e.g. at the stage outlined in [Section 9.5, Sample Drafting 9, Clause Y\(d\)](#)).

9.2.6 Dispute resolution

Any disputes relating to handover provisions are usually dealt with in accordance with the dispute resolution provisions agreed under the PPP Contract ([see Section 11, Governing Law and Dispute Resolution](#)). It may be appropriate to agree a bespoke process for certain handback issues, for example, regarding the remediation required pursuant to the termination surveys – in this instance, an independent assessor’s decision could be considered final or the matter could be referred to an independent expert ([see Section 11.2.5, Independent experts for technical disputes](#)). [See Section 9.6, Sample Drafting 9A, Clause 2\(2\)\(a\) and \(e\), \(3\)\(b\) and \(4\)\(e\)](#).

The Contracting Authority should note that if the assessor cannot be deemed truly independent it may not be reasonable to expect the Private Partner to agree his decision is final. This could be the case, for example, where due to the nature of the PPP Project and the skills required, only those who have (or have had) some connection with the Contracting Authority will have the necessary specialist expertise to act as an assessor (e.g. in projects relating to national security or defense).

9.2.7 Contracting Authority options

Some jurisdictions (such as the UK) have required Contracting Authorities to have the contractual option either to take back the asset or leave it with the Private Partner, regardless of whether the asset has an alternative use. It is questionable whether there is any benefit to the Contracting Authority in having this right when the only realistic outcome is that the asset will revert to it. Whether the Private Partner is willing to accept this provision will depend on the relevant jurisdiction and it may not be possible in some jurisdictions if the assets are built on land within the public domain ([see Section 9.1.2](#)).

EMERGING AND DEVELOPED MARKET DIFFERENCES

A Private Partner may be willing to accept the risk of being left with an asset with no alternative use if it assesses the risk of the Contracting Authority taking this option as being so low as to be inconceivable – this is more likely in a known and predictable market (i.e. where the Contracting Authority/government has demonstrated a commitment to the long-term provision of the relevant asset/service and/or user need is clearly long term). In markets where this is not the case (which may be more likely in less established markets), the Private Partner may be reluctant to take this risk, especially if the asset may have decommissioning costs associated with it.

Some more Developed Markets (again, such as the UK) suggest that including an option for the Contracting Authority to extend the existing PPP Contract is another way of incentivizing the Private Partner to perform its maintenance obligations in the latter stages of the PPP Contract (in addition to the incentive of avoiding availability and performance payment deductions as described in [Section 9.2.1](#)). Any Contracting Authority considering this approach would need to be sure that exercising the option would (a) comply with any applicable procurement rules and (b) be the best value-for-money option for it. Within the EU, such options to extend are as a rule only valid if the clause is “detailed, precise and unequivocal” and included in the original tender documentation. In addition, an “excessive” or openended duration of a PPP Contract is usually problematic from a competition and public law perspective. (These aspects are not addressed in the Sample Drafting.)

9.2.8 Handback on early termination

While the guidance above (and some jurisdictions’ PPP Contracts) particularly contemplates the natural expiry of the PPP Contract, the relevant contractual provisions should also address early termination situations, recognizing that there may be different timeframes and methods of addressing costs involved and, on a Private Partner default termination, Lenders’ step-in rights. [See Section 9.5, Sample Drafting 9, Clause AA\(e\) and Clause Y\(a\) and Section 6, Termination Events, Section 7, Lenders’ Step-in Rights and Section 8, Termination Payments.](#)

If the PPP Contract is terminated early, then the Contracting Authority will want to rely on a fallback regime, which usually requires the asset to meet the requirements applicable at the stage of the PPP at which the termination occurs. The handback procedures may be similar to those set out for natural expiry, but with accelerated timeframes. In the operating phase, the standards required will typically be verifiable by reference to the maintenance standards and performance levels required under the PPP Contract (as well as by the periodic lifecycle reports and reviews and the handover condition required on natural expiry), as outlined in [Section 9.2.1](#).

In a PPP Project where the main obligation is to maintain the asset rather than to deliver other services (e.g. to maintain a prison but not provide custodial or other services), the Contracting Authority should consider a more rigorous and regular maintenance inspection and remediation process to ensure that it is getting what it is paying for. This should also mean that on early termination the asset condition is broadly to the expected standard and the termination survey should not throw up any major items. [See Section 9.6, Sample Drafting 9A, Clause 2\(4\).](#)

If early termination occurs prior to availability (i.e. in the construction phase), the Contracting Authority may need to rely on an expert or other third party mechanism to determine the handback requirements (and compensation mechanism). The early termination and handback provisions will need to dovetail appropriately.

The key aspect of early termination is to ensure that the Contracting Authority has the asset and all necessary rights to continue the service and the Private Partner is protected against unilateral, discretionary handback requirements (including demands for compensation) by the Contracting Authority.

CIVIL AND COMMON LAW DIFFERENCES

In some jurisdictions such as the UK where Lenders may have security over the relevant asset, the Contracting Authority may find that Lenders are unwilling to release such security until they have received the full termination compensation payment due to them. As this may affect the transfer back of the asset to the Contracting Authority, the Contracting Authority and its advisers will need to carefully consider the options available to it on termination. It may not be possible to agree an approach upfront in the PPP Contract and this is discussed further in [Section 8.6, Method and timing of payment: Asset transfer](#). This may not be a relevant concern in civil law jurisdictions, such as France, where Lenders do not typically take security over the project assets as this only gives them limited rights; they usually take security over the Private Partner itself.

9.2.9 Planning for the end of the PPP Contract

In addition to ensuring the PPP Contract includes comprehensive end-of-term requirements, the natural expiry of a PPP Contract is inevitable and from a practical perspective is something the Parties should prepare for well in advance of the end date⁹². Broadly speaking, concrete preparation and planning of the handback should typically start at least three years prior to expiry. The duration and process leading to handback will depend on the nature of the specific PPP Project and the assets and service involved. At the appropriate time, the Contracting Authority should start to consider what it wants to happen when the PPP Contract expires and which contractual options (if any) it wishes to choose. For example, it should consider whether the service is still needed and, if so, whether it should be delivered by the Contracting Authority or through a re-tender and also what plans it needs to put in place to ensure that there is a clear program of action. In some PPP Contracts there will only be one scenario: return to the Contracting Authority with assets meeting certain (technical) minimum requirements to ensure the Contracting Authority can continue to operate the asset.

On an early termination of the PPP Contract, the Contracting Authority should also aim to prepare as far in advance and as comprehensively as is practical in the circumstances, recognizing that certain termination scenarios may facilitate this more than others (e.g. a planned voluntary termination should allow for a more managed timeframe and process than, say, a Private Partner default termination where rectification is not possible by the Private Partner or its Lenders and the Contracting Authority takes over the asset in a short timeframe). [See Section 9.2.8](#).

For broader considerations in relation to end of contract matters and lessons learned, see, for instance, the APMG PPP Guide, Chapter 8: Operations and Hand-back, Section 11 Exit Strategy and Handback Considerations.⁹³

⁹² See APMG PPP Guide, Chapter 8: Operations and Hand-back, Section 9.1.1 Expiry of the PPP Contract. [See link in Appendix A, Additional PPP Resources](#).

⁹³ [See link in Appendix A, Additional PPP Resources](#)

9.3 ALTERNATIVE USE/RESIDUAL VALUE RISK

As mentioned above, there may be exceptions to the principles outlined in [Section 9.1.2](#). If the asset or land will have an alternative use – and therefore has what is known as a “residual value” – at the end of the PPP Contract, this may enable a different approach to be taken to the handback provisions when negotiating the PPP Contract. This is because it may be possible to require the Private Partner to take the asset or the land at the end of the PPP Contract on the basis that it should be able to realize some value to meet its expected return, as opposed to being paid out in full over the life of the Contract. If the Private Partner takes such “residual value risk”, in theory it should be able to bid a lower price for the PPP Contract.

The reasons why this approach is not seen in most PPP Projects are as follows:

- most PPP assets (such as hospitals, prisons, military facilities or equipment) are unlikely to have an alternative use that the Private Partner can easily exploit. Only assets of a certain type and in suitable locations are likely to be capable of conversion to private use (e.g. office buildings in an urban location or residential accommodation not within a restricted access site);
- the same typically applies to project land – depending on the location and the activities that have been carried out on it during the PPP Project it may have no market value or may not be transferable to the Private Partner under (public) law principles or legislation. The location may have little value, there may be no prospect of obtaining authorisations for alternative use or it may be contaminated to such an extent due to the project that the remediation costs would not be compensated by any development value (which may be the case, for example, in a waste facility project);
- many PPP assets are of a type which legally have to be under the Contracting Authority’s (or other governmental) authority and control and cannot be owned/operated independently by the private sector – for example, military assets, or in some jurisdictions, power transmission or highways operation and maintenance. As mentioned above, publicly-owned project land may also not be legally capable of transfer out of public ownership; and
- it is likely to be extremely difficult to quantify any residual value at contract signature because PPP Contracts are long term and the Private Partner is therefore likely to ignore any potential value in setting its PPP Contract price, even if it appears to accept the risk.

Unless there is clear residual value and the Contracting Authority is demonstrably able to realize better value for money through transferring residual value risk, provisions in PPP Contracts which appear to transfer residual value risk could in some cases be seen more as a cosmetic measure to help account for PPP Projects off government balance sheets.

EMERGING AND DEVELOPED MARKET DIFFERENCES

The Private Partner is likely to be unwilling to accept an option where it bears any real residual value risk in a market where (a) the future demand and use of the project asset is uncertain (which will depend on other infrastructure investment and maintenance – e.g. roads and utilities being built and maintained) and (b) the land value is unquantifiable. Its financial model may depend on debt and equity return being paid out during the life of the project. Even if the PPP Contract provides for the Private Partner to bear residual value risk, its pricing may in practice reflect little or no adjustment.

If the Private Partner is prepared to take some real residual value risk, the Contracting Authority should note that while the Private Partner may price its bid lower, it may well (as with any risk) price in some contingency in case the residual value realized is lower than anticipated. If that risk does not materialize and there is no rebalancing mechanism as regards the residual value actually achieved, the Contracting Authority will have paid more for the PPP Contract than it should have. In order to address this, the Contracting Authority could seek to include a mechanism in the PPP Contract which allows it to share in the value realized up to a certain amount. The Private Partner may, however, suggest that the reverse position is also addressed (particularly if it does not include any contingency), with the Contracting Authority being required to share the risk of the residual value being lower than anticipated.

The UK PF2 Guidance suggests that where assets have an alternative use the Contracting Authority should still have the option to take back the project assets (or re-tender the PPP Project) by making a payment to the Private Partner. For the reasons given above, determining the amount of such payment is likely to be challenging.

Ultimately, the Contracting Authority may decide that the best approach is to take back the asset in accordance with the more typical approach outlined in this [Section 9, Handback of Assets at End of Contract](#). It is then in a position to take such steps as are appropriate at the end of the PPP Contract if it no longer wants the asset/land and they have an alternative use. In this way the Contracting Authority will retain the whole of any resulting benefit.

The Sample Drafting does not include drafting for this Section.

9.4 ASSET MAINTENANCE DURING THE PPP CONTRACT

Maintenance obligations: In order to ensure that the project asset is appropriately maintained through the life of the PPP Contract, the Contracting Authority should place certain maintenance obligations on the Private Partner. These will typically require the Private Partner in general terms to maintain the asset so that the required service is provided, the asset is maintained in good order, it achieves its intended design life and is handed back in the contractually required condition (*see Section 9.2.2*). While these are quite general obligations, the PPP Contract usually distinguishes between “light” maintenance and “heavy” maintenance, with corresponding planned maintenance

schedules and a program for replacing key assets (known as “lifecycle assets”) in accordance with their intended design life as specified in the output specification, which the Contracting Authority has reviewed and approved. Some PPP Contracts only include “heavy maintenance” while cleaning and other light maintenance services remain a user responsibility. *See Section 9.55, Sample Drafting 9, Clause ZZ and Section 9.6, Sample Drafting 9A, Clause 2(1)(a).*

Maintenance risk: The risk associated with the assets being appropriately maintained to meet the service requirements should remain at all times with the Private Partner. This will incentivize the Private Partner to take maintenance obligations and risks into account (and optimize asset life and performance) from the start of the process. Whether the Private Partner is complying with its maintenance obligations and carrying out necessary maintenance will be reflected in the levels of availability and performance it achieves. The risk of availability payment or performance deductions (or, in the case of a toll road, reduced user demand due to poor asset condition) is the Private Partner’s incentive to comply with its maintenance obligations through much of the PPP Contract. *See Section 9.6, Sample Drafting 9A, Clause 1(1)(e).*

Planned maintenance/asset replacement: The purpose of approved planned maintenance and lifecycle replacement schedules is that periods of unavailability due to such scheduled works do not result in payment deductions and that the relevant works are carried out at a time which minimizes the impact on the service (for example, in a schools project, in the vacation periods). The PPP Contract typically provides mechanics enabling planned works to be postponed or brought forward where appropriate and for any corresponding net cost savings to be shared by the Parties (on the basis that the contract price will have been sized to take into account planned maintenance costs, as described in *Section 9.2.1*). This will typically include a requirement in relation to lifecycle assets for the Private Partner to provide the Contracting Authority with periodic reports (e.g. annually) and for the Parties to carry out regular reviews (e.g. every five years). *See Section 9.5, Sample Drafting 9, Clause ZZ and Section 9.6, Sample Drafting 9A, Clause 1.*

In PPP Contracts where maintenance is the main service provided there may also be more detailed inspection and rectification regimes throughout the contract term. *See Section 9.2.8.*

Maintenance/lifecycle funds: The Private Partner’s Lenders will typically oblige it to establish ring-fenced maintenance-related funds to build up sufficient reserves to meet its maintenance and asset replacement obligations when they fall due. This will particularly be the case in relation to “heavy maintenance” such as replacing significant lifecycle assets (such as school heating boilers or hospital medical equipment) as set out in the lifecycle asset replacement plan; these are often known as “lifecycle funds”. The Contracting Authority should not usually need to impose separate contractual requirements and it is only as natural expiry approaches that the PPP Contract typically provides for certain measures. However, this is seen as a requirement in some PPP Contracts (e.g. some PPP Projects in France) and the Private Partner draws on the relevant account to fund heavy maintenance/lifecycle maintenance. Any remaining sums may be transferred to the Contracting Authority when the contract ends. *See Section 9.2.2, Maintenance retention fund/Other maintenance/lifecycle funds.*

9.5 SAMPLE DRAFTING 9

*Securing continuity/Treatment of Assets at Expiry Date**

*[*Note: Adapt clause to include option not to take back the asset if applicable]*

Required definitions:

“Natural Expiry Date” means the date which is the [25/30th] anniversary of the [acceptance date for commercial operations].

“Expiry Date” means the Natural Expiry Date, or if the PPP Contract is terminated earlier in accordance with its terms, such earlier termination date.

Clause AA

- (a) On or before a date falling no later than [12/24] months prior to the Expiry Date, the Contracting Authority shall notify the Private Partner in writing whether it wishes to re-tender the provision of the Service.
- (b) If the Contracting Authority wishes to re-tender the provision of the Service then:
 - (i) from the date of receipt of the notice in Clause AA(a) the Private Partner shall do all necessary acts (including entering into any contracts) to ensure that the successor contractor obtains all of its rights, title and interest in and to the Assets with effect on and from the Expiry Date; and
 - (ii) the Contracting Authority will bear all costs of any such re-tendering of the PPP Contract [except to the extent that such costs are deducted from any termination payment in accordance with Clause [●] or as otherwise determined in accordance with Clause [●]].
- (c) If the Contracting Authority does not wish to re-tender the Service then the Assets shall transfer to the Contracting Authority on the Expiry Date and from the date of receipt of the notice in Clause AA(a) the Private Partner shall do any necessary acts (including entering into any contracts) to ensure that the Contracting Authority obtains all of its rights, title and interest in the Assets with effect on and from the Expiry Date.
- (d) From the date of receipt of the notice in Clause AA(a) the Private Partner shall take all reasonable steps and cooperate fully with the Contracting Authority and any successor contractor so that any continuation in the Service is achieved with the minimum of disruption and so as to prevent or mitigate any inconvenience or risk to health or safety of the employees of the Contracting Authority and members of public.
- (e) If the Expiry Date is prior to the Natural Expiry Date, the Private Partner must meet the requirements under Clause AA(b)(i), and Clause AA(c) from the time that the Private Partner receives notice of the Expiry Date until the Expiry Date, unless the Contracting Authority, acting reasonably, determines such requirements cannot be met due to the limited notice period the Private Partner has received of the Expiry Date, in which case, the Private Partner must meet such requirements as soon as practicable after the Expiry Date.

Drafting to reflect how length of contract term is determined, including any extensions.

This date should be consistent with Clause [Y] (Surveys on Expiry and Termination) to enable a decision to be made in sufficient time to facilitate the build up of an adequate retention fund.

Some models set out a non exhaustive list of actions.

Drafting to reflect cost agreement and eg Contracting Authority should not bear re-tendering costs following termination for Private Partner default.

Some models set out a non exhaustive list of actions.

Some models set out a non exhaustive list of actions.

Surveys on Expiry [and Termination]

Clause Y

- (a) [Eighteen] months prior to the Expiry Date, the Contracting Authority shall be entitled to carry out a final survey of the Assets to assess whether they have been, and are being, maintained by the Private Partner in accordance with its obligations under Clause ZZ [and any express Handover Condition clause].
- (b) The Contracting Authority shall notify the Private Partner in writing a minimum of [7] days in advance of the date it wishes to carry out the final survey. The Contracting Authority shall consider in good faith any reasonable request by the Private Partner for the final survey to be carried out on a different date if such request is made at least [2] days prior to the notified date and the Private Partner (acting reasonably) is able to demonstrate that carrying out the final survey on the notified date would materially prejudice the Private Partner's ability to provide the Service.
- (c) When carrying out the final survey, the Contracting Authority shall use reasonable endeavors to minimize any disruption caused to the provision of the Service by the Private Partner. The Private Partner shall afford the Contracting Authority (free of charge) any reasonable assistance required by the Contracting Authority during the carrying out of the final survey. The cost of the final survey shall be borne by the [Contracting Authority/Private Partner/Parties jointly].
- (d) If the final survey shows that the Private Partner has not complied with or is not complying with its obligations under Clause ZZ [or any express Handover Condition clause], the Contracting Authority shall:
- (i) notify the Private Partner of the rectification and/or maintenance work which is required to bring the condition of the Assets to the standard they would have been in if the Private Partner had complied or was complying with its obligations under Clause ZZ [and any express Handover Condition clause];
 - (ii) specify a reasonable period within which the Private Partner must carry out such work; and
 - (iii) recover the cost of the survey from the Private Partner by means of [a withdrawal from the Retention Fund Account – defined in (e) below] [a retention from the next availability payment] [other means of reimbursement].
- (e) If the Private Partner has been notified under Clause [Y](d)(i) above that rectification and/or maintenance work is required, [12] months prior to the Expiry Date the Contracting Authority shall deduct the costs of that work as quantified by that survey from the next following installment (or, if the amount of such installment is insufficient, the next installments as necessary) of the Availability Payment and pay such amount into an interest-bearing account in its name (the "Retention Fund Account").
- (f) The Private Partner shall carry out such rectification and/or maintenance work to the Contracting Authority's reasonable satisfaction within the period specified and any costs it incurs in carrying out such rectification and/or maintenance work shall be at its own expense.

The drafting of this Clause may need to be amended if it is likely that an independent third party will carry out the final survey.

Drafting/timing to be adapted if more than one survey envisaged and to reflect early termination survey needs, as applicable (e.g. see Clause AA(e)).

Drafting will need adapting to reflect agreed position regarding cost – see also (d)(iii).

Parties could agree a revised handover condition and corresponding payment adjustment at this stage, if applicable. See Section 9.2.5.

Drafting will need adapting to reflect agreed position regarding survey cost – see also (c) – as well as cost security.

Drafting to reflect agreed approach as regards deductions or other cost security and treatment of any surplus due to lifecycle asset savings.

- (g) If and to the extent that the Private Partner carries out the necessary rectification and/or maintenance work to the Contracting Authority's reasonable satisfaction within the specified period, the Contracting Authority shall reimburse the Private Partner's costs of so doing by withdrawing amounts from the Retention Fund Account. If the amount in the Retention Fund Account is insufficient to cover the Private Partner's costs, the Private Partner shall bear the balance of its costs itself.
- (h) If and to the extent that the Private Partner fails to carry out the necessary rectification and/or maintenance work to the Contracting Authority's reasonable satisfaction within the specified period, the Contracting Authority shall be entitled to carry out itself, or procure, such rectification and/or maintenance work at the Private Partner's expense and shall make withdrawals from the Retention Fund Account to pay for such work or, where there are insufficient funds in the Retention Fund Account, make deductions from the Availability Payment to pay for such work.
- (i) If:
- (i) all the rectification and/or maintenance work identified by the Contracting Authority has been carried out to the Contracting Authority's reasonable satisfaction; and
 - (ii) all such work has been paid for by the Private Partner; and
 - (iii) no termination notice given in accordance with this PPP Contract is outstanding,
- then the Contracting Authority shall pay any credit balance (including any accrued interest) on the Retention Fund Account to the Private Partner as soon as practicable.

The Parties will need to agree whether reimbursement will be made by staged payments during the course of the works or by a lump sum payment on completion of the works. One of the relevant considerations may be the size and nature of the rectification/maintenance works.

If the balance is not sufficient the Contracting Authority can recover the balance from the Private Partner either as a debt or through set off – see Section 9.2.2, Maintenance retention fund.

For example, within a certain period after the Expiry Date.

Maintenance

Clause ZZ

- (a) The Private Partner shall ensure on a continuing basis that at all times its maintenance and operating procedures are sufficient to ensure that:
- (i) the Service is continuously available as required by this PPP Contract;
 - (ii) subject to any relaxation in standards agreed in accordance with Clause [●] [*e.g. accelerated or postponed maintenance*], the Assets are kept in good structural and decorative order (subject to fair wear and tear) in accordance with this PPP Contract;
 - (iii) it can maintain the design intention of the Assets to achieve their full working life; and
 - (iv) subject to any relaxation in standards agreed in accordance with Clause [●] [*i.e. relaxation of handback requirements – see Clause Y(d)(i)*], the Assets are handed back to the Contracting Authority on the Expiry Date in a condition complying with the requirements of this Clause.
- (b) The Private Partner shall undertake routine repair and maintenance of the Assets in accordance with a Schedule of Planned Maintenance which has been approved by the Contracting Authority.

In a maintenance focused PPP Contract, maintenance-related provisions may reflect more rigorous requirements and also an enhanced inspection/rectification regime.

The PPP Contract should also contain requirements in relation to an approved lifecycle asset replacement program.

9.6 SAMPLE DRAFTING 9A

This is an example of a more detailed approach to handback, with Clause 1 setting out inspections and detailed requirements in respect of ongoing reporting and monitoring through the whole life of the PPP Contract. This approach, which may be particularly relevant in a PPP Project where maintenance is the principal service provided, gives the Contracting Authority a close view of the condition of the asset through the contract term and may also provide reassurance that the condition will not be unexpectedly poor on early termination or expiry.

Clause 1 *Quality Control and Checks*

(1) Quality control

- (a) The Private Partner is responsible for the quality, quality control and timely execution of the Service/Maintenance [define], as well as for the quality of the Documents [define].
- (b) To ensure this, the Private Partner must set up and maintain a management system that applies to the Service/Maintenance (including the Service/Maintenance undertaken by Sub-contractors and other agents) and the procedures that the Private Partner will follow in organizing, managing and controlling the implementation of the PPP Contract and ensuring the required quality (“**Management System**”).
- (c) The Private Partner must draw up a management plan describing the Management System (including a monitoring plan describing how the Private Partner will monitor whether the relevant requirements of the [output specification/schedule of requirements] (“**Schedule of Requirements**”) are complied with (the “**Monitoring**”), and submit it to the Contracting Authority for acceptance in accordance with Clause [●] [*relevant procedures for project management*] (“**Management Plan**”).
- (d) In the performance of the Service/Maintenance, the Private Partner must always comply with the Management Plan, and ensure compliance by its Sub-contractors and other agents.
- (e) The Private Partner remains solely responsible for any errors, omissions, mistakes or defects in the Documents and/or in any planned or performed Service/Maintenance, and any review, inspection, assessment or acceptance by the Contracting Authority does not affect the Private Partner’s responsibility.

Drafting may specify further details including requirements per phase of the PPP Project, process details and how modifications may be adopted.

Drafting should ensure that any acceptance/approval by the Contracting Authority does not change the allocation of risk to the Private Partner.

(2) Registration and Handling of Notifications

The Private Partner will set up a system for the registration and handling of complaints, requests, information requests and malfunction reports (“**Reports**”) in which the Private Partner will register all such matters (“**Registration System**”).

Drafting may set out details required, including recording how the reported matters are addressed.

(3) Periodic measurements

- (a) Except as regards the Private Partner’s specific measurement obligations as set out in the Schedule of Requirements, the Private Partner must, from the Availability Date [Define], carry out periodic measurements at least every three months to assess the extent to which it is in compliance with its relevant obligations under the Schedule of Requirements. These periodic measurements must be performed according to the Monitoring Plan, and the results must be processed as soon as possible in the Registration System and immediately notified to the Contracting Authority.
- (b) The Private Partner must draw up measurement protocols for the performance of the periodic measurements referred to in Clause 1(3)(a) and include these measurement protocols in the Monitoring Plan.
- (c) The Private Partner and the Contracting Authority must provide the Party carrying out the periodic measurements (“Measurer”), on its reasonable request, access to all areas in the [Project asset] and provide all information that the Measurer considers necessary in order to perform the periodic measurements.

(4) Inspections

- (a) The Contracting Authority (or its nominee) may at any time carry out announced or unannounced inspections to assess whether the Private Partner is complying with its obligations under the PPP Contract.
- (b) The Private Partner must provide the inspector access to the locations where the Service/Maintenance is being prepared or performed and provide them with all information reasonably requested.
- (c) When carrying out an inspection, the Contracting Authority must endeavor to minimize any hindrance to the performance of the Service/Maintenance.
- (d) The Contracting Authority shall provide the Private Partner with the results of the inspection as soon as possible, and the Private Partner will process the results as a Report in the Registration System as soon as possible and at the latest within [●] working days.
- (e) The Contracting Authority is not required to notify the Private Partner of any shortcomings identified by the inspection results and an inspection does not imply approval or acceptance of the Service/Maintenance.
- (f) The cost of an inspection is at the Contracting Authority’s expense, except in the case of an inspection announced at least two working days in advance, where the cost will be at the Private Partner’s expense (subject to a maximum of [specify amount]) if any items are identified which were not yet recorded in the Registration System and incur an aggregate [payment deduction – *define*] of at least [*specify amount*].

Drafting may specify if the Parties are allowed to attend relevant inspections.

(5) Monitoring report

Within [●] working days after the start of a [Payment Period – *define*], the Private Partner must provide the Contracting Authority with a report of the Monitoring results during the previous Payment Period.

Drafting to specify any required content, including detail of any consequent payment deductions.

Clause 2 Transfer

“End Date” means the day [25/30] years after the [Availability date – define].

(1) Conditions for Transfer

- (a) The Private Partner must ensure that, at the End Date, the [Project asset] complies with the [specify requirements – e.g. Schedule of Requirements, applicable law and relevant permits] (together the “Transfer Requirements”).
- (b) The Private Partner must, from one year before the End Date, until one year thereafter, provide all reasonable assistance to the Contracting Authority and/or, at its request, to its nominees, in order for maintenance to be continued without interruption after the End Date and to allow the proper transfer of maintenance to the Contracting Authority and/or its nominees.
- (c) To this end, the Private Partner will (inter alia) ensure a thorough and comprehensive transfer of knowledge relating to the Maintenance [define], to the extent reasonably necessary to enable the Contracting Authority and/or its nominees to maintain the [Project asset] after the End Date. This knowledge transfer will include at least the following activities:
 - (i) training the employees of the Contracting Authority and/or its nominees in performing the maintenance;
 - (ii) providing the Contracting Authority and/or its nominees with such information about the Maintenance as is reasonably required to enable them to carry out maintenance after the End Date in a way which minimizes any inconvenience to the Contracting Authority’s operations;
 - (iii) providing information about the profiles and skills of staff, potential agents and other resources used by the Private Partner for the Maintenance, as may be required for the Contracting Authority and/or its nominees to carry out maintenance after the End Date; and
 - (iv) providing reasonable access to the relevant personnel of the Private Partner or its agents for at least one year after the End Date.

Drafting relates to natural expiry. Consider additional drafting to reflect early termination needs/timings (e.g. see Section 9.5, Sample Drafting 9, Clause AA(e)).

(2) Transfer Inspections

- (a) In view of the provisions in Clause 2(1), the Contracting Authority and the Private Partner must inspect the [Project asset] jointly, led by an independent and impartial expert appointed by agreement of both Parties (acting reasonably). The independent expert’s costs will be borne by the Private Partner. In the absence of agreement within 40 working days after a Party has requested an inspection in accordance with this Clause 2(2), the independent expert shall be appointed by [tie-in with dispute resolution provisions].
- (b) The first inspection must take place no earlier than 120 months and no later than 114 months before the End Date. A follow-up inspection must be carried out at least every 24 months. An inspection must take place no earlier than

36 months and no later than 24 months before the End Date (“Guarantee Inspection”). The last inspection must take place no earlier than six months and no later than four months before the End Date, unless otherwise agreed by the Parties.

- (c) The inspections take place at the request of the Private Partner. If the Contracting Authority wishes an additional inspection, possibly by another independent and impartial expert, it will pay for the associated costs. Any request for an inspection must be made in writing to the other Party no later than 20 working days before the inspection.
 - (d) Within 20 working days after each inspection, the independent expert must provide both Parties with a summary of the maintenance to be performed in addition to the Service/Maintenance included in the [specify relevant plans], so that the [Project asset] will meet the Transfer Requirements at the End Date (“Additional Maintenance”), supplemented with a schedule for the implementation of this Additional Maintenance and a statement of the costs involved.
 - (e) Each Party may verify whether the summary, schedule and statement of costs (payable by the Private Partner) regarding the Additional Maintenance are realistic, correct and complete. Either Party may, within 15 working days of their receipt request the independent expert to provide clarification or to carry out additional investigations into the Additional Maintenance and provide a supplementary summary with a schedule and statement of costs, in each case within 20 working days of the request. If either Party then wants to contest such clarification or supplementary summary, it must institute a dispute pursuant to Clause [Dispute resolution] within 15 working days after the expiry of such 20 working day period.
- (3) Transfer Guarantee
- (a) If the Guarantee Inspection indicates that Additional Maintenance is required, the Private Partner must, for the purpose of ensuring compliance with its obligations under this PPP Contract and within 25 working days of receipt of the Additional Maintenance summary, provide a guarantee for an amount equal to the cost of such Additional Maintenance as demonstrated by the statement of costs referred to in Clause 2(2)(d). The guarantee must be issued by a credit institution acceptable to the Contracting Authority and be in the form set out in Schedule [●] or such other similar form approved by the Contracting Authority (“Transfer Guarantee”).
 - (b) If, as a result of subsequent inspections, it appears from (i) the summary in accordance with Clause 2(2)(d), as clarified or adjusted pursuant to Clause 2(2)(e), or (ii) the outcome of a procedure as referred to in Clause [Dispute resolution]), that (A) Additional Maintenance is required, and (B) the cost of it exceeds the maximum amount of the outstanding Transfer Guarantee, then the Private Partner must provide an additional guarantee, within 20 working days, for an amount equal to that difference, issued by a credit institution acceptable to the Contracting Authority and in the form set out in Schedule [●] or such other similar form approved in advance by the Contracting Authority (“Additional Transfer Guarantee”).

(c) If a subsequent inspection or outcome of a [*Dispute Resolution*] procedure shows that the Additional Maintenance cost is lower than the total amount of the outstanding Transfer Guarantee (and, if applicable, Additional Transfer Guarantee(s)), then the Contracting Authority, at the Private Partner's request, will notify the issuer(s) of the relevant guarantee(s) that such outstanding amounts shall be reduced by an amount(s) which results in the total outstanding amount being reduced by an amount equal to the difference.

Form of guarantee should include provisions to effect this.

(d) The Transfer Guarantee and Additional Transfer Guarantee(s) shall be valid for two years. Three months prior to the expiry of any Transfer Guarantee (and, if applicable, any Additional Transfer Guarantee(s)), the Private Partner must extend (or provide a replacement of each guarantee) for one year, failing which the Contracting Authority will be entitled to call on the relevant guarantee.

Form of guarantee/drafting should allow for extension or replacement of the guarantee, as applicable.

(4) Transfer certificate

(a) No later than two months prior to the End Date, the Private Partner shall submit a report to the Contracting Authority indicating that the Transfer Requirements have been met, or will have been met by the End Date.

PPP Contracts must contain provisions about the form and contact details that must be used for notices and requests etc.

(b) The End Date inspection for the issue of the Transfer Certificate [*define*] shall be conducted in the presence of the Private Partner, or following a minimum of ten working days' notice to the Private Partner.

(c) If the Transfer Requirements have been met, the Contracting Authority will deliver the Transfer Certificate to the Private Partner on the End Date. If the Transfer Requirements have not been met, the Contracting Authority will deliver a refusal report to the Private Partner as soon as reasonably practicable on or before the End Date.

Drafting may contain details of what the refusal report must contain and any time period for rectification.

(d) If a refusal report is delivered, the Private Partner shall, without notice and in all cases within the reasonable period set by the Contracting Authority in the refusal report, ensure that the [Project asset] is brought up to conformity with what is required in order for the Transfer Certificate to be delivered.

(e) Following its actions in accordance with Clause 2(4)(d), the Private Partner will notify the Contracting Authority when it believes the Transfer Requirements have been met. Within 15 calendar days following receipt of this notification, the Transfer Certificate will be delivered by the Contracting Authority, or a second refusal report will be delivered to the Private Partner. Unless the Private Partner does not dispute the grounds of refusal, the Private Partner must lodge a dispute pursuant to Clause [Dispute resolution] within 15 calendar days of receipt, failing which the Private Partner will be deemed to have agreed to the grounds of refusal.

(f) The Contracting Authority will issue the Transfer Certificate on the End Date if:

(i) the Contracting Authority has determined that the Transfer Requirements have been met;

- (ii) the Private Partner has transferred all the [Guarantees – *define*] provided to the Private Partner by any agents in connection with the performance of the [Service/Maintenance] to the Contracting Authority;
 - (iii) subject to the provisions of Clause [*Permits*], the Private Partner has provided all Permits to the Contracting Authority, and the Private Partner has taken all reasonable steps to transfer the Permits (if necessary) to the Contracting Authority, or its nominee;
 - (iv) the Private Partner has complied with the requirements of Clause (2)(b) and 2(1)(c); and
 - (v) the Private Partner has provided the Contracting Authority with the documents, information and cooperation referred to in Clause [*Permits*].
- (g) Within 14 calendar days after the issue of the Transfer Certificate, the Contracting Authority shall, at the Private Partner's request, inform the issuer(s) of the Transfer Guarantee and/or the Additional Transfer Guarantee(s) of the expiry of the relevant guarantee(s) and return the originals to the issuer(s), subject to Clause 2(4)(j).
- (h) The Contracting Authority may refuse to provide the Transfer Certificate if at the End Date all the conditions mentioned in Clause 2(4)(f) have not been met.
- (i) When the Private Partner has fulfilled its obligations in Clause 2(4)(f), or only minor deviations are established which are limited in number and unlikely to cause interference with the use, operation, life-span, safety or security of the [Project asset], the Contracting Authority will deliver the Transfer Certificate subject to a deduction reflecting such deviations and/or an obligation on the Private Partner to remedy such deviations within a period to be determined by the Contracting Authority.
- (j) If the Transfer Certificate is delivered subject to a deduction and/or an obligation as set out in Clause 2(4)(i), the Transfer Guarantee (or where applicable, the Additional Transfer Guarantee(s)) will only be reduced to a total amount equalling twice the cost necessary to remedy such deviations, or the net [termination compensation] to be paid will be reduced by such amount. This amount (or as applicable, the Transfer Guarantee and/or Additional Transfer Guarantee(s)) shall be released within 20 working days if and to the extent it is determined that the deviations have been resolved.
- (k) On the End Date, regardless of whether or not the Transfer Certificate is issued, the PPP Contract will terminate, without prejudice to the Private Partner's obligation to ensure that the [Project asset] complies with what is required for the issue of the Transfer Certificate. As regards such obligation, the Contracting Authority will grant the Private Partner access to the [Project asset] in accordance with such arrangements as are agreed between them.

PPP Contracts typically also provide that certain obligations will continue beyond expiry/termination where necessary to give effect to the intention of the relevant provisions (such as confidentiality, dispute resolution, cooperation post termination etc.).

10

CONFIDENTIALITY, DISCLOSURE AND TRANSPARENCY



10.1 KEY ASPECTS

10.1.1 *The concepts of confidentiality and transparency*

Most commercial contracts contain provisions by which the parties agree to protect the confidentiality of the contract terms as well as each other's commercially sensitive information (such as pricing and intellectual property) received in connection with the contract. When one of the parties is a public sector entity the interest of the parties in keeping certain information confidential needs to be weighed against the necessity for transparency and disclosure. While both private and public sector parties may want to keep certain information confidential the promotion of transparency and disclosure has increasingly been acknowledged by international⁹⁴ and national law and become a key consideration for governments, non-governmental organizations and international organizations in their activities. The underlying objectives can be multiple, including reducing the level of corruption (as well as complaints of corruption, secrecy or unfairness in procurement processes), reassuring the general public in regard to probity, service standards and costs of public contracts, encouraging competition and facilitating a better informed market.

10.1.2 *Why do PPP Contracts contain confidentiality and transparency provisions?*

Transparency and disclosure is a high priority for PPP Projects as the Contracting Authority is a public sector entity or agency. It has become increasingly common for Contracting Authorities⁹⁵ to require a presumption in favor of transparency and disclosure in PPP Contracts to ensure that information on PPP Projects, PPP Contracts and related documents can be shared by them, to the fullest extent possible, with the public at large. This has led to obligations on the Private Partner to meet and facilitate such transparency and disclosure requirements. Multiple factors have influenced this development. The main drivers in the PPP context are to reduce the risk of corruption, increase private sector involvement in infrastructure investment, increase public confidence and awareness – particularly as regards the disclosure of fiscal risks and contingent liabilities for governments – and achieve value for money. As with any infrastructure project, PPP Projects may also involve social and environmental, public interest and human rights considerations. These are additional factors in favor of enhanced transparency and disclosure of relevant impact studies and other project-related documentation by both the Contracting Authority and the Private Partner.

The purpose of including express confidentiality and transparency provisions is so that both Parties have a clear understanding of what information may (or may not) be shared publicly or with other parties and how such information may be disclosed.

⁹⁴ The right to freedom of information is e.g. enshrined in Article 19 of the International Covenant on Civil and Political Rights as interpreted in paras 18–19 of the General Comment no. 34 of the Human Rights Committee, CCPR/C/GC/34 of 12 Sept. 2011.

⁹⁵ See A Framework for Disclosure in Public-Private Partnerships, World Bank 2016.

Given commercial sensitivities as well as public interest-related limitations, transparency and disclosure obligations in a PPP Contract are typically subject to a number of limited exceptions in order to protect commercially or otherwise sensitive information relating to the Parties, the PPP Contract and the PPP Project. In most cases it is the Private Partner who has the most information to protect as it will not want its competitors to gain access to information which could give them a commercial advantage. However, the Contracting Authority may also wish to keep certain information confidential, for example if the PPP Contract is in the defense sector. In some highly sensitive projects, the Contracting Authority may require the Private Partner and other parties and individuals directly involved in delivering the service to sign a written undertaking to be bound by national security legislation. In some jurisdictions (e.g. in the EU), there are also data protection obligations which apply to the Parties and which are likely to be addressed in a specific clause.

EMERGING AND DEVELOPED MARKET DIFFERENCES

While the maturity of a jurisdiction's PPP market may be a factor in the level of transparency and disclosure sought under PPP Contracts, the World Bank's Framework for Disclosure in Public-Private Partnerships 2016 ("WB Disclosure Framework 2016") also suggests that the practice relating to PPP disclosure may have developed more rapidly in Emerging Markets, perhaps due to the pressing need for new infrastructure. An additional relevant factor to such development may be if the PPP Contract has to satisfy the disclosure policy requirements of other relevant bodies (such as multilateral agencies) in order for those bodies to support the PPP Project.

10.2 KEY CONSIDERATIONS FOR THE CONTRACTING AUTHORITY

10.2.1 Duty of disclosure

For public policy reasons, many jurisdictions have policies, laws or regulations imposing disclosure obligations on Contracting Authorities and/or ensuring the public have access to public procurement information. Mandated proactive disclosure can either be incorporated into the country's freedom of information ("FOI") legislation⁹⁶, PPP policies, laws and regulations⁹⁷, procurement legislation, public financial management (PFM) legislation⁹⁸ and sector-specific legislation as well as legislation relating to budget transparency. Some jurisdictions have even developed standard clauses related to transparency and confidentiality in PPP Contracts.⁹⁹ A comprehensive overview of existing frameworks, good practice cases and jurisdictional studies is given by the WB Disclosure Framework 2016 and the companion jurisdictional and case study

⁹⁶ For example, Chile's Access to Public Information Law (2008), India/Karnataka's Right to Information Act (2005) and New South Wales' Government Information (Public Access) Act (2009).

⁹⁷ For example, Kenya's PPP Act (2013); Brazil, Minas Gerais PPP Law (2003), India Draft PPP Policy (2012), UK PF2 Guidance: for details and further information see Table 3 PPP Legislation and Transparency Elements in: WB Disclosure Framework 2016.

⁹⁸ For details see Table 3 PPP Legislation and Transparency Elements in: WB Disclosure Framework 2016.

⁹⁹ Examples with short summaries are provided in Table 11 of the WB Disclosure Framework 2016.

volumes¹⁰⁰. Clauses dealing with transparency, disclosure and confidentiality should always be drafted following an analysis of the legal and policy framework and it is usual to include specific reference to any such laws and regulations. It is for the Contracting Authority to decide whether contractual obligations should go beyond what is legally required, but its default position should always be to aim for full transparency.

As mentioned above, there may also be international financial institutions and multilateral agencies supporting the PPP Project which, as a condition of their support, require Contracting Authorities to comply with their own policies on transparency. The information required to be disclosed under such policies does not, however, usually include disclosure of commercially sensitive or proprietary information.

10.2.2 Scope of the transparency and disclosure undertaking

A disclosure and transparency provision typically deals with how all announcements relating to the PPP Contract and the PPP Project are to be managed. The Contracting Authority will want to control how all information relating to the PPP Project is publicly communicated and will require prior approval of any media announcements and communications. *See Section 10.3, Sample Drafting 10, Clauses (1) and (2).*

Some jurisdictions (for example, Belgium) may not address public communications in the way outlined in *Section 10.3, Sample Drafting 10* and may simply treat the information as confidential and require the Contracting Authority's prior consent to press releases and other public announcements by the Private Partner.

In jurisdictions with disclosure frameworks it has also become best practice to require the posting of important project and contract information in the public domain. The Contracting Authority may therefore also want to ensure that it has the right under the PPP Contract to make public the terms of the PPP Contract as well as related information (subject to applicable confidentiality restrictions) by its preferred means. This may include publishing on the internet. The level of information available for it to disclose regarding the progress of the PPP Project will be dependent upon the Private Partner's compliance with reporting provisions elsewhere in the PPP Contract which oblige the Private Partner to disclose certain information (such as performance data) to the Contracting Authority. *See Section 10.3, Sample Drafting 10, Clauses (3)-(5).*

While some Contracting Authorities may not specifically be required to publish the PPP Contract by legislation, in both common and civil law jurisdictions the public are increasingly using FOI legislation to gain insight into the terms of PPP Contracts. Specific provision can be made in the PPP Contract in this regard although some Contracting Authorities in some jurisdictions use less extensive clauses than *Section 10.3, Sample Drafting 10*, and, for example, may rely on the type of wording under *Section 10.3, Sample Drafting 10, Clause (9)(d)* to enable them to respond to requests under freedom of information legislation and other statutory disclosure obligations.

¹⁰⁰ Disclosure in Public-Private Partnerships: Jurisdictional Studies, World Bank 2016 and Disclosure in Public-Private Partnerships: Good Practice Cases, World Bank 2016.

10.2.3 Scope of the confidentiality undertaking

The need for transparency and disclosure should be balanced against the legitimate interests of the Private Partner and the Contracting Authority in keeping certain information related to a PPP Project confidential. However, as highlighted above, the Contracting Authority's aspiration should be full transparency except for limited types of confidential information.

In the context of a PPP Project, confidential information is typically information the disclosure of which would be likely to prejudice a Party's commercial interests. This will include information contained in the PPP Contract terms or supporting documents, such as trade secrets, commercially sensitive intellectual property rights and know-how and personal data. Key financial information, such as pricing elements and methodology and the Private Partner's financial model, including details of the costs of financing through debt and equity and other aspects, are also typically treated as confidential information. [See Section 10.3, Sample Drafting 10, Clause \(6\)](#). From the Contracting Authority's perspective, confidential information will include information which it is not in the public or national interest to disclose (e.g. defense, national security and custodial matters).

Confidential information in a document does not prevent the disclosure of that document entirely, but should be addressed by redacting the relevant information from the disclosed document.

Confidential information in the context of a PPP Project should be the exception rather than the rule and should be justified by reference to principles of confidentiality in applicable underlying transparency and disclosure policies and legislation. Concerns relating to particular information should be addressed specifically in the drafting. Any disclosure of such information should be clearly justified and made in accordance with the terms of the confidentiality provisions in the PPP Contract. Certain categories of information are typically excluded from confidentiality undertakings, such as information already in the public domain or received legitimately from another source. Confidentiality undertakings also do not usually apply where a Party is obliged to disclose information, for example, as part of a legal, regulatory or judicial process.

10.2.4 Approach

[Section 10.3, Sample Drafting 10](#), which is based on the UK PF2 Guidance, can be viewed as representing a good balance between protecting the Private Partner's commercially sensitive information and complying with the Contracting Authority's legal obligations (and policy aspirations) as regards greater public transparency. A similar approach is followed in the Infra Australia PPP Guidelines and the South Africa PPP Guidelines. In principle, there should be no distinction between the approach appropriate in mature and less mature markets.

EMERGING AND DEVELOPED MARKET DIFFERENCES

While the approach to drafting taken in this Guidance is representative of an established market, it would also be appropriate for Emerging Market PPP Contracts, particularly in jurisdictions where governments may wish to implement transparency measures during the life of the PPP Contract (or have already done so). The terms will also be familiar to international private sector Parties and such transparency can help build private sector confidence in Emerging Market governments seeking to establish and implement PPP programs or PPP Projects.

10.3 SAMPLE DRAFTING 10

Public Relations and Publicity

- (1) The Private Partner shall not by its directors, officers, employees or agents, and shall procure that its Sub-contractors shall not, communicate with representatives of the press, television, radio or other communications media on any matter concerning the PPP Contract without the prior written approval of the Contracting Authority.
- (2) The Private Partner may not represent the views of the Contracting Authority on any matter, or use the name of the Contracting Authority in any written material provided to third parties, without the prior written consent of the Contracting Authority.

Publication of the PPP Contract in the public domain

- (3) The Parties agree that the provisions of this PPP Contract [*and insert any other relevant documents defined as the Project Agreements*] shall, subject to Clause (7) below, not be treated as Confidential Information and may be disclosed without restriction and the Private Partner acknowledges that the Contracting Authority, subject to Clause (7) below, is entitled to:
 - (a) publish this PPP Contract [*and some of the Project Agreements*] on a website; and
 - (b) publish (on the internet or otherwise) a summary of the PPP Contract [*and the Project Agreements and any associated transaction document*] which shall include (i) the terms and conditions of the PPP Contract [*and the Project Agreements and any associated transaction document*] and (ii) any document or information arising out of or connected to the PPP Contract [*and the Project Agreements and any associated transaction document*], including performance of the PPP Contract [*and the Project Agreements and any associated transaction document*].
- (4) The Parties agree that Base Case Equity IRR information shall not be treated as Confidential Information and the Private Partner acknowledges that the Contracting Authority intends to publish such information on a website.
- (5) The Parties agree that information in respect of any direct or indirect change in ownership which has actually taken place shall not be treated as Confidential Information.

See Section 10.2.2 regarding the effectiveness of limb (ii).

Confidentiality

- (6) For purposes of this PPP Contract, “Confidential Information” means:
 - (a) information (however it is conveyed or on whatever media it is stored) the disclosure of which would, or would be likely to, prejudice the commercial interests of any person, trade secrets, commercially sensitive intellectual property rights and know-how of either Party, including all personal data and sensitive personal data; and

Confidential information should be redacted where appropriate from the relevant document/media so that the remaining information can be disclosed.

- (b) the sub-set of Confidential Information listed in Column 1 of Part I – Commercially Sensitive Contractual Provisions and Column 1 of Part II – Commercially Sensitive Material of Schedule [*insert reference to the Commercially Sensitive Information Schedule*] in each case for the period specified in Column 2 of Parts I and II of such Schedule (“Commercially Sensitive Information”).
- (7) Clause (3) above shall not apply to Confidential Information which shall, subject to Clause (9) below, be kept confidential for the periods specified in Schedule [*insert reference to the Commercially Sensitive Information Schedule*].
- (8) The Parties shall keep confidential all Confidential Information received by one Party from the other Party relating to this PPP Contract [*and any Project Agreements*] or the PPP Project and shall use all reasonable endeavors to prevent their employees and agents from making any disclosure to any person of any such Confidential Information.
- (9) Clauses (7) and (8) above shall not apply to:
 - (a) any disclosure of information that is reasonably required by any person engaged in the performance of their obligations under the PPP Contract for the performance of those obligations;
 - (b) any matter which a Party can demonstrate is already, or becomes, generally available and in the public domain otherwise than as a result of a breach of this Clause [*Confidentiality*];
 - (c) any disclosure to enable a determination to be made under Clause [*insert reference to Dispute Resolution clause*] or in connection with a dispute between the Private Partner and any of its sub-contractors;
 - (d) any disclosure which is required pursuant to [*insert reference to legislation containing public disclosure obligations*] as well as any other statutory, legal (including any order of a court of competent jurisdiction) or Parliamentary obligation placed upon the Party making the disclosure or the rules of any stock exchange or governmental or regulatory authority concerned;
 - (e) any disclosure of information which is already lawfully in the possession of the receiving Party, prior to its disclosure by the disclosing Party;
 - (f) any provision of information to:
 - (i) the Parties’ own professional advisers or insurance advisers; and/or
 - (ii) the Lenders or the Lenders’ professional advisers or insurance advisers or, where it is proposed that a person should or may provide funds (whether directly or indirectly and whether by loan, equity participation or otherwise) to the Private Partner to enable it to carry out its obligations under the PPP Contract, or may wish to acquire shares in the Private Partner in accordance with the provisions of this PPP Contract to that person or their respective professional advisers but only to the extent reasonably necessary to enable a decision to be taken on the proposal; and/or
 - (iii) international or bilateral financial institutions involved in the PPP Project as Lenders, political risk insurers or guarantors; and/or

Consideration should also be given to having a general provision for the disclosure of information that is ‘required in the public interest’. See also Clause (9)(j)(ii).

- (iv) any rating agency which may be engaged to provide a rating or rating assessment in relation to any Senior Debt;
 - (g) any disclosure by the Contracting Authority of information relating to the design, construction, operation and maintenance of the PPP Project and such other information as may be reasonably required for the purpose of conducting a due diligence exercise, to any proposed new private partner, its advisers and Lenders, should the Contracting Authority decide to re-tender the PPP Contract or undertake any market testing;
 - (h) any registration or recording of the required permits and property registration required;
 - (i) any disclosure of information by the Contracting Authority to any other relevant authority or their respective advisers or to any person engaged in providing services to the Contracting Authority for any purpose related to or ancillary to the PPP Contract; or
 - (j) any disclosure for the purpose of:
 - (i) the examination and certification of the Contracting Authority's or the Private Partner's accounts;
 - (ii) any examination pursuant to *[insert reference to any auditing obligations for public contracts]* of the economy, efficiency and effectiveness with which the Contracting Authority has used its resources;
 - (iii) complying with a proper request from either Party's insurance adviser, or insurer on placing or renewing any insurance policies; or
 - (iv) (without prejudice to the generality of Clause (d) above) compliance with *[insert reference to any laws requiring disclosure (e.g. environmental laws)]*.
- (10) When disclosure is permitted under Clause (9) above, other than Clauses (9)(b), (d), (e), (h) and (j), the Party providing the information shall ensure that the recipient of the information shall be subject to the same obligation of confidentiality as that contained in this PPP Contract. [The Private Partner shall expressly inform any person to whom it discloses any information under this Clause *[Confidentiality]* of the confidentiality restrictions set out in this Clause *[Confidentiality]* and shall procure its compliance with the terms of this Clause *[Confidentiality]* as if it were Party to this PPP Contract and the Private Partner shall be responsible for any breach by any such person of the provisions of this Clause *[Confidentiality]*.]
- (11) Where the Private Partner, in carrying out its obligations under the PPP Contract, is provided with information relating to *[end users]*, the Private Partner shall not disclose or make use of any such information otherwise than for the purpose for which it was provided, unless the Private Partner has obtained the prior written consent of that *[end user]* and has obtained the prior written consent of the Contracting Authority.

Many jurisdictions require audit reports to be prepared in respect of transactions to which a Contracting Authority is a Party. Where applicable, this provision should also address the issue of public disclosure of these audit reports. See also Clause (9)(d).

- (12) On or before the expiry date, the Private Partner shall ensure that all documents or computer records in its possession, custody or control, which contain information relating to *[end users]* including any documents in the possession, custody or control of a Sub-contractor, are delivered up to the Contracting Authority.
- (13) The provisions of this Clause *[Confidentiality]* are without prejudice to the application of *[insert any relevant law governing official secrets or national security information]*.

SCHEDULE [●]

Commercially Sensitive Information

Part I - Commercially Sensitive Contractual Provisions

COLUMN 1	COLUMN 2
Commercially Sensitive Contractual Provisions	For a period ending on date below

Part II - Commercially Sensitive Material

COLUMN 1	COLUMN 2
Commercially Sensitive Material	For a period ending on date below

11

GOVERNING LAW AND DISPUTE RESOLUTION

11.1 KEY ASPECTS

11.1.1 Overview

This [Section 11](#) discusses the importance of governing law and dispute resolution clauses in PPP Contracts¹⁰¹. As explained further below, the choice of governing law determines the substantive law that will be applied to determine the rights and obligations of the Parties under the PPP Contract. However, the choice of governing law does not determine the *means* by which any dispute about the Parties' rights and obligations under the PPP Contract will be resolved. The dispute resolution mechanism should be specified separately and expressly in a PPP Contract. This is usually by way of a submission to the jurisdiction of the court of a particular country or by the inclusion of an arbitration clause. For example, the Parties might select the Contracting Authority's law as the governing law of the PPP Contract, and international arbitration as the means of dispute resolution. This would mean that any dispute arising out of the PPP Contract would be resolved by an arbitral tribunal applying that domestic law.

This [Section 11](#) explains the concepts of governing law and jurisdiction and the key considerations for Contracting Authorities when considering these issues, including how Parties might select a dispute resolution provision and the core elements of such a provision. Particular guidance is given on important considerations for Contracting Authorities where arbitration is selected as the dispute resolution mechanism. Finally, some guidance is provided on immunity waiver clauses, alternative dispute resolution and the use of independent experts for the resolution of technical disputes.

11.1.2 The concept of a governing law provision

Even though domestic law may automatically apply in the absence of a specific governing law clause, all PPP Contracts should contain an express choice of governing law. The system of law specified in the governing law provision governs most aspects of the PPP Contract, including its interpretation and validity. The objective of a governing law clause is to achieve certainty (insofar as it is possible to do so) between contracting Parties as to the nature and scope of their respective rights and obligations. If the governing law of the PPP Contract is not expressly chosen, a court will decide it, with consequent possible unpredictability.

The governing law of a PPP Contract is typically the domestic law of the Contracting Authority's jurisdiction, as the Contracting Authority will be familiar with that law and its requirements. As indicated in [Section 7.2.3](#), the Direct Agreement is typically (although not always) governed by the same law as the PPP Contract, so its governing law is usually also the domestic law of the project jurisdiction. This avoids any issues arising as a result of domestic law applying to the Contracting Authority's relationship with its citizens and domestic companies but a foreign law applying to its relationship with the Private Partner and other PPP parties.

¹⁰¹ Sometimes referred to as "forum selection" or "choice of court" clauses.

In some jurisdictions, a Contracting Authority may be prohibited or restricted from contracting under an external (foreign) law.

As the Contracting Authority will typically want to contract the PPP Contract under its domestic law, an awareness of the factors that Equity Investors and Lenders (particularly if non-domestic) will take into account in carrying out due diligence in this regard can help inform the Parties' risk allocation in the PPP Contract. These factors are also helpful to governments in establishing an environment conducive to successful PPP procurement (*see Section K, PPP Contracts in Context*). They include:

- non-legal factors, such as market acceptability¹⁰², familiarity and convenience and relative cost;
- potential need for a detailed investigation into an unfamiliar system of law;
- commercial orientation, stability and predictability of the chosen legal system;
- insulation of the PPP Contract from legal changes. This is often one of the most important reasons for (typically foreign) investors generally to seek the choice of an external (foreign) system of law. Private sector parties in certain jurisdictions may be concerned, for example, that if the governing law is the local law of the Contracting Authority, it may subsequently pass legislation which adversely impacts the Private Partner's performance of the PPP Contract or imposes foreign exchange controls which adversely affect the Private Partner. Private Partners typically seek to address this through change in law or MAGA provisions, although such provisions would not necessarily assist in relation to mandatory public law issues; *See Section 3, Change in Law and Section 2, Material Adverse Government Action*.
- a desire to coincide the governing law with the dispute resolution forum if that forum is not the local courts (i.e. the courts which will hear any dispute arising in connection with the PPP Contract). Legal unpredictability may result if the court is called upon to apply a foreign law with which it is not familiar;
- an ability to use lawyers who have specialist experience in the PPP Contract concerned if such experience is not yet available domestically;
- language; and
- the desire for a single body of law to apply to the PPP Contract and each of the Project Agreements (which will facilitate consolidation in a single forum).

Governing law clauses are generally straightforward to draft. The selection should be clearly specified in the PPP Contract, usually next to, or as part of, the Dispute Resolution provision (see below). The governing law specified should be the system of law of a country, not to a collection of general concepts. Split governing law clauses and conditional governing law provisions should be avoided, as they add undesirable complexities. However, if the Contracting Authority does not opt for domestic law, it will still wish to ensure mandatory domestic law is factored in (for example mandatory legislation on government assets and public service restrictions and obligations).

¹⁰² This may include whether the respective choice of governing law would affect the Lenders' ability to obtain political risk insurance from multilateral or bilateral development agencies (or private insurers), which would be particularly important for PPP Projects reliant on this type of support to be bankable.

Many conflicts of law regimes provide for the application of overriding mandatory provisions of the place of performance, irrespective of the selection of governing law in a contract.

Many PPP Contracts now also include a choice of governing law in respect of “non-contractual obligations”. This term, found in European Union (“EU”) legislation, is understood to include torts such as negligence or pre-contractual misrepresentations. If the Contracting Authority or Private Partner were to bring a tortious claim that they were induced to enter into the PPP Contract by a misrepresentation made by the other Party, a choice of non-contractual governing law should indicate to the relevant court that this claim should be determined under the chosen governing law. It makes sense for all obligations relating to the PPP Contract to be governed by the same law. Accordingly, the choice of governing law for non-contractual obligations should ideally match the choice for contractual obligations. However, if the governing law is not domestic law, Contracting Authorities should consider the likelihood of claims by third parties (including citizens and local businesses) under domestic law. If domestic law does not apply to contractual obligations, the assessment will ultimately have to decide whether the optimal position is for the law governing non-contractual obligations to be (i) the same as the law for contractual obligations between the Parties or (ii) domestic law as that will, as a rule, govern non-contractual obligations between third parties on the one hand, and all other entities involved (Contracting Authority, other government bodies, Private Partner, etc.) on the other hand.

Section 11.3, Sample Drafting 11, Clause (1) includes a contractual and non-contractual governing law provision. This guidance and *Section 11.3, Sample Drafting 11* are intended to be of general application, and to be used by Parties from civil and common law jurisdictions, irrespective of whether the selected law is a civil or common law system of law.

11.1.3 The concept of a dispute resolution provision

As explained above, the governing law provision determines what system of law governs any dispute arising out of the PPP Contract, but a dispute resolution clause is then needed to specify which forum will then apply that law to resolve any such dispute and, in the case of arbitration, the procedure pursuant to which such dispute will be heard and resolved.

A dispute resolution clause sets out a pre-agreed mechanism for the resolution of any disputes that may arise out of the PPP Contract. All PPP Contracts should include a dispute resolution clause to provide as much certainty as possible about *where and how* disputes will be resolved. Such a clause aims to ensure that Parties stick to the agreed mechanism and helps reduce the risk of their wasting time and costs arguing about where a claim can be heard. A good dispute resolution clause will also reduce the risk of duplicative proceedings and irreconcilable decisions by different courts or tribunals. These clauses may be called “jurisdiction clauses”, “choice of court” or “forum selection” clauses.

EMERGING AND DEVELOPED MARKET DIFFERENCES

If there is no contractually agreed dispute resolution clause, there will be uncertainty about where disputes under the PPP Contract should be referred. The Parties' preferred courts may not accept jurisdiction over a dispute if there is no contractual clause specifying they are to determine disputes. Disputes may be commenced and heard by unreliable or inexperienced courts. This can be a particular risk in new and untested markets, where local courts may be unfamiliar with resolving complex commercial disputes in a timely way. There may also be a lack of confidence in the impartiality of the process.

The enforceability of the eventual decision will also be an important factor for Equity Investors and Lenders (see below). Given that disputes under PPP Contracts are likely to have some form of financial impact on the Private Partner and the choice of forum can impact enforceability of the respective decision, the inclusion of a workable dispute resolution clause is a key element in any assessment of the bankability of the PPP Project by the Private Partner and its Equity Investors and Lenders. *See Section E, PPP Contracts in Context.*

As with the governing law guidance, the guidance outlined below on selection and drafting of dispute resolution provisions and *Section 11.3, Sample Drafting 11* is intended to be of general application, and to be used by Parties from civil and common law jurisdictions, irrespective of whether the selected court is a civil or common law jurisdiction or the arbitration is seated in a civil or common law jurisdiction.

11.2 KEY CONSIDERATIONS FOR THE CONTRACTING AUTHORITY

This *Section 11.2* begins with a short overview of the key elements of any dispute resolution provision at *Section 11.2.1*. *Section 11.2.2* then explains factors a Contracting Authority should consider when selecting a dispute resolution provision, i.e. factors relevant to choosing between court litigation (whether before local courts or the courts of an “offshore” jurisdiction) or arbitration. It also includes some important guidance as to whether a Contracting Authority is able to refer disputes to a particular forum, for example for reasons of public policy. The guidance then discusses a number of the key elements of a typical dispute resolution provision in a PPP Contract. Key points covered include when a Contracting Authority may be confronted with potential Sponsors who want to move away from local courts, when the Contracting Authority may select international arbitration as the dispute resolution mechanism, specific drafting issues in relation to arbitration clauses, when Parties might include alternative dispute resolution mechanisms such as expert determination and mediation, and finally some guidance on waivers of any immunities and privileges that a Contracting Authority (and other sovereign/quasi-sovereign entities) may have.

11.2.1 *What are the key elements of a dispute resolution provision?*

In a PPP Contract, a dispute resolution provision typically specifies:

- (1) the governing law of the PPP Contract (if not specified in a different clause);
- (2) an obligation to attempt to reach a quick and amicable settlement;
- (3) a provision for the resolution of specific technical disputes by an independent expert;
- (4) a recourse to either (a) the courts that will have jurisdiction to determine the dispute or (b) international arbitration to finally determine all disputes not resolved informally or by expert determination. An arbitration clause should specify the “seat” of arbitration and usually also incorporates by reference institutional procedural rules. It may also set out certain bespoke procedural rules to govern the arbitration process and joinder and consolidation provisions in the event the dispute concerns multiple related contracts and/or multiple parties and where arbitration is selected;
- (5) an obligation to continue performance of the PPP Contract during the resolution of the dispute;
- (6) where appropriate, a waiver of sovereign and other immunities and consent to enforcement and execution; and
- (7) the allocation of costs.

11.2.2 *Selecting an appropriate dispute resolution provision*

11.2.2.1 Local courts – A Contracting Authority will generally want to select its local courts as the forum for the resolution of any disputes under the PPP Contract. This selection may be made for a variety of reasons including familiarity, compatibility with any concession/PPP legislation and because the PPP Contract is governed by local law. It also minimizes the risk that local users and other stakeholders will bring claims in a different court from the Private Partner. The costs of litigating before local courts may also be much lower than before certain “offshore” courts or the costs involved in an international arbitration. *See Section 11.3, Sample Drafting 11, Clause (13), Option 1.*

11.2.2.2 Offshore courts – In some situations, however, Private Partners may be reluctant to agree to have disputes determined by the local courts of a Contracting Authority. For example, they may be concerned that the courts in the Contracting Authority’s country are inexperienced in dealing with complex disputes under a PPP Contract (which may also lead to significant delays) or may be more favorable to the local parties/the Contracting Authority. In these circumstances, Private Partners may push for the inclusion of an external (i.e. “offshore”) jurisdiction provision in the PPP Contract and seek to select a court or courts with experience of resolving complex international disputes in a fair, timely and predictable manner.

Offshore courts may be the preferred choice for Private Partners even where the PPP Contract is governed by a different (i.e. local) law. Courts in certain jurisdictions regularly determine commercial disputes arising under contracts governed by different laws

(e.g. the English courts often determine disputes arising under foreign (non-English) law and do so by hearing expert evidence on that foreign law although this can increase costs). *See Section 11.3, Sample Drafting 11, Clause (13), Option 1.*

Offshore court litigation may be preferred as the dispute resolution mechanism for Private Partners if they perceive particular courts as being efficient and with a judiciary consisting of highly regarded commercial lawyers with experience of resolving disputes under PPP Contracts. Further reasons for preferring offshore courts may be the possibility of obtaining injunctive relief from those courts or the ability to obtain “summary” judgment (the early determination of a dispute without a full hearing). It is a procedure available in some courts but is less common in arbitrations.

From the Contracting Authority’s perspective, even if offshore courts might not be its preferred option, there may be circumstances where this option needs to be considered as a necessary compromise in order to ensure the PPP Project is bankable. *See Section E, PPP Contracts in Context.*

Transparency and public access to information about disputes may be an important factor in this selection. In some jurisdictions the legal process is public; pleadings can be accessed online, court hearings are open to the public and judgments are published online (see for example the British and Irish law reports free website, BAILII¹⁰³). This position contrasts with arbitration (see below) which is generally a confidential and private process.

11.2.2.3 Process agent clauses – In many common law jurisdictions, in order to initiate a claim the claimant must serve proceedings on the defendant and there may be detailed procedural requirements about service of process where a defendant is outside the jurisdiction. If a common law offshore jurisdiction is selected, to avoid complications with service overseas, a Party may ask the other Party to identify a “process agent” within the jurisdiction to accept service of process on their behalf. The cost of appointing a process agent is relatively low and avoids far greater costs and procedural delays in serving out of the jurisdiction¹⁰⁴. An example of a process agent clause is at *Section 11.3, Sample Drafting 11, Clause (23)*. A process agent clause may also be included as part of an arbitration clause (see below).

11.2.2.4 Arbitration – Arbitration is a contractually agreed method of dispute resolution that is an alternative to litigation before the courts. Broadly, the Parties agree that one or three individual arbitrators will determine their dispute rather than a court. *See Section 11.3, Sample Drafting 11, Clause (13), Option 2.*

Arbitration may also be selected if there is a desire to keep the dispute confidential. Unlike court proceedings, arbitration proceedings often take place in private (but not always and the approach varies depending on the jurisdiction and any institutional rules). Private Partners concerned about the enforceability of any decision made in respect of a dispute under the PPP Contract may seek to negotiate an arbitration clause rather than a court (litigation) clause because arbitration awards tend to be more widely enforceable than court judgments. Arbitration can, however, be expensive and sometimes as time-consuming as court proceedings. The Parties can include provisions

¹⁰³ <http://www.bailii.org/>

¹⁰⁴ For example, if practicable, a Contracting Authority may consider specifying its local Ambassador as the process agent.

in their arbitration clause for summary judgment or expedited procedures and certain institutional rules also include provisions in this regard. The Parties have to pay for the arbitrators' time and may also have to pay for an institution's administrative costs. [See Section 11.2.3.](#)

11.2.2.5 Local limitations on forum selection – Before selecting a foreign court or choosing an offshore arbitration as the dispute resolution mechanism in any PPP Contract, it is important to establish that, under all applicable laws, the Contracting Authority is able to agree to refer disputes to a foreign court or be subject to international arbitration (related to this it is also important to establish it can agree to be subject to a “foreign” law). For example, a Contracting Authority may be required under local laws relating to concession arrangements to refer all disputes relating to a PPP Project to the local courts (and/or to contract only under local law).

There may also be general prohibitions or limitations under local law in relation to a Contracting Authority's ability to agree to an offshore jurisdiction clause or foreign seated arbitration clause (or agree to a foreign law). For example, under local law sovereign entities may need specific waivers and approvals to agree contractually to arbitrate offshore, or to select a foreign jurisdiction clause and/or to contract under foreign laws. It will also be important to establish that under local law the Contracting Authority can contractually agree to waive immunity ([see Section 11.2.6](#)). Specific permissions may be required and certain formalities may need to be followed. Issues of capacity and authority may arise in this regard.

There may also be reputational and political issues with the Contracting Authority being seen to exempt public sector projects from the jurisdiction of domestic courts.

These are important points to establish at the outset of the tender process or negotiations.

11.2.2.6 General considerations – Given the long-term nature of the PPP Contract, it can be in the Parties' interests to have a dispute resolution process which supports their long-term relationship. Generally, a dispute resolution provision in a PPP Contract should also include a clause imposing a time-limited obligation to attempt to resolve a dispute informally (amicably) in the first instance. There are various alternative dispute resolution options which are discussed further below. [See Sections 11.2.4 and 11.2.5.](#)

In some circumstances a process agent clause may be appropriate even where the Parties have chosen arbitration as the dispute resolution mechanism. This is because ancillary court proceedings may be taken in the local courts of the seat and the agent would be served with any such proceedings. This is generally only required where a common law seat of arbitration is specified because those local courts have supervisory jurisdiction over the arbitration.

The relative merits of arbitration against litigation before a particular court or courts will need to be assessed carefully for each project. If the Parties intend to instead choose an offshore jurisdiction clause, the drafting of such a clause is generally more straightforward than the drafting of an arbitration clause, which tends to be more bespoke. In all cases, the selection of a forum must be clear and unambiguous.

11.2.3 Key steps if selecting arbitration

STEP 1: Choosing arbitration and selecting the rules of established independent arbitration institutions

If the Contracting Authority decides to select arbitration as the dispute resolution mechanism for the PPP Contract, it is recommended that institutional (administered) arbitration is chosen.

- (1) **Institutional Arbitration.** Instead of drafting an overly long arbitration clause containing bespoke procedural rules, it is easier and often more appropriate for the Parties to incorporate the procedural rules of an established independent arbitration institution. For consistency, all dispute resolution processes under the PPP Contract and the related Project Agreements should apply the same institution's rules. The PPP Contract drafting will therefore vary to some extent according to the institutional rules selected.

Reference to the rules of the arbitral institution usually incorporates the assistance of an institution, which may act as an appointing authority (if required) during the constitution of the tribunal, deal with the payment of arbitrators' fees during the proceedings and make arrangements for the respective hearings and issuance of the award.

The Parties can select from a variety of institutional rules and institutions. The rules of the International Chamber of Commerce ("ICC Rules") are frequently used¹⁰⁵. Other common options for international disputes include the London Court of International Arbitration rules ("LCIA Rules"), the Arbitration Institute of the Stockholm Chamber of Commerce rules ("SCC Rules"), the Hong Kong International Arbitration Centre rules ("HKIAC Rules"), the Singapore International Arbitration Centre rules ("SIAC Rules") and the Cairo Regional Centre for International Commercial Arbitration rules ("CRCICA Rules"). These institutions have model clauses available on their websites¹⁰⁶. *See Section 11.3, Sample Drafting 11, Clause (13), Option 2.*

When selecting institutional rules, care should be taken to review those rules to assess their suitability. The institution's track record in resolving international disputes should also be considered.

Although there are similarities between the institutional rules and the approach of institutions, there are some differences. For example, some rules specify a time limit within which a decision must be given; other rules are silent on this issue. By way of illustration, under the ICC Rules, the Tribunal has six months to render a final award (although this may be extended). The SIAC Rules provide that the Tribunal must submit the draft award to the Registrar within 45 days of proceedings closing (although this too may be extended).

Most institutional rules are regularly updated and introduce innovations and improvements. For example, many now provide for the appointment of an

¹⁰⁵ For illustration purposes only, *Section 11.3, Sample Drafting 11, Clause (12), Option 2* onwards is based on a choice of the ICC Rules. This drafting is for guidance only and will need review/adaptation when using an alternative institution's rules.

¹⁰⁶ See the following websites for some examples: <http://www.hkiac.org/arbitration/modelclauses>; <http://www.siac.org.sg/modelclauses>; and <https://sccinstitute.com/dispute-resolution/modelclauses/>

emergency arbitrator to deal with urgent applications (see for example Article 9B in the LCIA Rules) or the resolution of disputes under an expedited process (for example Article 9C in the LCIA Rules).

In addition, there is a dispute settlement mechanism specifically designed for disputes between foreign private investors and States (or their agencies or subdivisions) created by the Convention on the Settlement of Investment Disputes between States and Nationals of Other States (the “ICSID Convention”). ICSID arbitration is available when the home State of the Private Partner and the host State of the project differ in nationality, and both States are party to the ICSID Convention (currently 154 Contracting States). As with the incorporation of any other institutional arbitration clause, both the Contracting Authority (the host State or its agency or subdivision) and the Private Partner may resort to ICSID arbitration for breach of the obligations set forth in the PPP Contract.

While recourse to ICSID arbitration provides some comfort to the Parties as to the enforceability of awards, it might not always be an option for a PPP Contract. This is because the ICSID Convention establishes essential jurisdictional conditions for access to ICSID arbitration and the Parties would need to include a fall-back clause in the PPP Contract in case a dispute is determined not to meet these requirements¹⁰⁷.

- (2) **Ad hoc arbitration.** If the Contracting Authority opts for non-administered or ad hoc arbitration, the PPP Contract will need to include a detailed procedure for the conduct of the proceedings, including, for example, the process for the selection of the tribunal deciding the case, its powers and the issuance of awards (*see Step 3*). In the absence of locally tested standards, this requires extra care as crucial elements of the arbitral process may have been omitted which can result in procedural stalemate once the dispute arises.

As an intermediate alternative to pure ad hoc arbitration, the Contracting Authority may also choose a particular set of existing arbitration rules to govern each step of the arbitration process. This is the case, for example, if the PPP Contract incorporates a reference to arbitration under the rules of the United Nations Commission on International Trade Law (“UNCITRAL Rules”). The UNCITRAL Rules are often used in commercial disputes involving a public and a private entity, and are also commonly incorporated in international investment agreements (*see Section 11.3, Sample Drafting 11, Schedule 2*). It is important to note that, by contrast with institutional or administered arbitration, the selection of UNCITRAL Rules does not entail the automatic selection of an arbitral institution that will assist in the administration of the case. Many institutions, such as the Permanent Court of Arbitration, the LCIA, the International Chamber of Commerce, the International Centre for Settlement of Investment Disputes (“ICSID”), the American Arbitration Association (“AAA”) and the SCC are available to provide institutional support for proceedings under the UNCITRAL Rules. Should the Parties agree to such institutional support, it should be expressly specified in the arbitration clause in addition to the selection of the UNCITRAL Rules¹⁰⁸.

¹⁰⁷ The Parties to a PPP Contract may also resort to the “ICSID Additional Facility Rules” which are available for certain disputes that do not meet the essential jurisdictional conditions under the ICSID Convention.

¹⁰⁸ It is advisable for the PPP Contract to provide for institutional support to be expressly stated in the arbitration clause to avoid delays although the Parties can in theory agree on the administration of the dispute once a dispute has arisen.

EMERGING AND DEVELOPED MARKET DIFFERENCES

In Developed Markets, the Contracting Authority will generally opt for domestic courts. The selection of an established arbitral institution and of institutional procedural rules is of particular importance in many developing countries, where PPP Projects are unlikely to be bankable if recourse to acceptable arbitration arrangements or offshore courts with established PPP expertise is not agreed.

STEP 2: Choosing the seat of arbitration¹⁰⁹

If the Contracting Authority selects arbitration¹¹⁰ (as opposed to court litigation) as the dispute resolution mechanism, it is critical to specify a seat of arbitration. The importance of the seat (typically a major city) is that it places the arbitration within the legal framework of a particular jurisdiction (regardless of where any hearings in the arbitration are physically held). *See Section 11.3, Sample Drafting 11, Clause (16).*

There are three key reasons to carefully consider the choice of seat:

- (1) The national courts at the seat have “supervisory” jurisdiction over the arbitration. This can be significant because those courts can influence the arbitral process by, for example, staying concurrent court proceedings or granting injunctive relief to protect assets subject to the arbitration. It is also the courts of the seat that will generally be competent to hear applications to set aside an arbitral award.
- (2) Most national arbitration laws incorporated through selection of the seat include mandatory procedural provisions (e.g. regarding rights of appeal or the power of the courts to remove arbitrators) which will apply regardless of any contrary stipulation in the Parties’ arbitration agreement.
- (3) An arbitral award is often only as good as the ability to enforce it effectively. Companies operating internationally typically hold assets in many jurisdictions. Before concluding an agreement providing for arbitration, it should be verified that the chosen seat of arbitration, as well as those countries in which enforcement of any award is likely to be sought (which may or may not be the State of the Contracting Authority), are party to the Convention on the Recognition and Enforcement of Foreign Arbitral Awards 1958. Usually referred to as the “New York Convention”, there are now 159 Contracting States to this Convention. An arbitral award rendered by a tribunal “seated” in a New York Convention Contracting State should be enforceable in all other New York Convention Contracting States without a review of the merits, subject to limited grounds on which a court may refuse enforcement. However, local advice should always be sought as to the practices of the courts where enforcement is likely to be sought.

¹⁰⁹ Choosing the seat may be the Parties’ first step in forum selection but this may coincide with the selection of institutional rules (see Step 1).

¹¹⁰ This does not apply to ICSID arbitration which is delocalized.

CIVIL AND COMMON LAW DIFFERENCES

The courts in civil and common law jurisdictions often have different approaches to dispute resolution. However, where resolution of disputes is by arbitration then, generally speaking, it does not matter whether the arbitration has its seat in a civil law or a common law jurisdiction (nor does it matter whether the Parties are from civil or common law jurisdictions).

As highlighted above, the key selection factors are whether a jurisdiction is considered to be “arbitration friendly” (the national arbitration law and local courts are supportive of the arbitration process and will not interfere with arbitral proceedings unnecessarily) and whether it is a signatory to the New York Convention.

STEP 3: Determining the method of constituting the arbitral tribunal and selecting the arbitrators – number, qualifications and nationality

The arbitration clause should specify the number of arbitrators as well as the method by which such arbitrators will be appointed. In this context, it should be noted that most institutional arbitration rules will contain default provisions in the event the Parties fail to agree on the number of arbitrators and/or method of constituting the tribunal, or fail to appoint the agreed number of arbitrators.

Typically, for large value contracts such as a PPP Contract, the Parties would choose to have three arbitrators, even though this will make the resolution of any dispute more costly as the Parties must pay the fees of three arbitrators. This is because a three arbitrator tribunal is less likely to reach a maverick decision than a sole arbitrator and so reduces unpredictability. *See Section 11.3, Sample Drafting 11, Clause (14).*

Some arbitration clauses may specify particular expertise or other requirements as to qualifications arbitrators should have; for example, that an arbitrator should be a lawyer experienced in a particular type of transaction. It may be helpful to specify that all or the majority of arbitrators are legally qualified in the governing law. The Parties may also wish to pre-select the language of arbitration proceedings and take this into consideration in specifying arbitrator requirements. The Parties should, however, avoid being too prescriptive, as this may narrow the pool of potential arbitrators available.

Sometimes the Parties wish to specify that none of the arbitrators can be of the same nationality as any of the Parties to the arbitration – for example, if there are concerns as regards impartiality. Certain institutional rules include provisions relating to the nationality of arbitrators, and these should be checked.

STEP 4: Consolidation and joinder – related contracts/related parties

The PPP Contract will be part of a wider “network of agreements” between various parties. The Private Partner may, for example, enter into a PPP Contract with the Contracting Authority regarding the underlying facility, but all cash flows may be governed by a separate agreement between an off-taker and the Private Partner¹¹¹. When this is the case, the Private Partner may require that all the related Project Agreements contain a similar dispute resolution provision, together with consolidation and joinder language whereby all parties to the related contracts agree to submit disputes to the same arbitral tribunal, under the same rules. For greater efficiency, it is recommended that all agreements contain similar dispute resolution clauses under which there is pre-agreement to consolidation of related disputes and the joinder of related parties to any arbitration¹¹². However, the same principle does not always apply with regard to many agreements concluded with Lenders (or other finance parties) or Sub-contractors, as disputes arising under those contracts can be the sole responsibility of the Private Partner and it may be appropriate to keep the dispute processes separate. This will avoid the Contracting Authority getting dragged into expensive and time-consuming peripheral disputes. On the other hand, there may be areas of overlap, e.g. where the counterparty to a Project Agreement is claiming on the basis of a provision that has been passed down from the PPP Contract, participation in a consolidated dispute resolution process may be desirable and so limited joinder arrangements may be appropriate. Any assessment of the need for joinder provisions is likely to be fact-dependent. *See Section 11.3, Sample Drafting 11, Clause (21).*

Generally, consolidation and joinder is less of a concern with jurisdiction clauses where courts often will order consolidation of proceedings before it (and the Parties often can otherwise apply to the relevant courts for removal/transfer from one jurisdiction to another) or the joinder of parties under local procedural rules or inherent jurisdiction.

11.2.4 Informal (alternative) dispute resolution – negotiation, mediation and alternatives

Given the long-term nature of many PPP Contracts and the desirability of maintaining an on-going relationship between the Parties, the inclusion of an informal (alternative) dispute resolution mechanism in the dispute resolution clause is often helpful. There are many forms of alternative dispute resolution (“ADR”), ranging from informal meetings of senior executives (*see Section 11.3, Sample Drafting 11, Clause (4)*) to mediation, the use of a panel of senior representatives and the appointment of an external Disputes Board (*see Section 11.3, Sample Drafting 11, Schedule 1, Options 1, 2 and 3*). Some of these are discussed further below.

The inclusion of an ADR clause can encourage the informal resolution of disputes, at a relatively early stage, before significant amounts of time and costs have been spent in any formal arbitration or court proceedings and, importantly, before relationships have deteriorated.

The dispute resolution clause should specify if the recourse to ADR is mandatory and a condition precedent to commencing arbitration (or court proceedings) and whether the result of the ADR is binding or non-binding. If ADR is mandatory, the Contracting

¹¹¹ Other examples include government support agreements and direct agreements.

¹¹² The ICC Rules provide some assistance in this regard in any event: see Articles 7-10.

Authority should, as a rule, confirm or provide that the Parties are free to seek urgent (including injunctive) relief from the arbitral tribunal or court if needed prior to or during the ADR process. Parties must always ensure, however, that there is a fall-back disputes clause (whether arbitration or litigation) if ADR fails to resolve the dispute.

11.2.4.1 Mediation – It may be desirable to add a requirement for the Parties to attempt to settle their disputes through mediation. Mediation is a settlement process involving an external “mediator” who acts as a neutral facilitator to help Parties try to arrive at a negotiated settlement of their dispute. The use of external mediators is increasingly seen in the United States, in the UK and parts of continental Europe, in Turkey, in parts of the Middle East and in some parts of South East Asia. Mediation can be a useful means of getting Parties together and helping to forge an acceptable settlement, before legal costs escalate – this could prove particularly worthwhile in large transactions such as PPP Projects. On the downside, unproductive mediation may simply cause delay in the final resolution of the dispute and increase costs (if the prospect of a negotiated settlement is very low). There have also been concerns about the impartiality of mediators and confidentiality breaches in the process. Parties are usually free to agree to resolve a dispute by mediation even if there is no contractual clause requiring them to do so. *See Section 11.3, Sample Drafting 11, Schedule 1, Option 1.*

11.2.4.2 Disputes Board – A Disputes Board is a more formal mechanism usually involving the appointment of a panel of external individuals at the commencement of a contract to whom disputes can be referred throughout the life of the contract. This process is common in construction contracts and usually requires the Parties to pay for the retention of external experts. One consideration for the Parties is whether to appoint the Disputes Board at the outset of a PPP Project or whether to appoint it on an ad hoc basis only when a dispute arises. The former model is more expensive (at least at the outset of the PPP Project) but it helps ensure the Disputes Board is familiar with the PPP Project and so disputes can be resolved more expeditiously when they arise. The latter approach, though potentially less expensive, may not be as effective at finally settling disputes – which can result in the Parties having to arbitrate their disputes anyway and incurring greater costs when a dispute does have to be arbitrated. A key consideration is whether its decision will be final and binding;¹¹³ the dispute may have to be re-tried before an arbitral tribunal (or the courts) if the Parties do not give effect to the Disputes Board’s decision. Disputes Boards lack the consensual approach of mediation (or a panel of the Parties’ senior representatives) and there continues to be a debate about the efficacy and costs of this mechanism. If the decision of the Disputes Board is binding, there is little difference as compared with the arbitration process (therefore the process may be redundant given the inclusion of the arbitration clause). If the recommendation is not binding there may be little difference with the obligation to try to reach amicable settlement – the involvement of and decision by experts may, however, be helpful in steering the Parties towards a resolution. *See Section 11.3, Sample Drafting 11, Schedule 1, Option 3.*

¹¹³ For example, the ICC Dispute Board Rules give parties a choice between three different types of Dispute Boards: (a) Dispute Review Boards (which issue non-binding recommendations); (b) Dispute Adjudication Boards (which issue contractually binding decisions); and (c) Combined Dispute Boards (which issue non-binding recommendations but may issue binding decisions if the parties so request). *Section 11.3, Sample Drafting 11, Schedule 1, Option 3 illustrates type (a).*

11.2.5 *Independent experts for technical disputes*

As noted in [Section 11.2.1\(3\)](#), PPP Contracts typically include a clause providing that “technical disputes” be referred to an independent expert or panel of experts for determination. For example, valuation issues or accountancy issues are regularly referred to expert determination because Parties may believe it is advantageous for the individual determining the dispute to have detailed knowledge of a particular market/area.

The Contracting Authority will also need to think carefully about the definition of “technical disputes” so as to avoid, as far as possible, a dispute about scope. One option is to list particular clauses of the PPP Contract and specify that disputes under such clauses will be considered “technical disputes” unless otherwise agreed. To encourage efficiency, it is recommended that the clause specifies that the determination of the expert should be final and contractually binding, except in the case of manifest error or fraud. This approach should, however, be confirmed by local counsel, as certain jurisdictions may not give effect to an expert determination clause, even if this is specifically agreed in the PPP Contract¹¹⁴.

An expert determination is generally not “enforceable” in the same way as a court judgment or arbitral award. This means if the expert determination is not complied with voluntarily the Parties will need to resort to arbitration (or court litigation) in any event to resolve the dispute and obtain an enforceable award or judgment. For example, a Party may have to bring a claim for breach of the PPP Contract in respect of a failure to comply with the expert’s determination. Accordingly, even if an expert determination clause is included in the PPP Contract, it must also include an arbitration clause (or a jurisdiction clause) as a fall back to cover a situation where there has been a failure to comply with a determination. It is also important that matters outside the scope of the expert determination clause, as well as situations where something has gone wrong with the expert process itself, can be referred to arbitration (or the courts). [See Section 11.3, Sample Drafting 11, Clauses \(6\)-\(12\)](#).

11.2.6 *Waiver of immunities*

As highlighted in [Section 11.2.1](#), one of the negotiation points for a Contracting Authority to consider is whether and to what extent the dispute resolution clause in a PPP Contract should include, where required, a waiver of any privileges and sovereign immunities which the Contracting Authority enjoys before local and foreign courts (such as immunity from any suits by the Private Partner)¹¹⁵. The Contracting Authority should seek advice on the nature and extent of an acceptable and enforceable immunity regime early in the process. Generally speaking, a PPP Contract is expected to be fully enforceable and Private Partners and Lenders are therefore likely to have a

¹¹⁴ For example, it is understood that, whilst in theory there is scope for courts in the PRC to enforce an expert determination clause on the basis of general principles set out in PRC contract law, in practice there is a risk that the court may consider such a clause as contrary to public policy. In Thailand there is a risk that expert determination clauses may also be ineffective.

¹¹⁵ This does not apply to ICSID arbitration as a State or Contracting Authority that consents in writing to arbitration pursuant to the ICSID Convention is already waiving its immunity from being sued by the Private Partner and must therefore recognize an ICSID Convention award and enforce the pecuniary obligations under it as if it were a final judgment of a local court. However, the same does not apply to “immunity from execution”. The concrete measures taken to execute the pecuniary obligations of an ICSID award will be governed by the law of the State in which execution is sought, which includes that State’s rules on sovereign immunity.

policy of seeking an appropriate waiver of sovereign immunity clause with sovereigns or quasi-sovereigns. The Contracting Authority will need to assess whether it is bankable to resist a waiver entirely or whether negotiating limitations is an acceptable compromise.

Immunity is a complex legal area but, in short, a waiver may cover both a waiver from any court proceedings connected to the resolution of the dispute (if an arbitration clause is used this relates to any court orders needed to assist the arbitration) and the recognition of an award/judgment. If required, it would also include an agreement by the sovereign entity to execution/enforcement against certain of its assets and an agreement to certain forms of relief e.g. asset freezes. The precise ambit of any waiver in a PPP Contract is likely to depend on relevant laws of the court considering the issue and the Parties' bargaining power in the relevant real-life contractual negotiations. An illustration of the scope of a wide-ranging waiver is set out in [Section 11.3, Sample Drafting 11, Clause \(24\)](#).

Even if a Contracting Authority were to agree to submit to the jurisdiction of an offshore court to determine the dispute (i.e. waive its immunity from suit), it may not, however, be prepared to agree to a foreign court granting pre-and post-judgment attachments of its assets. A Contracting Authority may also wish to resist any waiver of immunity from enforcement and execution against its assets. It should be noted that under some laws an agreement to arbitrate is deemed to be a waiver of immunity from suit. A foreign sovereign is not immune from suit where a dispute relates to both commercial activities and is not a foreign sovereign act. It is important to remember many jurisdictions treat immunity from suit separately from immunity against enforcement and will not construe a waiver in respect of immunity from suit as constituting a waiver from or consent to enforcement. Ultimately, a Contracting Authority may find it has more scope to resist or negotiate limits to any waiver in respect of recognition or enforcement of judgments or awards, than it has to resist a waiver of immunity from suit (which is more likely to be a prerequisite for investment).

It is also important to understand whether or not it is legally possible for the Contracting Authority to waive its privileges and immunities as a matter of local law (whether under constitutional arrangements, public policy or otherwise).

11.3 SAMPLE DRAFTING 11

Governing Law

- (1) This PPP Contract and any non-contractual obligations arising out of or in connection with it are governed by and shall be construed in accordance with the laws of [country].

Dispute Resolution

- (2) If any dispute arises out of or in connection with this PPP Contract including any dispute concerning any non-contractual obligations arising out of or in connection with it (a “Dispute”) it shall be resolved in accordance with this Clause [●].
- (3) Either Party may by notice in writing to the other Party, at the address for sending of notices under this PPP Contract and in a manner provided by Clause [●], give notice that a Dispute has arisen (“Notice”). The Notice shall set out brief details of the nature of the Dispute.

Negotiation

- (4) The Parties shall attempt to settle any Dispute referred to in a Notice by good faith negotiation. Each Party shall be represented in any negotiation by that Party’s [CEO/a person with authority to settle the Dispute]. Such negotiation shall take place within fifteen (15) days of the delivery of the Notice. Any negotiations shall be confidential and shall be conducted without prejudice to the rights of the Parties in any future proceedings.
- (5) Nothing in [Clause (4)] will prejudice the right of a Party to seek urgent injunctive or declaratory relief or other urgent relief in respect of a Dispute.

Expert Determination

- (6) Any Dispute arising out of or in connection with Clauses [*insert reference to every clause where a Dispute is considered a Technical Dispute*] (a “Technical Dispute”) which is not resolved amicably in accordance with Clause [●], shall be resolved in accordance with Clauses [●]. In any other case, the Dispute shall be resolved in accordance with Clauses [*reference to Jurisdiction or International Arbitration clause as appropriate*].
- (7) A Technical Dispute shall be referred, at the request of either Party, to an independent expert for determination. The Parties shall agree on the appointment of the expert and shall agree with the expert the terms of his/her appointment. If the Parties are unable to agree on the identity of the expert, or if the person proposed is unable or unwilling to act, then, within [seven] days of either Party serving details of a suggested expert on the other or the proposed expert declining to act, either Party shall then be entitled to request that an expert be appointed by [the International Chamber of Commerce] on the application of a Party.

The governing law selected in a PPP Contract determines the legal system whereby the rights and obligations under the PPP Contract will be determined. Typically, the national law of the Contracting Authority will be the applicable law.

The clause could alternatively provide for a two-stage negotiation process, with senior representatives only being required to be involved at the second stage.

An alternative approach is to list individual experts on an agreed list and select from that list. However, the selection of individuals at the transaction stage may be a time-consuming distraction at a stage when the Parties are trying to complete the deal. Further, when a dispute arises there is a risk the experts identified may not be available or may be conflicted, especially in a long-term PPP Contract.

All costs of and associated with the request for the appointment of an expert by the [International Chamber of Commerce] shall be borne equally between the Parties.

- (8) The expert appointed may be an individual, partnership, association or body corporate and shall be generally recognized as an expert in [*specify field*] and shall have [X] years of experience in that field.
- (9) The expert shall act on the following basis:
 - (a) [on his/her appointment, the expert shall confirm his/her neutrality, independence and the absence of conflicts in determining the Technical Dispute]/[no person shall be appointed as an expert who at the time of appointment (or at any time before he/she gives his/her determination under such appointment, is a director, officeholder, employee or [] of []];
 - (b) the expert shall act as an expert and not as an arbitrator;
 - (c) the expert's determination shall (in the absence of manifest error) be final and binding on the Parties and not subject to appeal;
 - (d) the expert shall decide the procedure to be followed in the determination in accordance with this PPP Contract [and in consultation with the Parties] [and shall be requested to make his/her determination in writing, with reasons, within [30] days after his/her appointment or as soon as practicable thereafter];
 - (e) any amount payable by one Party to another as a result of the expert's determination shall be due and payable within [seven] days of the expert's determination being notified to the Parties or as specified within the determination;
 - (f) any action required by the expert determination shall be implemented within [14] days following the expert determination being notified to the Parties or as specified within the determination;
 - (g) the expert may, if he/she thinks fit, award interest at the rate of [●] on any amount which is determined to be payable (excluding costs) by one Party to the other from the date of [the Notice] referred to in Clause [●];
 - (h) the costs of the determination, including the fees and expenses of the expert (but excluding the Parties' own costs which shall be borne by the Party incurring those costs), shall be borne equally by the Parties.
- (10) The expert determination and all matters connected with it shall be held in complete confidence by each of the Parties and shall not be disclosed to any other person except:
 - (a) to the auditors and to the legal advisers of that Party to whom the confidentiality obligations set out in this agreement shall extend; or

It is essential to include an appropriate appointing body in case the Parties are unable to agree on an expert. If there is no appointing authority, the clause may fail altogether. The ICC offers three services whereby it will (1) put forward the name(s) of one or more experts or neutrals upon a request from one or more Parties, a court or an arbitral tribunal, (2) make a binding appointment if the Parties request this, or (3) supervise the entire expert proceedings if necessary. Alternatively, a number of professional bodies are willing to assist in selecting appropriate experts in their fields, so a relevant professional body could be named here.

Parties should consider whether they want to provide that the expert may not be connected with any particular companies or organisations due to the possibility of conflicts arising.

- (b) where that Party is under a legal or regulatory obligation to make such a disclosure, but limited to the extent of that legal obligation; or
 - (c) to the extent that it is already in the public domain (other than as a result of a Party's breach of this agreement); or
 - (d) with the prior written consent of the other Party to this agreement [such consent not to be unreasonably withheld].
- (11) The Parties agree to take all reasonable steps to make their employees and agents aware of the terms of [Clause (10)] and to instruct them to observe those terms.
- (12) If the Parties fail to agree:
- (a) whether or not a Dispute is a Technical Dispute within fifteen (15) days of service of the Notice;
 - (b) whether the expert's determination was in manifest error or fraudulent; or
 - (c) whether a Party has failed to implement fully the expert's determination,
- then the matter shall be resolved in accordance with Clauses [●] [reference to Jurisdiction or International Arbitration clause as appropriate].

Option 1: Jurisdiction [delete if choosing arbitration – Option 2]

- (13) The courts of [] shall have exclusive jurisdiction to determine any Dispute and any matter provided by Clause [(12)]. The Parties irrevocably submit to the courts of [as above] and agree not to argue they are an inconvenient forum.

Option 2: International Arbitration [delete Clauses (13) – (21) if choosing courts – Option 1]

- (13) Any matter provided by Clause [(12)] and any Dispute which is not a Technical Dispute and has not been resolved amicably between the Parties in accordance with Clause [(4)] shall be referred to and finally resolved by arbitration pursuant to the Rules of Arbitration of the International Chamber of Commerce (“ICC Arbitration Rules”) which are deemed incorporated by reference into this PPP Contract.¹¹⁶
- (14) The number of arbitrators shall be three (3) appointed in accordance with the ICC Arbitration Rules (the “Arbitral Tribunal”).
- (15) The arbitrators shall be fluent in [English and other relevant language]. The language of the proceedings shall be [English] and all documents submitted in such proceedings shall be in [English or accompanied by a certified English translation].

Broadly, this means that only the chosen court is competent to take jurisdiction over disputes, although this is usually subject to certain standard exceptions. It may be preferable to have certainty as to which courts will have jurisdiction by identifying the chosen court in this way. Other options exist and specific advice should be sought.

Where there is a US nexus, insert a “jury waiver” provision. Further, where proceedings need to be ‘served’ to be formally initiated then a process agent provision may be added.

Consider if this is potentially too restrictive.

¹¹⁶ For illustration purposes only, Option 2 drafting is based on a choice of the ICC Rules. It will need review/adaptation when using an alternative institution's rules.

(16) The seat of arbitration shall be *[insert choice]*. [This agreement to arbitrate is governed by and shall be construed in accordance with the laws of *[country]*.]

As noted, the seat of arbitration is key and requires careful consideration. See Section 11.2.3. It should be noted that arbitral hearings can physically take place in another location than the seat of arbitration. If the place of hearings (the venue) is important for the Parties, it should be agreed upon at an early stage of negotiations.

The Parties may wish to add a provision specifying the law applicable to the arbitration agreement. To keep matters simple it is often helpful to specify the same law as for the seat.

(17) The Parties undertake to keep confidential all awards in any arbitration, together with all materials in the proceedings created for the purpose of the arbitration and all other documents produced by another Party in the proceedings not otherwise in the public domain – save (i) with the permission of the Arbitral Tribunal or (ii) to the extent that disclosure may be required of a Party by legal duty or regulatory obligation or to protect or pursue a legal right, or to enforce or challenge an award in bona fide legal proceedings before a state court or other judicial authority.

(18) The Arbitral Tribunal shall issue a reasoned award in writing and shall endeavor to do so within *[sixty (60) calendar]* days from the date of the close of the arbitration hearing. The award of the Arbitral Tribunal shall be final and binding upon the Parties from the date it is made.

(19) Judgment on the award of the Arbitral Tribunal may be entered and enforced by any court of competent jurisdiction.

Unlike courts that may have an inherent discretion to consolidate related disputes or join Parties, as arbitration is contract based, the Parties need to provide the tribunal with jurisdiction to consolidate such proceedings.

(20) Unless otherwise determined by the Arbitral Tribunal, the Arbitrators' fees and associated institutional costs shall be split equally between the Parties.

Consolidation

(21) In order to facilitate the comprehensive resolution of related disputes, in the event that more than one arbitration is commenced under this PPP Contract and under *[add related agreements]*, (the "Related Agreements"), the Private Partner and the Contracting Authority consent to the consolidation of arbitrations as follows:

See discussion under Section 11.2.3, Step 4: Consolidation and Joinder – related contracts/related Parties.

(a) For the purposes of the Rules, the arbitration agreement set out in this PPP Contract and the arbitration agreement contained in each Related Agreement shall together be deemed to be an arbitration agreement that binds each Party to this PPP Contract and each Party to each Related Agreement.

If applicable, drafting should consider an exception/regime to address where claims brought in domestic and non domestic courts.

(b) Any Party to this PPP Contract or any Related Agreement may, in accordance with the ICC Arbitration Rules, be joined to any arbitration commenced under this PPP Contract or any Related Agreement.

(c) In accordance with the ICC Arbitration Rules, Disputes may be resolved in a single arbitration together with Disputes (as defined in any Related Agreement) arising out of any such Related Agreement.

(d) Pursuant to Article 10(a) of the ICC Arbitration Rules, the Parties agree to the consolidation of any two or more arbitrations commenced pursuant to this PPP Contract and/or the arbitration agreement contained in any Related Agreement into a single arbitration, as provided for in the ICC Arbitration Rules.

- (e) Each Party waives any objection, on the basis that a Dispute has been resolved in a manner contemplated in this Clause [●], to the validity and/or enforcement of any arbitral award made by an arbitral tribunal following the Dispute being resolved in that manner.

Continuing Obligations [Clause (14) if choosing Option 1]

- (22) Performance of this PPP Contract shall continue during [Option 1: court proceedings] [Option 2: arbitration proceedings] or any other Dispute resolution mechanism pursuant to this Clause [●].

Process Agent [Include if applicable – see Section 11.2.2.3 and adapt numbering if choosing Option 1]

- (23) [Specify Party not incorporated in the jurisdiction of the offshore court] irrevocably appoints [Add name of agent] as its agent under this PPP Contract for service of process for service of process [Option 1: in any proceedings before the [Specify Offshore courts]][Option 2: in the event that recourse is sought to the [Specify Offshore courts] in relation to any arbitral proceedings contemplated by this Clause]. If any person appointed as process agent under this Clause is unable for any reason to so act, [Specify Party] must immediately appoint another agent. [Specify Party] agrees that failure by a process agent to notify it of any process will not invalidate the relevant proceedings or render service of those proceedings ineffective. This Clause does not affect any other method of service allowed by law.

Waiver of Immunities [Adapt numbering if choosing Option 1 and/or if process agent clause used]

- (24) [To the fullest extent permitted by law the Contracting Authority irrevocably and unconditionally]:
- (a) submits to the courts of any jurisdiction in relation to the recognition of any judgment or order of the courts of [jurisdiction of arbitration seat] in support of any arbitration in relation to any Dispute and in relation to the recognition of any arbitral award and waives and agrees not to claim any sovereign or other immunity from the jurisdiction of any court in relation to the recognition of any such judgment or court order or arbitral award and agrees to ensure that no such claim is made on its behalf.
- (b) [consents to the enforcement of any order or judgment in support of arbitration or any award made or given in connection with any Dispute and the giving of any relief in the courts of any other jurisdiction whether before or after final arbitral award including, without limitation:

There may be circumstances in which a provision along these lines would not be appropriate. (e.g. if the PPP Project is not time critical and/or the Dispute is fundamental).

The Contracting Authority may wish to include a reservation of its immunities notwithstanding the disputes provision.

This clause is a wide-ranging waiver which a Contracting Authority is likely to want to resist or limit, in particular subclause (b).

Contracting Authorities may choose to agree to an immunity from suit waiver language because as a matter of applicable law such immunity is deemed to be waived, for example because it is a commercial transaction. Specialist legal advice should be sought. A Contracting Authority may wish to limit the waiver to specify submission to the jurisdiction of only one court.

- (i) relief by way of interim or final injunction or order for specific performance or recovery of any property;
- (ii) attachment of its assets; and
- (iii) enforcement or execution against any property, revenues or other assets whatsoever (irrespective of their use or intended use) and waives and agrees not to claim any sovereign or other immunity from the courts of any other jurisdiction in relation to such enforcement and the giving of such relief (including to the extent that such immunity may be attributed to it), and agrees to ensure that no such claim is made on its behalf.]

A Contracting Authority is likely to resist consenting to injunctive relief or attachments of its assets as this may be seen as disruptive and an unjustified erosion of its sovereignty. Much may ultimately depend on the respective bargaining power.

(25) The Parties agree that this PPP Contract is a commercial matter. The Contracting Authority is not immune from suit as any dispute concerns sovereign, not commercial, activities.

A Contracting Authority is likely to want to limit the assets against which enforcement action can be taken e.g. listing assets that are outside the scope.

SCHEDULE 1 – FURTHER DRAFTING OPTIONS

In addition to the informal negotiation provision included in [Section 11.3, Sample Drafting 11, Clause \(4\)](#), the Parties may decide to include some or all of the informal dispute resolution provisions below. When considering these further options, reference should be made to [Section 11.2.4](#). For illustration purposes, the drafting is based on a choice of the ICC Rules. This drafting will need review/adaptation when using an alternative institution's rules.

Option 1 – Mediation

- (1) If the Parties are unable to negotiate the settlement of a Dispute referred to in a Notice within [15] Business Days of the date of the Notice (or such further period as is agreed in writing between the Parties before the expiry of that [15] Business Day period), [either/any] Party may refer the Dispute to mediation by notice in writing to the other [Party/Parties] [at the address given for the sending of notices under this agreement at Clause [reference] (Notices), and in a manner provided for in that Clause] (a “Mediation Notice”). If a Party refers a Dispute to mediation in accordance with this Clause [Mediation] [both/all] Parties to the Dispute shall be obliged to follow the procedure below.
- (2) The mediation shall be conducted by a single mediator who shall be appointed by agreement in writing between the Parties. If the Parties are unable to agree on the identity of a mediator within [five (5)] Business Days of the date of the [Mediation Notice], or if the mediator agreed by the Parties is or becomes unable or unwilling to act, the mediator shall be appointed by [the ICC] on the application of [either/any] Party.
- (3) The mediation shall be conducted in [place] and in the English language under the [ICC Mediation Rules]. Each Party shall be represented at the mediation by an individual with authority to settle the Dispute.
- (4) Save for the purposes of implementing and/or enforcing a written legally binding settlement agreement or as otherwise required by law, the mediation shall be conducted without prejudice to the rights of the Parties in any future proceedings.
- (5) The costs of the mediation, including the fees and expenses of the mediator (but excluding each Party's own costs, which shall be borne by the Party incurring those costs) shall be borne equally by the Parties, unless otherwise agreed in writing.

Option 2 – Escalation to a panel of senior representatives

- (1) As soon as is practicable after the effective date of this agreement, the Contracting Authority and the Private Partner will establish a panel of senior representatives of the Parties (“Senior Panel”). The Senior Panel will meet and attempt to resolve informally any Disputes referred to the Senior Panel by notice for resolution (“Senior Panel Notice”).
- (2) The Senior Panel will comprise [four members], [two] appointed by each of the Contracting Authority and the Private Partner. Each Party is entitled to terminate the appointment of a representative designated by it to the Senior Panel and to appoint a replacement.

Option 1 may be useful to encourage informal resolution at an early stage in the dispute.

Option 2 is often seen in construction disputes, but can add costs and delay final resolution.

In many PPP Projects this option is omitted on the basis it is unnecessary and delays final resolution.

- (3) The representatives on the Senior Panel will be duly authorized to make decisions on behalf of, and to bind contractually, the Party appointing such representative in relation to the Dispute referred for determination.
- (4) [At any meeting the representatives on the Senior Panel may, by unanimous resolution, elect to appoint a mediator to assist them in resolving a Dispute on such terms as they may then agree.]
- (5) The Senior Panel must meet and attempt in good faith to resolve any Dispute referred to the Panel by negotiations within [fifteen (15) business] days of the date on which the Senior Panel Notice was delivered. If the Senior Panel fails to meet within this timeframe, and no extension is agreed by the Parties then either Party may submit the Dispute to arbitration or in the case of a Technical Dispute, an expert in accordance with Clause [Expert Determination].
- (6) Senior Panel Notices convening meetings of the Senior Panel will specify the nature of the Dispute.
- (7) Meetings of the Senior Panel will be held in [insert name of City or address] unless otherwise agreed by the Parties.
- (8) The quorum of any Senior Panel meeting will be [at least one representative of each of the Contracting Authority and the Private Partner]. If a quorum is not present within 30 minutes after the time appointed for commencement of the meeting, that meeting will be adjourned to a time, day and place agreed upon by the representatives of both Parties. In the event there is no agreement concerning the adjourned meeting or there is no quorum at the adjourned meeting, either Party may submit the Dispute to arbitration in accordance with Clause [Arbitration] or in the case of a Technical Dispute, an expert in accordance with Clause [Expert Determination].
- (9) The Senior Panel will attempt to resolve the Dispute within [ten (10) business] days, following the date on which the Senior Panel initially convenes pursuant to Clause (5), above. If the Senior Panel is unable to resolve the Dispute within that period, either Party may immediately submit the Dispute to arbitration or expert determination as required pursuant to Clause [Expert Determination] or Clause [Arbitration].
- (10) At any meeting of the Senior Panel, voting on any decision relating to the Dispute will be by unanimous resolution, with each representative having one vote. Duly passed resolutions of the Senior Panel will be final and contractually binding on the Contracting Authority and the Private Partner provided that they are in writing and signed by all members of the Senior Panel.
- (11) If the Dispute is not resolved by amicable settlement between the Parties or through a resolution by the Senior Panel, as evidenced by the signing of its written terms, within [thirty (30) calendar] days of delivery of the Senior Panel Notice provided in Clause (1) above], any Party may submit the Dispute to arbitration in accordance with Clause [Arbitration] or in the case of a Technical Dispute to an expert in accordance with Clause [Expert Determination].

Option 3 – Disputes Review Board Clause

- (1) Failing an amicable settlement on a Dispute that is not a Technical Dispute pursuant to Clause [*insert reference to the amicable settlement clause*] above within [*thirty (30) calendar*] days of the receipt of the notice provided therein, any such Dispute shall be referred by either Party for resolution by the dispute review board (“Dispute Review Board”) in accordance with this Clause [●].
- (2) The Parties hereby agree to establish a Dispute Review Board in accordance with the Dispute Board Rules of the International Chamber of Commerce (the “ICC Dispute Board Rules”), which are incorporated herein by reference.
- (3) The Dispute Review Board shall comprise three (3) members, each of whom shall be fluent in [*English*] with professional experience in the matters with respect to contractual obligations in projects similar to the PPP Project, appointed in accordance with the ICC Dispute Board Rules.
- (4) All Disputes arising out of or in connection with this PPP Contract shall be submitted, in the first instance, to the Dispute Review Board in accordance with the ICC Dispute Board Rules. For any given dispute, the Dispute Review Board shall issue a recommendation in accordance with the ICC Dispute Board Rules.
- (5) If any Party fails to comply with a recommendation when required to do so pursuant to the ICC Dispute Board Rules, the other Party may refer the failure itself, without having to refer it to the Dispute Resolution Board, to arbitration in accordance with Clause [*insert reference to the arbitration clause*]. A Party that has failed to comply with a recommendation when required to do so pursuant to the ICC Dispute Board Rules shall not raise any issue as to the merits of the recommendation as a defense to its failure to comply without delay with the recommendation.
- (6) If any Party sends a written notice to the other Party and the Dispute Review Board expressing its dissatisfaction with a recommendation, as provided in the ICC Dispute Board Rules, or if the Dispute Review Board does not issue the recommendation within the time limit provided in the ICC Dispute Board Rules, or if the Dispute Review Board is disbanded pursuant to the ICC Dispute Board Rules, the Dispute shall be finally settled under arbitration in accordance with Clause [*insert reference to the arbitration clause*].

Option 3 is often seen in construction disputes, but can add costs and delay final resolution.

See Section 11.2.4.2 as regards when to establish the Disputes Board.

SCHEDULE 2 – ASSESSING WHETHER THE PRIVATE PARTNER MIGHT HAVE RECOURSE TO AN INTERNATIONAL INVESTMENT AGREEMENT

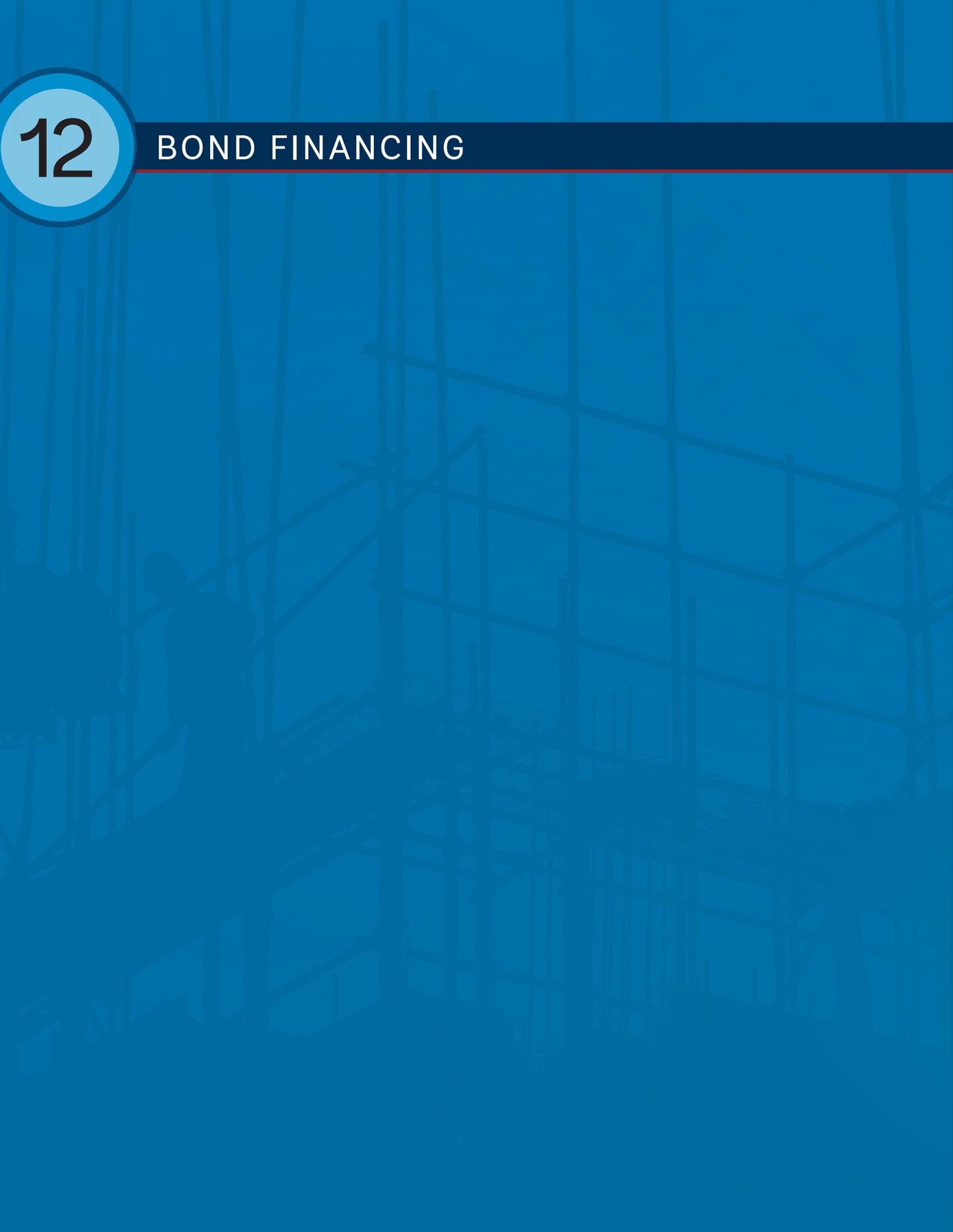
The Parties should consider whether the Private Partner may, in addition to its contractual rights, at some point have recourse to an international investment agreement (“IIA”), which could be either a Bilateral Investment Agreement (“BIT”) (of which more than 3,000 have been signed globally), a multilateral investment treaty (such as the Energy Charter Treaty) or the investment chapter in a Free Trade Agreement (“FTA”). These IIAs provide investors with a number of substantive protections against State measures, such as arbitrary and discriminatory treatment, expropriation without adequate and prompt compensation or failure to provide fair and equitable treatment and full protection of security. The majority of IIAs also provide investors with the right to refer investment disputes to binding arbitration against the host State in which they have invested.

If the home States of the Private Partner and the Contracting Authority are both Parties to an IIA, the Private Partner might, under certain circumstances, be able to bring claims for breaches of substantive protections set forth in the respective IIA, and which relate to the PPP Contract, under the arbitration mechanism established in the IIA. Very often, the mechanisms envisaged in this respect will be arbitration under the UNCITRAL Rules, ICSID arbitration or the ICSID Additional Facility Rules (an additional set of arbitration rules that apply to the settlement of disputes that do not meet the jurisdictional requirements set forth under the ICSID Convention). The Parties may wish to apply the UNCITRAL Rules on Transparency in Treaty based Investor State Arbitration in any subsequent investor-state arbitration between them.

It is important to note that generally the right to bring a claim pursuant to an IIA exists independently of, and may be in addition to, any contractual claims under the PPP Contract.

12

BOND FINANCING



12.1 KEY ASPECTS

12.1.1 *The concept of Bond Finance*

In the general corporate world, instead of borrowing from a bank, companies may choose to raise private finance by issuing bonds which are purchased by investors. Bonds in this context are debt instruments and may provide more certain, longer-term financing than bank debt. The company which issues the bond pays interest to the bondholders periodically, most commonly at a fixed rate but also potentially at a floating or index linked rate and repays the principal amount either in full on final maturity or in scheduled installments. As with a bank loan, specific documentation is required for a bond issue and there is an established process to follow.

Bond issues may be public (listed on a stock exchange) and freely tradeable between investors. Alternatively, bonds may be issued by private placement (offered to a very limited number of investors) in which case they may be subject to transfer restrictions. The restrictions will depend on the relationship between the issuer and the investors. A privately placed transaction can be listed or unlisted. If a bond is publicly listed, the issuer will have to comply with the listing authority's detailed rules on the level of information it must disclose to prospective investors about its business and also will be subject to securities laws which will dictate the specifics of the disclosure.

A public bond issue is usually assigned a credit rating by at least one rating agency. A private placement may or may not have a credit rating. This provides an independent assessment of the underlying credit of the issuer and is a guide to investors as to the likelihood of the issuer meeting its principal and interest payment obligations under the bonds. Some investors may only (for regulatory or policy reasons) invest in 'investment grade' issuances (i.e. those rated at least BBB- by Standard & Poor's or Fitch or Baa3 by Moody's).

As bonds can be issued with long maturity dates, they suit the investment profile of institutions seeking predictable long-term investments to match their maturing liabilities, such as pension funds and insurers.

12.1.2 *Why are PPP Projects bond financed?*

Prior to the 2008 global financial crisis, most PPP Projects were successfully financed through long-term commercial bank debt borrowed by the Private Partner. More recently, as a result of the financial crisis and ensuing banking regulation¹¹⁷, the volume of bank debt available for large infrastructure projects has reduced and loan tenor has shortened with a corresponding effect on pricing and the introduction of refinancing risk if debt cannot be obtained for the whole project period. In addition, comparing bids with different tenors has proved challenging, with questions around the non-compliance and comparability of bids without full-term committed pricing.

¹¹⁷ For example, the Basel III capital adequacy requirements imposed on banks.

This has meant that in some PPP markets (e.g. particularly Canada and Europe), both bidders and Contracting Authorities have had to consider alternative forms of finance – on the bidders’ side to ensure that their bids can be financed and remain competitive, and on the Contracting Authorities’ side to ensure that value for money is obtained from the range of financing options procured by bidders (e.g. by requiring non-bank financing solutions to be submitted as part of bids).

Even in markets where liquidity is not such a concern, there are also other reasons to consider bond financing as an alternative financing method. In some circumstances, bond finance – private or public – can offer long-term finance for PPP Projects at a more affordable price than bank debt. Recent examples of this in Developed Markets include the projects funded under the EIB’s Project Bond Credit Enhancement Programme. Due to the longer term repayment profile of bonds, scheduled repayments may be lower than bank loan repayments and, in such cases, this should feed through to a lower priced PPP Contract for the Contracting Authority (or end user). From the Private Partner’s perspective, it may also result in more cash being available for distribution to its Equity Investors during the repayment term than would be the case in a bank financing. The long-term (and generally fixed rate) nature of bond financing also enables the Private Partner to fix its financing costs for the life of the PPP Project (or the remaining life if after a refinancing) without the need for separate interest rate hedging arrangements, giving it certainty and reducing the likelihood of a subsequent refinancing. However, as discussed in [Section 12.3.2](#), bond financing is unlikely to be suitable for all PPP Projects, particularly those of smaller value due to the relative size of transaction costs.

Investor appetite is another reason to consider bond financing. Non-bank financial institutions (such as insurance companies and pension funds) are becoming increasingly interested in investing in PPP Projects because they recognize that the long-term predictable returns in PPP Projects can provide a hedge to the profile of their long-term liabilities. Facilitating the entry of such institutions to the PPP debt market widens the lender base and increases liquidity. With more private finance available, Contracting Authorities should in turn be able to procure more PPP Projects and at more competitive pricing.¹¹⁸

Bond financing of PPP Projects does have its own challenges, however, which are described further in this [Section 12](#). One key factor is that, particularly for a public bond, the pricing of the bond may not be finally committed until shortly (e.g. five business days) before financial close. This may cause difficulties for the Contracting Authority in the evaluation of bids, given that the choice may be between a bid with committed financing and one where the financing may be notionally more competitively priced, but on an uncommitted basis.¹¹⁹ A bond financing process also has certain timing implications which need to be factored into the procurement process. Some PPP Projects may also require credit enhancement in order to achieve a successful bond financing – this is discussed further in this [Section 12](#) and is particularly relevant in projects with specific risks (whether political, technological or developmental). In such cases, Contracting Authorities should consider engaging with potential credit enhancement providers early on in the procurement process if there are likely to be benefits in widening the field of possible financing options. [See Section 12.5](#).

¹¹⁸ A number of institutions have produced resources on bond financing as an alternative to bank financing of infrastructure projects. Please see links in [Appendix A, Additional PPP Resources](#) – these have been drawn on where appropriate in compiling this Guidance.

¹¹⁹ It should be borne in mind, however, that even in a bank financing, certain elements of pricing are only fixed at financial close – [see Section 12.3.4](#).

In some cases (e.g. due to the type of risks mentioned above or constraints such as timing), PPP Projects may be financed by other means (e.g. bank debt) at financial close but refinanced by bond financing at a later stage (usually after construction completion). This [Section 12](#) focuses primarily on bond financing at financial close but also touches on the refinancing approach.

The guidance in this [Section 12](#) gives an overview of the bond financing process in a PPP Project, highlights the factors a Contracting Authority will want to take into account in assessing whether bond financing could be a suitable option for its PPP Project and (if it decides that it is) what considerations are then relevant both during the bid phase and ultimately in reaching successful close with a bond-financed bid. The key point for the Contracting Authority is that it would need to be prepared to adapt its approach to facilitate bond financing where appropriate – this should not require the Contracting Authority to take on more risk or responsibility than under a bank financing.

12.2 UNDERSTANDING PROJECT BOND FINANCING

12.2.1 Overview of bond process

Bonds issued in a PPP Project financing context are commonly known as “project bonds”. The Private Partner may be the issuer of the project bonds itself, but it is common for the bonds to be issued by a special purpose entity (the “Issuer”), separate from the Private Partner, who on-lends the proceeds to the Private Partner. This may be for reasons of convenience, or for regulatory or tax reasons. Commonly, the Issuer and the Private Partner will be sister companies. Issuers, like Private Partners, must ensure they comply with their constitutional documents, applicable legislation and regulations and obtain all necessary internal and external authorisations.

The process for issuing the bonds will depend on whether they are to be publicly issued or privately placed. The timing depends on a range of issues and due diligence requirements, such as the time required for due diligence and credit review by rating agencies and investors, preparation of disclosure documents such as an offering memorandum or prospectus, the listing process (if applicable), the opening of bank accounts, planning and implementation of a roadshow marketing process and preparation of final transaction documentation.

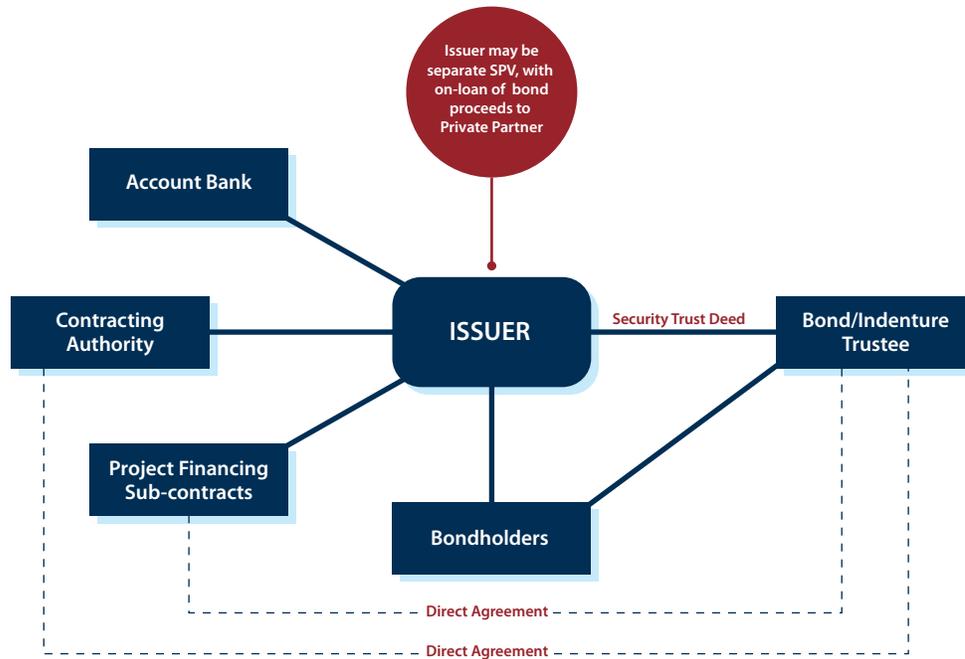
The arranging bank and Private Partner representatives usually go on an investor roadshow at which they will present the Issuer, the PPP Project, the management of the Private Partner, the proposed financing and the risk mitigation features, and give the investors the opportunity to ask for more information. In the case of a private placement, a similar but more targeted process aimed at individual investors would take place.

Project bonds are repaid in installments which may be equal or sculpted and/or a ‘balloon’ (larger) principal repayment at final maturity. Interest is typically paid regularly and is known as the bond “coupon” – this is the investors’ return.

12.2.2 Project Bond structure – single source financing

If a PPP Project is financed solely by bond financing, the structure will resemble this:

PROJECT BOND STRUCTURE – SINGLE SOURCE

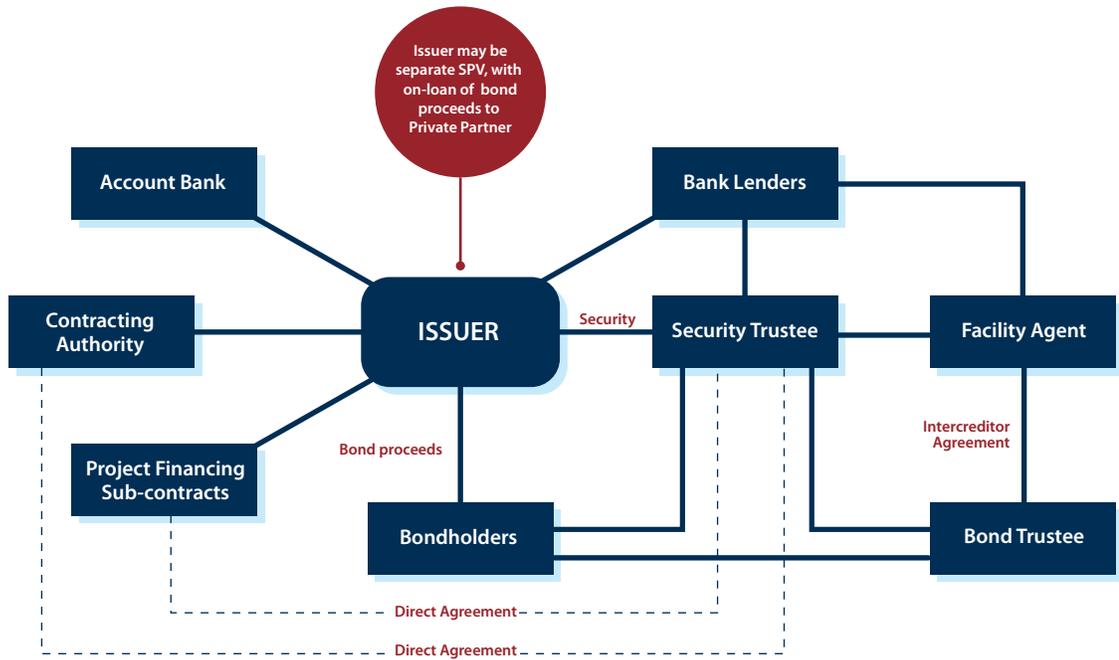


12.2.3 Project bond structure – multi-source financing

Many large project financing transactions include both commercial bank facilities and project bond financing. This multi-source approach may be used for a variety of reasons, including the diversification of financing sources, the use of bank financing as a temporary bridge while awaiting optimal capital market financing conditions and the need for revolving working capital finance, which realistically can only be provided by banks.

If the PPP Project is to be financed by a mixture of bond and bank finance, the structure is likely to resemble the following:

PROJECT BOND STRUCTURE – MULTI-SOURCE



12.2.4 Parties

The key parties in a project bond financing are the Issuer, the bondholders and, for a public bond, the arranger and the bond trustee. In a private placement there may be a representative for bondholders, but this is not universal.

As in a bank-funded project, a security trustee or agent will hold security interests for the bondholders.

12.2.5 Documentation

The bond-specific documentation will depend on the transaction, but a bond issue generally requires the following:

- A form of offering memorandum – this must contain all information and disclosure which an investor needs to make an informed investment decision. The standard of disclosure will be mandated by the rules of the relevant stock exchange and/or applicable securities laws. The Issuer is responsible and liable for the accuracy of this document both under securities laws and contractually under indemnities given to the arrangers under the subscription arrangements for the bond. The offering memorandum sets out risk factors relating to the bonds and information on the Issuer’s business, the project (including any risk mitigation), the Issuer, the Private Partner, any guarantor and the use of the bond proceeds. For a PPP Project, it also discloses the nature of the PPP Contract the Private Partner has with the relevant Contracting Authority. A public bond issuance will always involve an

offering memorandum; a private placement may have a (less formal) information memorandum. In each case, as well as its legal and contractual relevance, the offering memorandum is a marketing tool, used by the arrangers to sell the bonds.

- For a public bond issuance, a Subscription or Purchase Agreement – between the Issuer and the Arranger by which the Arranger subscribes for the bonds.
- A Trust Deed (or Indenture for New York law bonds) – between the Issuer and the Bond Trustee. The bonds are constituted under this document and it may contain the covenant package (if there is more than one source of finance, a common terms agreement may be used).
- For private placements, a Note Purchase Agreement or Note Subscription Agreement – under which the privately placed bonds will be constituted and the initial holders will agree to buy the bonds.

As with a bank financing, there will also be security, equity and intercreditor documents, and the PPP Contract will usually require some limited amendment as described in [Section 12.3.9](#) below.

12.2.6 Public bond issuance

As mentioned in [Section 12.2.1](#), public bonds may be issued either by the Private Partner, or by a separate (usually sister) company incorporated to issue the bonds and on-lend the proceeds to the Private Partner. An Issuer may choose to distribute its project bonds through either an arranger (typically a bank) or a syndicate of banks (in which case the arranger will be the “lead manager” or “lead arranger”). The arranger structures the transaction, and subscribes for the bonds pursuant to a Subscription Agreement (or less commonly underwrites the bonds via an Underwriting Agreement). In practice however, the arranger will only enter into the agreement to subscribe for the bonds a few days (normally five business days) prior to the closing date, and prior to doing so the arranger will have entered into back-to-back arrangements with investors whereby investors commit to buying the bonds from the arranger. If this arrangement is not honored by the investor, the arranger remains bound to subscribe for (or underwrite) the bonds pursuant to the terms of the Subscription (or Underwriting) Agreement.

12.2.7 Private placement issuance

The debt private placement process is similar to the public bond process but more straightforward. No arranger is appointed, but rather a placement agent who will facilitate but not underwrite the placement. No syndicate of banks is required as the debt will be privately placed to a small number of select investors. The terms and conditions of the bonds will be negotiated directly between the Issuer and the investors (similar to the negotiation process for a bank loan). Similarly, the flow of due diligence information will be directly between the Issuer and the investors. An agent will probably still be required to carry out administrative tasks, such as making the payments of principal and interest to investors.

12.2.8 Types of non-bank bond investor

Non-bank capital market investors are typically insurers, specialist fund managers, pension funds and sovereign wealth funds. Traditionally, some of these investors have tended to invest in project equity as opposed to debt, but they are now looking increasingly at the debt side. Their investment strategies vary and various factors influence their approach, such as market trends, investment beliefs, regulation, risk appetite, liability considerations, cultural factors, governance structures, tax issues, jurisdiction and, ultimately, domestically available assets. Some may require investments to have an investment grade credit rating or security, or to be listed. Others can hold non-investment grade or unrated instruments. The return they expect on bond investments will depend on the risks involved and how easily they can liquidate their investment. As with commercial banks, they will have competing demands on their funds and only invest if risks are mitigated to their satisfaction.

The two main challenges for institutional investors looking to invest in PPP Projects are understanding the risk profile of the asset and the need for extensive interaction with creditors. These are discussed further in [Sections 12.3.8 and 12.5.1](#).

12.2.9 Drawdown of Bond Finance

Bond proceeds are usually received in a lump sum at Financial Close, but as the PPP Project's expenditure profile may vary, the Private Partner will need to invest these proceeds until they are actually required by the PPP Project over its construction period¹²⁰. This typically results in a "negative carry" because the interest received by the Private Partner is generally lower than that paid to the bondholders (although this may be mitigated by an overall lower cost of funding). This contrasts with traditional bank financing where funds are drawn over the construction period as and when required.

In some circumstances (more likely in private placements), the bondholders may agree to staged drawdown of the bond proceeds (more in line with the PPP Project's expenditure profile). This means that bonds are only issued and subscribed for effectively as and when the funding is needed, rather than all being issued at financial close. While this may reduce the risk of negative carry, bondholders may require a higher return on their investment because they have to keep those funds available and are not able to freely invest them elsewhere. A staged drawdown structure will generally limit the universe of potential investors as only certain investors can cope with it. This is one reason why PPP Projects have been bank financed during the construction period and then refinanced by project bonds once financing is fully drawn and construction has completed so cash flow is being generated.

EMERGING AND DEVELOPED MARKET DIFFERENCES

A staged drawdown structure is less likely to be workable in an Emerging Market PPP Project. Similarly, while alternative solutions to reduce/avoid negative carry have been tried in Developed Markets, these are likely to be highly bespoke and only feasible for a certain class of investor in an established market.

¹²⁰ In a bond financing, the proceeds are often deposited with a highly rated bank until required, through a fixed-rate deposit, to reduce the cost of servicing unutilized debt.

12.2.10 Credit rating

As stated above, bond issuances (especially public issuances) often carry a credit rating from an external credit rating agency. Many investors will, for regulatory, capital adequacy or policy reasons only be able to invest in rated instruments. A credit rating is used as a tool during the marketing of the bond to investors.

Typically, each rating agency would also publish a ‘pre-sale report’, setting out its rating rationale for the PPP Project and assigning a provisional rating (denoted by a “[P]” in front of the rating). Information from the pre-sale report will typically be used to facilitate the roadshow phase. A definitive rating is typically assigned once the bonds have been issued and following the agency’s review of final documentation.

12.3 KEY CONSIDERATIONS FOR THE CONTRACTING AUTHORITY

12.3.1 Advisers

If bond financing is under consideration, the Contracting Authority should ensure it engages legal and financial advisers with the requisite experience in project bonds (as well as other financing options) as early as possible. Such advice will be essential in assessing suitability of financing, formulating bid requirements, evaluating bids, assessing pricing and deliverability, reviewing the relevant financing documents and understanding how the bond financing impacts the PPP Contract provisions and mechanics. As flagged in [Section 8.2.2, Termination Payments](#), understanding the relevant agreements is also key to limiting the Contracting Authority’s liability under any compensation provisions linked to the financing documents.

Suitability of financing

If the Contracting Authority wishes bidders to be able to submit the best value financing available, the bid process should, where appropriate, allow for financing approaches other than bank debt. At project preparation stage, the Contracting Authority should therefore assess the suitability of the key features of its proposed PPP Project for bond financing and, if it is considered suitable, publicize this to bidders when the PPP Project is first launched. In such circumstances, bid documentation and procurement rules should be drafted accordingly.

While the Private Partner will ultimately decide on its financing approach, the Contracting Authority’s role is to be neutral as to the financing method to the extent appropriate for its PPP Project, but to facilitate, where appropriate, different financing methods. Selecting the right type of financing will depend on a PPP Project’s particular characteristics. Both Sponsors and Contracting Authorities will need to take into account a range of factors and assess how these compare under different financing approaches (e.g. bank or bond financing – whether public or private placement). These include the flexibility to accommodate changes to circumstances over the life of the PPP Project, the degree to which the tenors and interest rate structures offered by finance parties lending through each type of financing best suit the requirements of the PPP Project’s revenues and debt profile, the nature of the transaction risk and the risk appetite of the target investors, the importance of confidentiality (in the context of the level of disclosure which may be required), the all-in cost effectiveness and economics of the method chosen, and the consequent value for money.

Contracting Authorities should bear in mind that bond financings involve significant preparatory costs (e.g. obtaining a credit rating, preparing the bond documentation and marketing). Legal costs can be significant especially in the case of publicly listed issues. Because of their costs, complexity and investor appetite, bond financings are typically best suited to PPP transactions of a significant size (e.g. involving bond financing in excess of USD200 million). Whilst public offerings may suit larger transactions, private placements, given the more flexible information flow and the less rigorous disclosure requirements, are potentially more suited to the PPP market. In addition, the universe of private placement investors is growing and therefore liquidity is enhanced.

If public authority bidding procedure rules require certainty of financing this may limit the choice to a degree. As explained above, in a public bond solution, the pricing and availability of the financing will as a rule only be committed very shortly prior to closing, although, as noted, elements of a bank-funded solution are similarly uncommitted until closing. In certain jurisdictions, the choice of financing for public authorities may also be shaped by practice rather than by law. [See Section 12.3.6.](#)

12.3.3 Comparing bids

Comparing bids can be more complex where different financing solutions are presented and bid documentation should be drafted to facilitate a transparent comparison of all finance solutions or categories of solutions.

One option for the Contracting Authority may be to require bidders to submit a compliant bid based on specific terms (e.g. bank debt), but to permit variant bids as well (e.g. bond financing). The Contracting Authority should bear in mind that preparing two financing offers is costly for bidders and bidders are likely to want to select a financing approach as the bid process reaches the latter stages and a fully developed solution is typically required. As is the case for any tenders that require significant bidder investment, the Contracting Authority may wish to consider whether it is appropriate to reimburse part of the costs associated with preparing financing proposals.

As flagged in [Section 12.3.1](#), specialist expertise is essential to assist in bid evaluation and, as regards bond solutions specifically, to assess differences in placement capability, pricing levels, pricing features and means of managing pricing risk – a process which can be more complicated in bond financings due to the pricing process. [See Sections 12.1.2, 12.3.4 and 12.3.5.](#)

12.3.4 Assessing deliverability

The deliverability and pricing of public bonds are normally only firmed up shortly before actual issuance (i.e. a few days prior to financial close) as the underwriting of bonds by their arrangers is not common practice. An element of deliverability risk will therefore remain with the Contracting Authority in a way which would not be the case in a bank financing. The position can be different in the private placement market, although this will depend on investors being willing to hold pricing during a bidding process. Contracting Authorities will often find it difficult to seek fully committed bond financing offers at bid or final offer stages and commitments obtained from banks at bid or final offer stages may be – or appear to be – stronger than those obtained for bond solutions. It should however be borne in mind that, whilst margins for bank debt may be fixed and commitments (which will generally have a certain level of

conditionality attached) can be obtained from banks in relation to the margin, the underlying swap rate which will affect the all-in cost payable by the Contracting Authority will only be fixed at financial close. Therefore, whilst deliverability risk may be somewhat greater in a bond solution, elements of the final cost of a bank solution equally remain a Contracting Authority risk until financial close.

Contracting Authorities can obtain some comfort that a public bond solution can be delivered by requiring bond arrangers to provide letters of support at bid or final offer stages and relying on the expert opinion of the Contracting Authority's adviser. The terms of the bond arranger support letters should therefore be set with care. In addition, at final offer stage, to help in mitigating the deliverability risk, it is advisable that the Contracting Authority require bidders to obtain a "pre-rating" on their proposed financial structure. The Contracting Authority may also ask bidders to (i) submit evidence that a minimum rating sufficient to drive investor demand is achievable (e.g. investment grade – that is, BBB or higher, or even A) and (ii) accept the risk of any price increases associated with failing to eventually secure the targeted rating. As flagged in [Section 12.3.3](#), Contracting Authorities may need to compare bond proposals from several bidders.

12.3.5 Assessing price

In order to be able to carry out a proper comparison of financing offers, the Contracting Authority should set out in the tender documents clear minimum requirements and evaluation criteria to facilitate a correct comparison of (uncommitted) bond financed bids as against committed bank or corporate financed bids. The same complexity occurs when bidders are allowed to submit offers with mixed financing. The Contracting Authority may also wish to include requirements relating to rating (both the level and the identity of the agency or agencies providing the rating). In addition to assessing price (which may be difficult without a firm pricing commitment), it is key to assess the risk and robustness of the pricing methodology used by bidders for any proposed bond solution (detailing the various pricing components). The pricing methodology should refer, to the extent possible, to market prices for similar bond issues or baskets of bond issues or, where such comparators are not available, sovereign issuances or issuances by government agencies or parastatal organisations could potentially be used as reference points. When seeking final offers, the Contracting Authority may consider providing indicative bond pricing data or benchmark yield curves on which bidders can base their offers. Bidders would use such pricing in their financial models to derive the price of their offer. Such pricing data should break down information according to different rating outcomes and other key features of the financing. The Contracting Authority could consider setting a pricing range within which the PPP remains affordable and the bonds would be issued and reserving the right not to close the transaction if pricing falls outside this range.

12.3.6 Price fluctuation between preferred bidder and financial close

As mentioned in [Section 12.3.4](#), the pricing of public bonds (and in some cases private placements) is only confirmed a few days prior to actual issuance and final public bond pricing is largely market-driven, so there is a risk of price fluctuation between final offers and financial close. In order to help eliminate any potential uncertainty in price between the bid stage and final pricing, at an early stage of the procurement process the Contracting Authority and the bidders should discuss a risk sharing mechanism for allocating the risk of price fluctuations. Depending on the jurisdiction, this will often result in bidders providing a firm upfront commitment, with the fluctuation risk being assumed as agreed – usually by the Contracting Authority but sometimes by all (or a combination) of the Sponsor, the bidder, the investors and the Contracting Authority. Such mechanisms may also be left to the bidders' discretion as part of their bid strategy.

Following the appointment of the preferred bidder, the Contracting Authority should also require the preferred bidder to track pricing movements and inform it on a regular basis up to financial close.

Contracting Authorities should also ensure that the mechanics of the closing fit with national (public) law rules on budget approvals (as the preferred bidder announcement or award may take place for a price that will only be determined after the award and may need to be conditional).

CIVIL AND COMMON LAW DIFFERENCES

Some civil law public procurement rules may oblige the Contracting Authority to agree on a total cost of the PPP Project at an early stage. This may steer the transaction towards bank financing and private placements because the price in a public bond issue is only set at the 'pricing' stage (a few days before issuance) which creates uncertainty in the exact total cost of the PPP Project. This seemed to be a feature of the French market for a time, but PPP Projects have been totally or partially bond financed in recent years.

Belgian market practice, and to a large extent public law, is in many ways similar to France, but again a bond-financed road project proved possible through a combination of innovative tender and contract rules, including measures whereby the Contracting Authority could assess and approve maximum expenditure prior to contract award.

12.3.7 Timing

Contracting Authorities need to be aware that bond solutions generally require more time to prepare than bank solutions as there is usually a need to obtain credit ratings, prepare the bond placement documentation, market the bonds with investors and meet regulatory requirements. The procurement timetable will need to cater for this.

As flagged in [Section 12.2.10](#), a pre-rating may be required at final offer stage and a final rating at financial close. A rating process typically lasts for at least four weeks – longer for a more complicated transaction. However, the preparation of the required supporting material needs to track the progress made in developing a bid. As a result, the process of seeking a pre-rating can only start once the deal structure (e.g. risk sharing, other key terms of the PPP Contract) is stable and is unlikely to change materially. Likewise, a

final rating can only be sought once the PPP Project documentation is virtually finalized. Overall, once a preferred bidder has been selected and the PPP Project documentation is finalized, seeking a final rating and marketing the bonds may take four to six weeks longer than financial close in a bank financing.

12.3.8 *Bondholder decision-making*

Holding project bonds requires more resources than holding sovereign or corporate bonds due to the need to respond efficiently to the numerous waivers, change consents and other issues which will inevitably arise during a PPP Project's construction phase. A key difference to bank lenders is that institutional investors may not have the same capacity to be actively involved with the Issuer and the Private Partner, however, particularly in Europe, there are more and more active private investors who will wish to be – and be capable of being – closely involved with a PPP Project on an ongoing basis. The Contracting Authority and its advisers need to be aware of this and check that the bondholder decision-making mechanisms in place will not inhibit the Private Partner's ability to perform the PPP Contract.

In monoline-guaranteed bonds, this risk was mitigated by the monoline acting as “controlling creditor” and taking decisions on behalf of the bondholders. This structure has, however, caused problems where monolines have been downgraded, but still continue to be entitled to take such decisions, despite not offering tangible credit enhancement. There are other mechanisms, known as monitoring advisers or similar, designed to facilitate effective decision-making, although these have not met with universal acceptance in the market since the monitoring adviser does not provide credit and therefore has no risk position alongside the bondholders to protect in its decision-making. Credit enhancement structures may achieve a similar result where there is a “credit provider”. [See Section 12.5.](#)

12.3.9 *Changes to documentation*

If a PPP Project is to be bond financed, the PPP Contract drafting must reflect the structure, parties and documentation involved. The key point to bear in mind is that in practice the drafting will not require much amendment. Broadly speaking, the main provisions affected are:

- Definition of the financing documents (e.g. “Senior Finance Documents”) – this will need to include the bond finance documentation (but not any on-loan documents between the Issuer and the Private Partner).
- References to the relevant parties – the Issuer may need to be referred to if separate from the Private Partner and the definition of Lenders may need adapting.
- Termination payments – these need to reflect the bond mechanics. [See Section 12.4.](#)
- Confidentiality – apart from facilitating the disclosure around the PPP Project in the offering memorandum, the provisions will also need to permit details of the PPP Project to be disclosed to potential investors where the bonds are transferable. In addition, as well as the initial disclosure in the offering memorandum of the project arrangements, including details of contracts, securities laws will generally require ongoing public disclosure of project performance, especially of significant

underperformance. This should both be borne in mind by project participants and be reflected in the Project Contract.

- Refinancing – the provisions need to permit ordinary trading of the bonds without triggering the refinancing provisions (e.g. by adapting the definition of “Exempt Refinancing”).

The same applies to ensure the Direct Agreement works effectively (*see Section 7, Lenders’ Step-in Rights*). Additional changes may be required to reflect certain bond mechanics (e.g. different reporting requirements/timing) and more than one Party may want the rights normally afforded to the Agent (e.g. both the Credit Provider and the Security Trustee would normally receive all notifications usually provided to an Agent).

In considering amendments to documents, a Contracting Authority wishing to attract the full range of financing options will want to avoid making bond-specific amendments beyond those strictly necessary to ensure that it is not making other finance solutions less attractive to bidders and/or discouraging bank debt providers from participating. It will also want to ensure that any solution-specific amendments are objectively and duly justified.

Where the PPP Project is being financed through other means (e.g. bank debt) at financial close, but a bond refinancing is envisaged upfront, contract provisions should be drafted with this in mind. This may entail drafting provisions appropriately in the PPP Contract signed at financial close (e.g. as regards refinancing), as well as potentially scheduling amendments designed to come into effect when the bond refinancing is implemented. If a bond refinancing has not been contemplated in the PPP Contract, appropriate amendments will need to be agreed at the time when discussing consent and related matters. *See Section 5, Refinancing.*

12.4 TERMINATION PAYMENT CALCULATION

12.4.1 Calculation of Outstanding Senior Debt

Only bonds that have been issued and purchased at financial close should count as Outstanding Senior Debt. Bonds which have been issued but are being held by the Issuer to be sold to raise further financing at a later stage (e.g. to cover the cost of certain changes required under the PPP Contract) should not count until they have actually been purchased. Only the actual amount paid for the bonds should be taken into account – if they are not issued “at par” (i.e. at their face value) but at a premium or a discount, careful consideration will be needed as regards their treatment.

12.4.2 Make-whole payments

The terms and conditions of project bonds usually include break cost provisions where there is an early repayment of the bonds to compensate bondholders for the loss of yield over the remaining life of the bonds. The bond terms will therefore generally call for the payment of a prepayment fee to put bondholders in an equivalent position as if the bonds had not been prepaid. This is known as a “make-whole” payment and is calculated according to a specified formula which applies a particular discount rate (which will be based on the yield on a government bond with a maturity equivalent

to the average life of the bonds), reflecting the fact that the payment is received early. Essentially, the make-whole amount would notionally allow the investor to invest the amount received in early redemption in a government bond and receive the same yield as if it had remained invested in the project bond. Contracting Authorities may wish to consider imposing more risk on investors by adding a margin to the government bond yield to produce the discount rate.

It may not be appropriate for the Contracting Authority to include such break costs in the termination compensation calculation for every termination situation. The recommended approach in some jurisdictions (e.g. the UK and Belgium) has been for the Contracting Authority to pay the full make-whole amount on termination for Contracting Authority default¹²¹, a reduced amount on voluntary termination, and no payment on any other termination (including Force Majeure and Private Partner default termination) although Contracting Authorities should consider whether a full make-whole payment is required in any circumstances. However, in Emerging Markets, for example, there may be justifications for including a make-whole amount in more termination scenarios (e.g. Force Majeure or potentially Private Partner default, although – particularly in the latter case – the value for money question would have to be addressed). In relation to private placements, some investors (particularly US investors) will insist on currency swap breakage payments on early termination of non-USD instruments, since such investors fund themselves only in US dollars. Contracting Authorities will need to consider the value for money questions inherent in funding such payments. *See Section 9, Handback of Assets at End of Contract.*

12.4.3 Fees and other costs

As with bond break costs, the Contracting Authority will also want to ensure that other bond-related fees and costs are only included in the termination compensation calculation if appropriate and that there is no double counting between the various financial instruments. There may also be fees associated with guarantees or other credit enhancement products.

12.5 CREDIT ENHANCEMENT

12.5.1 Benefits of credit enhancement

Credit enhancement can be helpful for PPP Projects that face challenges in long-term financing, or might otherwise not be financeable at all. It is also useful for large PPP Projects where liquidity may be an issue. While credit enhancement is not always essential, it is likely to be extremely useful, if not vital, in successfully financing PPP Projects with particular risks (e.g. political, technological or developmental). The Contracting Authority needs to be alive at an early stage of the procurement process to where credit enhancement and particular credit ratings are likely to be required by investors and how this could benefit it by possibly lowering the cost of financing

¹²¹ By extrapolation, other termination events for which the Contracting Authority bears the risk (e.g. MAGA and change in law) might follow a similar approach.

and resulting in a more competitive price and better value for money. The Contracting Authority should be prepared to engage early on with potential credit enhancement providers. [See Section 12.2.10.](#)

One example of a key challenge in achieving a successful bond financing at financial close is construction risk. The bond market has traditionally been averse to investing prior to construction completion, due to the perceived risk of the asset not being built and being unable to start earning income to meet principal repayments under the bonds.¹²² There are signs that investor attitudes are slowly changing as the investors begin to understand PPP Project risk better. Studies of infrastructure projects (e.g. by Moody's¹²³) have shown that the default rate in PPP Projects is relatively low (perhaps because of the level of due diligence typically carried out by all parties before PPP Contract signature, the in-built checks and balances in the project and finance documentation and the mutual desire of all parties to ensure the PPP Project starts generating income). However, credit enhancement can also help mitigate this risk to encourage non-bank investors' appetite.

Credit enhancement usually has the effect of taking the "first loss", insulating bondholders against a certain level of loss in a default or termination scenario, and/or providing liquidity in times of cash flow stress. This can provide reassurance to potential investors as well as potentially resulting in a higher credit rating. Depending on the form of credit enhancement, it may also result in the credit provider being the controlling creditor for decision-making purposes. [See Section 12.3.8.](#)

EMERGING AND DEVELOPED MARKET DIFFERENCES

The institutional investor market for infrastructure in Europe has evolved to the extent that there is now a ready supply of institutional capital for robust PPP Projects in stable countries. Credit enhancement is not always needed. However, it will continue to be needed to facilitate the use of non-bank funding in PPP Projects with technology risk, unusual development or construction risk, significant demand risk or in challenging jurisdictions.

12.5.2 Types of credit enhancement

Project bonds can be credit enhanced in whole or in part through various means, including:

- **Guarantee:** a guarantee of the Private Partner's obligations might be provided by a Sponsor (if it has a suitably high credit rating), a bank or a multilateral agency. In some cases, a guarantee might equate to wholesale credit substitution (as distinct from enhancement).

¹²² As in a bank financing, a bond financing is typically structured so that interest payments during construction are met out of drawdowns.

¹²³ Moody's Investors Service Data Report (5 March 2018): Default and Recovery Rates for Project Finance Bank Loans, 19832016.

- **Wrap:** this is the provision of insurance by a highly rated private sector financial guarantor (often a ‘monoline’ insurer), insuring the underlying principal and interest payments on a bond in return for a fee. Although not uncommon in Europe before the financial crisis, only one major international monoline insurer continues to operate. The insurer’s credit rating is key to the rating of the bonds.
- **Sovereign Guarantee:** in some circumstances, it may be value for money for governments to provide a guarantee (typically in return for a fee). This may be part of a concerted program to facilitate infrastructure investment.
- **Multilateral product:** the World Bank, MIGA and IFC have a long track record in providing guarantees for bonds.¹²⁴ These guarantees generally focus on specific risks which the private sector is unable to manage (such as adverse government action) and are available to World Bank and IDA countries. MIGA insurance focuses on political risk. More generally, since the financial crisis, bodies such as the EIB and the Asian Development Bank¹²⁵ have been considering ways to boost liquidity and incentivize capital markets investors to invest in infrastructure in both Developed and Emerging Markets. Multilateral funding agencies and development banks are the ideal channel for this type of support because they have both the credit quality and the political influence to stimulate investor appetite.

The EIB Project Bond Credit Enhancement Programme (PBCE) was launched to provide support for capital markets financing of infrastructure and to broaden the investor base for infrastructure projects. It offered credit enhancement in two forms: funded (internal) involving EIB as an internal Party investing in the capital structure, and unfunded (external). The unfunded form involved the provision of a standby letter of credit in favor of the bond trustee for 20% (and 30%, following the pilot phase) of the value of the bond. EBRD and MIGA also partnered on a risk mitigation product used on a Turkish project. EBRD provided a liquidity facility for construction cost overruns and to keep debt payments current during operation and MIGA provided political risk insurance to insulate the project from the risk of certain adverse government action.

Ten projects involving the PBCE were successfully bond financed in its pilot phase. Moody’s Investors Service¹²⁶ reported that this demonstrated the effectiveness of project bond credit enhancement in improving projects’ risk profiles, including in these cases by mitigating country-specific risk by achieving project ratings at or above the rating of the host sovereign¹²⁷ (which the EBRD/MIGA product also achieved). Both the PBCE and the EBRD/MIGA products have therefore had the effect of making the project bonds into an investment as safe as, or indeed safer than, government bonds.

124 <http://treasuryworldbank.org/documents/GuaranteesMatrix.pdf>

125 In 2015, Asian Development Bank provided a 75% guarantee to a Philippine project bond.

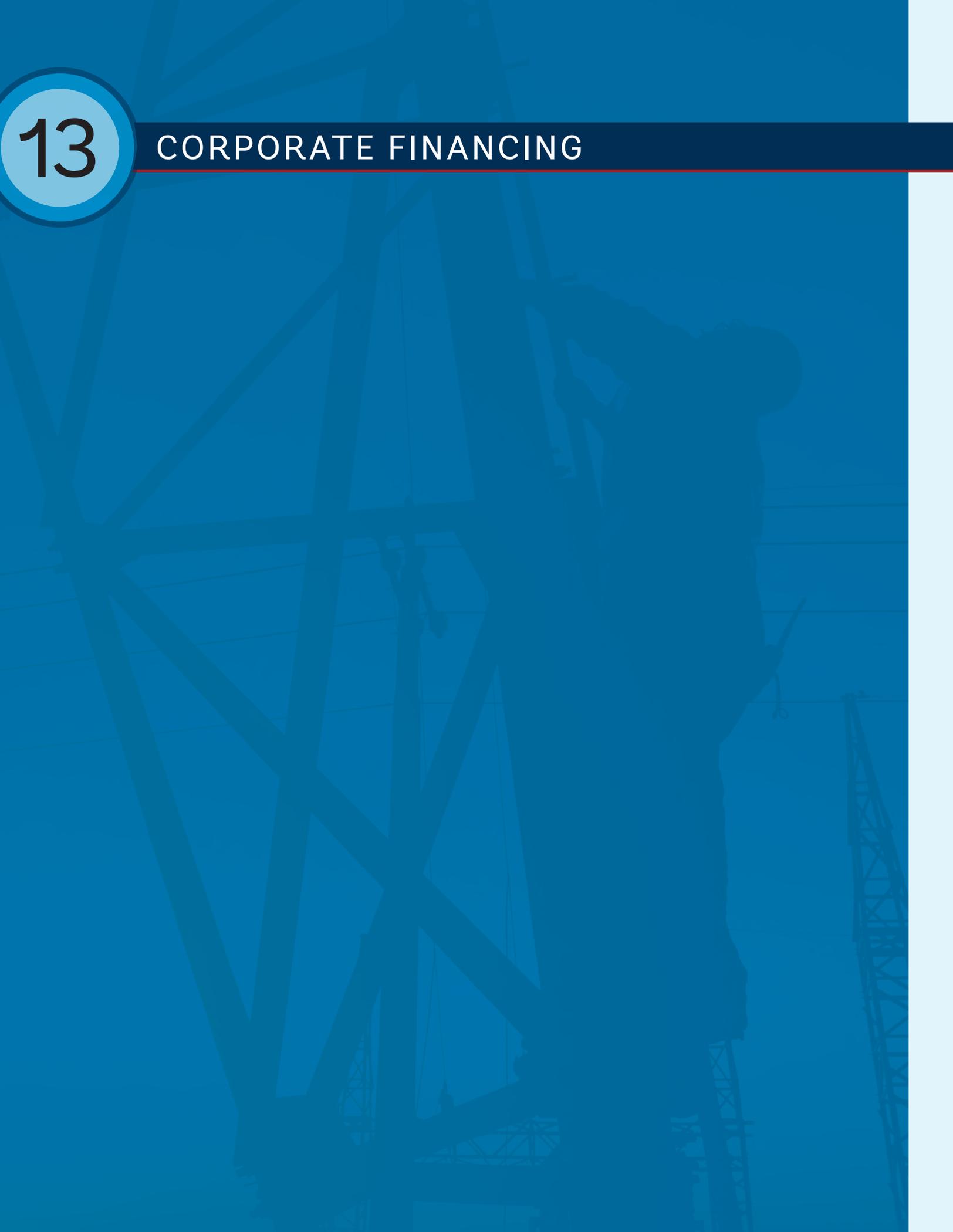
126 Moody’s Investors Service Sector In-depth (14 April 2016): Infrastructure Renewal and Investment – Europe project bond market set for growth after pilot initiative endorsed

127 As shown by the rating Moody’s assigned the N25 in Ireland (Baa1 positive) and CAV in Italy (Baa2 stable).

EMERGING AND DEVELOPED MARKET DIFFERENCES

Credit support such as the PBCE could be used to mitigate sovereign and macroeconomic risks as well as project-specific risks. It could benefit PPP Projects which are higher risk in stable creditworthy countries, as well as PPP Projects in countries with weak or challenging credit profiles. Many such credit enhancement tools are already available for this purpose from multilateral and bilateral institutions and their use is being gradually mainstreamed and increased.

Credit support can also overcome basic unfamiliarity with non-bank funding for infrastructure even in more developed financing markets (e.g. the first Belgian project bond was a PBCE pilot project).



13.1 KEY ASPECTS

13.1.1 *The concept of Corporate Financing*

Corporate entities typically use a range of financing means to fund their daily business needs across their corporate group. They will have credit facility arrangements with their relationship banks and may also raise finance through bond issues (public or private). They may also have multiple operating assets already generating revenue. If a new investment opportunity arises (such as a PPP Project), some corporate entities may prefer to put in place additional finance on a corporate basis instead of going down an investment-specific route (such as project finance). The strength of the corporate entity's balance sheet (potentially alongside consortium partners, parent companies or key Sub-contractor(s)) will be key to its ability to do this, as generally the lenders or investors involved in the new corporate financing will have recourse to the whole corporate entity, not just the specific asset being financed. Depending on the size of the corporate entity relative to the size of the investment in question, the lenders or investors may in fact be less concerned with the asset itself, and more focused on the performance of the corporate entity as a whole.

Some corporates may not even need to enter into specific additional financing arrangements for particular investments as their balance sheets are so strong that they have sufficient financial reserves to finance the investment in question.

The funding of investments in this way is called corporate financing and is also known as “on balance sheet” financing.

13.1.2 *Why are PPP Projects financed “on balance sheet”?*

As described in [Section C, PPP Contracts in Context](#), PPP Projects are typically funded through limited recourse project financing of an SPV owned by Sponsors. This is both because of the need to bring together different Sponsors to build and operate an asset (e.g. financial investors would not have the technical capability to build the required asset) and possibly because the amount of finance required is usually beyond the balance-sheet capacity of an individual Sponsor. Project financing is usually classified as “off balance sheet”, which may be useful from an accounting perspective for the parties involved and can often have a lower cost of capital than corporate financing because of the high gearing of cheaper third party debt to more expensive equity.

However, although not commonly used, corporate/on balance sheet financing can play a role in PPP-type projects and may be suitable in a number of circumstances. These include where a bidder is the sole Sponsor, has a strong balance sheet and typically uses corporate finance for new projects as part of its normal business model or where it may be more cost-effective to use balance sheet financing to reduce transaction costs (e.g. on smaller transactions). A bidder may wish to finance through equity rather than limited recourse financing for tax reasons or because it is willing to take more risk than third party lenders are prepared to take in a particular market (particularly

if it has access to export credit or other support) or simply because it is an overall less expensive form of funding. From the Contracting Authority's perspective, if a project is to be financed on balance sheet, the key is to ensure that an appropriate risk allocation is maintained between the Contracting Authority and the Private Partner, following the same principles as in a project financing (and as outlined in this Guidance). Ideally the procurement process should accommodate bids using corporate and other types of financing, as well as a mix. It is important to ensure that, the tender and (if applicable) draft-contract documentation works for different financing scenarios. In some circumstances, it may also prove simpler, faster and more cost-effective – e.g. because of the fewer parties (and advisers) involved and simpler documentation and debt mechanics.

It is also possible that PPP Projects may be financed by a combination of project and corporate finance and the procurement process and documentation will need to be adapted appropriately. For the purposes of this [Section 13](#), the assumption is that the PPP Project is to be wholly corporate-financed.

13.2 KEY CONSIDERATIONS FOR THE CONTRACTING AUTHORITY

13.2.1 Advisers

If corporate financing is an option, the Contracting Authority should (as with any form of financing under consideration) ensure it has engaged legal and financial advisers with relevant expertise as early as possible in the procurement process. Specialist advice will be needed in relation to formulating bid requirements, evaluating bids and assessing how the corporate financing impacts the PPP Contract provisions and mechanics. Understanding the overall contractual structure will also be key in formulating any compensation provisions and limiting the Contracting Authority's liability under the PPP Contract appropriately.

13.2.2 Procurement implications

As highlighted in [Section 12, Bond Financing](#), if the Contracting Authority wants bidders to be able to submit the best value financing available, the bid process must allow for a range of financing approaches. The Contracting Authority should consider from the start of the procurement process the implications of a corporate-financed bid as compared with a limited recourse project-financed bid. The procurement documentation should make clear whether such bids are permitted and what the bidder will need to address in its bid in terms of minimum requirements (e.g. regarding price commitment and contract terms), and in particular in place of bank commitment letters. The bid documentation should also spell out transparently how bids will be evaluated and how different solutions will be compared. Not only will this facilitate alternative financing solutions, but it will also mitigate the risk of non-compliant bids. Setting sufficiently ambitious prequalification/selection criteria (including as regards financial standing) and – if consortia are allowed – requiring (a mix of) joint and several liability, performance bonds, maintenance guarantees and/or parent company guarantees may be necessary.

13.2.3 *Due diligence*

In a project financing, there are usually several parties carrying out due diligence on the PPP Project from the private sector side: the Private Partner, its Sponsors and the lenders, as well as all their advisers. As mentioned in [Section E, PPP Contracts in Context](#), the lenders go through a rigorous process to satisfy themselves that the PPP Project is bankable and this can give the Contracting Authority additional comfort in terms of its own (and its advisers') assessment of the Private Partner's ability to successfully deliver the PPP Project. In a corporate-financed PPP Project, this level of third party due diligence may not happen, so the Contracting Authority may have to rely solely on its own (and its advisers') evaluation of the financial and technical robustness of the Private Partner, its bid and its Sub-contractors (who may or may not be part of the same corporate group).

13.2.4 *Creditworthiness of counterparty*

A project-financed PPP Project necessarily involves an SPV which is Party to carefully structured sub-contract arrangements and financing involving third party lenders, sponsor equity and guarantees or similar support at requisite levels (e.g. of equity or Sub-contractor obligations). The SPV's income and expenditure are relatively transparent and its financial robustness assessable.

In a corporate-financed PPP Project, this level of transparency may not be automatically present where the financing and sub-contracting arrangements are being kept within the relevant corporate group and no third party funding is involved. The Contracting Authority needs to be able to satisfy itself that its Private Partner in this scenario is at least as financially robust as it would be expected in a project financing (which would be largely ring-fenced from external factors).

As described in [Section 13.2.2](#), at the bid stage, the Contracting Authority will need to consider what comfort it requires from the bidder to show that the relevant corporate funding will be forthcoming as there will be no third party lenders to provide the type of commitment letter typically required in a project-financed bid. If the Private Partner is not demonstrably creditworthy in its own right (e.g. with a satisfactory credit rating), the Contracting Authority may need to request specific information about the proposed financing and/or require a form of guarantee or commitment letter from a creditworthy company in the corporate group (typically a parent company as its credit rating/financial standing will be the determining factor), or from a third party Sub-contractor or key supplier. If the bidder is a consortium, the Contracting Authority will want the consortium members (or appropriate parent companies) to take on joint and several liability under any credit support (this may be a requirement rather than an option in a public procurement process where entities have formed a consortium to meet minimum financial standing requirements).

13.2.5 *Price fluctuation between preferred bidder and financial close*

Unlike in a project financing, a corporate-financed bid may be able to offer a fixed price bid (without variation for funding costs, as its costs of funding will not be as directly affected by interest rates that may move between bid and financial close as in a bank financing, or by the price fluctuation risk in a bond financing). This certainty may be of particular value to the Contracting Authority, depending on the PPP Project circumstances, and encouraging bidders that are raising third party debt to pre-hedge may not be feasible.

13.2.6 Transparency

[Section 13.2.4](#) highlights that there may be less transparency regarding price and cost in a corporate financed bid where the sub-contracting and financing elements are kept within the corporate group. For example, group overhead costs and return on intra-group loans may be factored into the price in a way which would not be possible in a project financing and the true level of equity return may not be easily ascertainable. The Contracting Authority should try to obtain a level of transparency equivalent to a project-financed bid and in doing so should require a financial model as part of the bid submission so that it has sufficient information to understand the bidder's proposed flow of funds and capital structure.

The same applies during the life of the PPP Project. The Contracting Authority will want to ensure that it is able to obtain the same level of financial and technical information that it would expect in a project financing, particularly where relevant to its own liability under the PPP Contract.

As mentioned in [Section 10, Confidentiality, Disclosure and Transparency](#), governments in many jurisdictions are increasingly moving towards greater transparency in relation to public procurement and the use of public funds and this is also a factor in accessing support from multi-lateral agencies. It may therefore also be important from a policy perspective for the Contracting Authority to ensure that a sufficient level of detail is obtainable.

13.2.7 Addressing poor performance

The Contracting Authority should bear in mind that in a corporate-financed structure involving only one sponsor group, poor performance may not realistically be able to be addressed in the same way as it can be in a structure where more than one corporate group is involved, as well as possibly third party lenders. There will be a different dynamic without parties who would insist on contractual arrangements being put in place to enable a poorly performing Sub-contractor (and/or Private Partner) to be replaced before the PPP Contract is terminated (e.g. as would be the case in a typical project financing). Similarly, Direct Agreements with Sub-contractors are unlikely to be of much benefit if the whole PPP Contract is essentially being delivered by one corporate group and failure to perform is likely to be indicative of a systemic failure within the group as a whole.

As there are no third party lenders, there will be no Direct Agreement either ([see Section 7, Lenders' Step-in Rights](#)). While this means the Contracting Authority has fewer constraints on its ability to terminate the PPP Contract in default circumstances, the lack of third party lender involvement removes one line of defense to rescue a PPP Project in trouble.

The Contracting Authority should consider what alternative protection to seek in these circumstances – e.g. requiring certain guarantees or payment retention rights, direct rights against key suppliers or rights to appoint third parties to remedy defaults at the cost and risk of the Private Partner.

13.2.8 Flexibility

A corporate-financed Private Partner may have greater flexibility when it comes to agreeing significant changes to the scope of work/services under the PPP Contract if it does not have to involve third party lenders in the process.

13.2.9 Changes to documentation

If a PPP Project is being corporate-financed and there is no prospect of a refinancing/ introduction of senior debt post commencement, then logically various adjustments should be made to the PPP Contract terms to reflect the structure, parties and documentation involved. These will include:

- (a) References and provisions relating to financing documents (e.g. Senior Financing Documents) – there will not be Senior Finance Documents as in a project financing context. Advice will be needed as to the extent that relevant definitions and provisions should be adapted to take into account the corporate finance structure and any credit support required (such as parent guarantees). Some of these are explored further below.
- (b) References and provisions relating to relevant parties – e.g. there will not be any third party lenders.
- (c) Pricing adjustment provisions – PPP Contracts typically provide for an adjustment to pricing in certain circumstances (e.g. to cover the cost of implementing a qualifying change in law or the cost of certain delay events which are not the Private Partner's fault). In a project financing, the adjustment may be measured by reference to restoring senior debt cover ratios or Equity IRR. As there is no senior debt, this will need to be adapted (e.g. by providing for a lump sum payment(s) or using other criteria as a reference instead).
- (d) Insurance provisions – in a corporate financing, insurance cover may be provided via corporate group policy arrangements as opposed to by project-specific policies. This may feed through to a cheaper bid price but will also mean that the type of insurance provisions typically seen in a project-financed project may need adapting as the policies and premia will not necessarily be project-specific nor the terms as transparent. Advice will be needed to ensure the Contracting Authority has equivalent (or satisfactory) protection in terms of uninsurability, placing of insurances, size of deductibles, indemnity cover, endorsements, notice of policy changes, loss payee provisions and premium risk sharing. In addition, as there are no third party lenders, there should be no need to have a threshold above which insurance proceeds are applied against debt as opposed to reinstatement of the PPP Project.
- (e) Refinancing – these provisions should be tailored appropriately to reflect the fact that there will not be any third party financing (or none being planned) but also to cater for a possible future change in financing which should require Contracting Authority consent and which may give rise to a form of refinancing gain (e.g. from a corporate financing to a project financing). If this is envisaged at Financial Close then relevant amendments should be agreed as a schedule to the PPP Contract – if not, the changes and the sharing of the refinancing gain will need to be negotiated as part of the Contracting Authority consent process.
- (f) Termination payments – in a corporate-financed PPP Project with no third party debt the funding is being provided by the parent group and is in principle equity. However, it is likely that the principles relating to compensation set out in [Section 8, Termination Payments](#) will still need to apply in order for the parent group to be prepared to commit the level of funding required for the PPP Project. Appropriate adjustment to the calculation formulae will be required to reflect that there is no Senior Debt but instead just equity. [See Section 13.3.](#)

As mentioned in [Section 13.2.7](#), there is no need for a Direct Agreement if there are no third party lenders. The Contracting Authority should consider whether any alternative step-in/direct agreement-type contracts with other parties/parent companies might be appropriate in the proposed structure, including in relation to ensuring oversight of corporate documentation and any joint and several arrangements.

13.3 TERMINATION PAYMENT CALCULATION

13.3.1 Contracting Authority default, MAGA, change in law or voluntary termination

Following the market practice described in [Section 8.3.1, Termination Payments](#), in a corporate financing the Private Partner is still likely to expect full compensation if the PPP Contract is terminated early for Contracting Authority default, MAGA, change in law or voluntary termination. A form of financing-based compensation approach as described in [Section 8.3.3](#) (consisting of senior debt plus equity plus third party cost elements) can be adopted, but will need to take into account that there is no senior debt. Options are set out below.

- (a) As the equity element represents the full PPP Contract funding, if the Private Partner's sole business is the PPP Project, it is possible to choose any of the three Options described in [Section 8.3.3.2](#) in place of the senior debt plus equity element. Third party costs (e.g. redundancy and sub-contracting break costs) should be added as described in [Section 8.3.3.3](#).
- (b) If the PPP Project is not the Private Partner's sole business, the Options in [Section 8.3.3.2](#) will not be appropriate and one approach is to use the value of the PPP Contract as the basis for compensation – i.e. the amount which the PPP Contract could be sold on the open market (assuming no termination). Again, third party costs should be added. This reflects the approach described in [Section 8.4.2\(b\)](#).
- (c) An alternative to (b) is to base compensation on the net present value of future payments which would have been due under the PPP Contract from the termination date, less future operating costs and capital expenditure (in each case as shown in the Original Base Case and discounted at the pre-tax Base Case Project IRR). Third party costs should again be added.

Approaches which are based on a market value may prove hard to implement in practice on the basis that a market is unlikely to exist in some of these termination circumstances, particularly in an Emerging Market with a limited market anyway. An estimated value may have to be used instead.

In a corporate financing, the Private Partner may be able to more effectively mitigate costs to the Contracting Authority, particularly on a voluntary termination, in a way which proves less expensive to the Contracting Authority than in a project financing. One reason for this is that, with reasonable notice, resources and investment may be capable of being redeployed in other areas around the group on termination, reducing break costs.

With any of these scenarios, the Contracting Authority will want to ensure that termination fees under any Sub-contracts are not so disproportionate as to result in excessive compensation of intra-group companies who are Sub-contractors.

13.3.2 Private Partner default termination

In a Private Partner default termination, the debt-based option mentioned in [Section 8.4.2\(a\)](#) will not be applicable as there is no senior debt. The appropriate method of calculating any termination payment should be determined on a case-by-case basis and will depend entirely on the particular circumstances of the PPP Project and the nature and source of the corporate funding. Possible alternatives include:

- (a) basing compensation on the market value of the PPP Contract if re-tendered, as highlighted in [Section 8.4.2\(b\)](#) and [Section 13.3.1\(b\)](#). As bidders may want to bid on a project-financed basis, the PPP Contract drafting should allow for this. As stated above, the market value approach is uncommon generally and more difficult to implement in Emerging Markets and therefore careful consideration should be given to the justification for using this approach;
- (b) using the related and more feasible alternative to (a) of estimated market value as described in [Section 8.4.2\(b\)](#). However, again, such approach may be difficult in Emerging Markets, and the Contracting Authority may need to consider agreeing a “top up” or baseline amount;
- (c) following a similar approach to Force Majeure ([see Section 13.3.3](#)) and calculating capital and operating expenditure up to the termination date (as shown in the Original Base Case), subtracting payments up to that date and adding some element of third party costs; or
- (d) basing compensation on the equity investment cost, e.g. if financed by intercompany loans by reference to the coupons on those loans.

In any event, Contracting Authorities should bear in mind the principles set out in [Section 8.4.1](#), particularly in respect of unjust enrichment.

13.3.3 Force Majeure termination

On a Force Majeure termination, any compensation will again need to reflect that there is no senior debt. This can be done by calculating capital and operating expenditure up to the termination date (as shown in the Original Base Case), subtracting payments up to that date, and adding third party costs. As in any type of financing, the Contracting Authority will want to ensure that termination fees under Sub-contracts are proportionate to avoid disproportionate compensation of intra-group companies acting as Sub-contractors.

A

APPENDIX



ADDITIONAL PPP RESOURCES

Public-Private Partnership Legal Resource Center

<https://ppp.worldbank.org/public-private-partnership/>

Procuring Infrastructure Public-Private Partnerships 2018

<https://ppp.worldbank.org/public-private-partnership/library/procuring-infrastructure-ppps-2018>

PPP Reference Guide Version 3.0

<https://ppp.worldbank.org/public-private-partnership/library/ppp-reference-guide-3-0>

PPP Knowledge Lab

<https://pppknowledgelab.org/>

Tools to assess whether to implement a project as PPP

<https://pppknowledgelab.org/tools/tools-assess-whether-implement-project-ppp>

Benchmarking PPP Procurement 2017

https://library.pppknowledgelab.org/documents/3889?otp=b3RwIzE1NTgoMjAxODc=&ref_site=ppiaf

Mobilizing Islamic Finance for Infrastructure Public-Private Partnerships (Joint World Bank Group and Islamic Development Bank Report 2017)

https://ppiaf.org/documents/5369?ref_site=kl

Public-Private Partnerships Fiscal Risk Assessment Tool (April 2016)

<https://www.github.org/resources/publications/ppp-fiscal-risk-assessment-model-pfram/>

Public-Private Partnerships Fiscal Risk Assessment Model User Guide (April 2016)

<http://pubdocs.worldbank.org/en/422531461874706371/PFRAM20160401-Guidance-Note-for-PFRAM-March-28-2016.pdf>

Resilient Infrastructure Public-private Partnerships (PPPs): Contract and Procurement – The Case of Japan (World Bank, 2017)

<https://ppiaf.org/documents/5427/download?otp=b3RwIzE1NjA3NzkyMzI=>

Resilient Infrastructure Public-private Partnerships (PPPs): Contract and Procurement – The Case of India (World Bank, 2018)

<http://pubdocs.worldbank.org/en/230011532671561538/India-PPP-Country-Brief-drmhubtokyo.pdf>

A Framework for Disclosure in Public-Private Partnerships, World Bank 2016

<http://pubdocs.worldbank.org/en/143671469558797229/FrameworkPPPDisclosure-071416.pdf>

Disclosure in Public-Private Partnerships: Jurisdictional Studies (World Bank, 2015)

<http://pubdocs.worldbank.org/en/910311448299077946/Disclosure-in-PPPs-Jurisdictional-Studies.pdf>

Disclosure in Public-Private Partnerships: Good Practice Cases, World Bank 2015.
<http://pubdocs.worldbank.org/en/610581448292161621/Disclosure-in-PPPs.pdf>

Equator Principles
<https://equator-principles.com/>

IFC's Environmental and Social Performance Standards
https://www.ifc.org/wps/wcm/connect/Topics_Ext_Content/IFC_External_Corporate_Site/Sustainability-At-IFC/Policies-Standards/Performance-Standards

European PPP Expertise Centre Library
<http://www.eib.org/epec/index>

Global Infrastructure Hub: PPP Risk Allocation Tool 2019 Edition
<https://ppp-risk.gihub.org/>

Infra Australia PPP Guidelines
<https://infrastructure.gov.au/infrastructure/ngpd/files/Volume-3-Commercial-Principles-for-Social-Infrastructure-Dec-2008-FA.pdf>
<https://infrastructure.gov.au/infrastructure/ngpd/files/Volume-7-Commercial-Principles-for-Economic-Infrastructure-Feb-2011-FA.pdf>

Partnerships Victoria PPP Policy, Guidance and Templates
<https://www.dtf.vic.gov.au/public-private-partnerships/policy-guidelines-and-templates>

South Africa PPP Guidelines
<https://www.gtac.gov.za/Publications/1280-Standardized-Public-Private-Partnership-Provisions.pdf>

UK PF2 Guidance
https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/207383/infrastructure_standardisation_of_contracts_051212.PDF

UK Private Finance 2 (and related materials)
<https://www.gov.uk/government/publications/private-finance-2-pf2>

Dutch Model (DBFM infrastructure and DBFMO accommodation)
<https://www.rijksoverheid.nl/onderwerpen/publiek-private-samenwerking-pps-bij-het-rijk/documenten/richtlijnen/2016/06/01/dfbm-overeenkomst-rijkswaterstaat>
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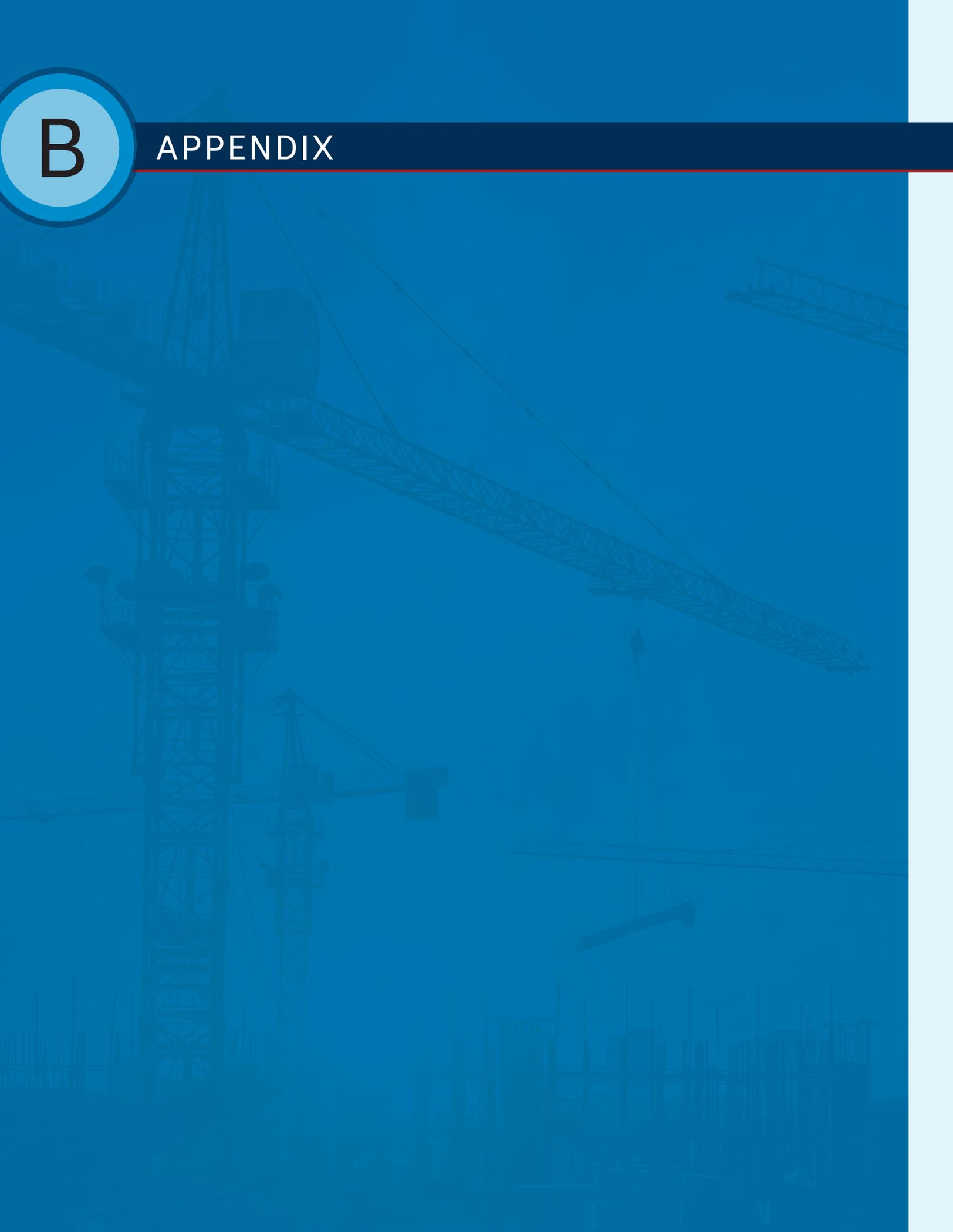
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B

APPENDIX



EXAMPLE LIST OF STANDARD CONTRACTUAL PROVISIONS IN A PPP CONTRACT

PART A: PRELIMINARY

1. Interpretation
2. Execution and Delivery of Documents
3. Commencement and Duration
4. Project Documents
5. The Project Operations

PART B: GENERAL PROVISIONS

6. General Obligations and Responsibilities of the Private Partner
7. Warranties
8. Indemnities and Liability
9. Limits on Liability
10. Contracting Authority's Data
11. Representatives
12. Liaison
13. Disaster Plan

PART C: LAND ISSUES

14. Nature of Land Interests
15. The Site
16. Consents and Planning Approval

PART D: DESIGN AND CONSTRUCTION

17. The Design, Construction and Commissioning Process
18. Right of Access of the Contracting Authority's Representative
19. Program and Dates for Completion
20. Independent Tester
21. Equipment
22. Pre-Completion Commissioning and Completion
23. Post Completion Commissioning

PART E: QUALITY ASSURANCE

- 24. Quality Assurance

PART F: INFORMATION TECHNOLOGY

- 25. Information Technology

PART G: SERVICES

- 26. The Services
- 27. Maintenance
- 28. Monitoring of Performance
- 29. Employment Matters
- 30. Site Security and Personnel Issues
- 31. Stocks, Consumables, Materials and Equipment

PART H: PAYMENT AND FINANCIAL MATTERS

- 32. Payment
- 33. Insurance
- 34. Custody of Financial Model
- 35. Information and Audit Access

PART I: CHANGES IN LAW AND VARIATIONS

- 36. Changes in Law (*see Section 3 Change in Law*)
- 37. Variation Procedure

PART J: DELAY EVENTS, RELIEF EVENTS AND Force Majeure

- 38. Delay Events
- 39. Relief Events
- 40. Force Majeure (*see Section 1 Force Majeure*)

PART K: TERMINATION (*See Sections 6 Termination Events, 8 Termination Payments, 9 Handback of Assets at End of the Contract.*)

- 41. Private Partner Events of Default and Termination
- 42. Contracting Authority Events of Default and Termination
- 43. Non-Default Termination [Voluntary, Force Majeure, Uninsurability etc]
- 44. Effect of Termination
- 45. Compensation on Termination (*see Section 8 Termination Payments*)
- 46. Handback Procedure (*see Section 9 Handback of Assets at End of the Contract*)

PART L: MISCELLANEOUS

47. Assignment, Sub-Contracting and Changes in Control
48. Intellectual Property
49. Confidentiality and Transparency (*see Section 10 Confidentiality, Disclosure and Transparency*)
50. Taxation
51. Bribery, Corruption and Payments (*see Section 6 Termination Events*)
52. Records and Reports
53. Dispute Resolution Procedure (*see Section 11 Governing Law and Dispute Resolution*)
54. Notices
55. Amendments
56. Waiver
67. No Agency
58. Entire Agreement
59. Conflicts of Agreements
60. Severability
61. Counterparts
62. Costs and Expenses
63. Mitigation
64. Governing Law and Jurisdiction (*see Section 11 Governing Law and Dispute Resolution*)
65. Further Assurance

SCHEDULES

Schedule 1	Definitions and Interpretation
Schedule 2	Completion Documents
Schedule 3	Custody Agreement
Schedule 4	Key Works Personnel
Schedule 5	Disaster Plan
Schedule 6	Lenders' Direct Agreement (<i>see Section 7 Lenders Step-in rights</i>)
Schedule 7	Land Matters
Schedule 8	Construction Matters
Schedule 9	The Program
Schedule 10	Review Procedure
Schedule 11	Collateral Agreements
Schedule 12	Outline Commissioning Program
Schedule 13	Equipment
Schedule 14	Service Requirements
Schedule 15	Independent Tester Contract
Schedule 16	Payment Mechanism
Schedule 17	Financial Model
Schedule 18	Insurance
Schedule 19	Variation Procedure
Schedule 20	Compensation on Termination (<i>see Section 8 Termination Payments</i>)
Schedule 21	Handback Procedure (<i>See Section 9 Handback of Assets at End of Contract</i>)
Schedule 22	Record Provisions
Schedule 23	Dispute Resolution Procedure (<i>see Section 11 Governing Law and Dispute Resolution</i>)
Schedule 24	Contracting Authority Information
Schedule 25	Refinancing (<i>see Section 5 Refinancing</i>)
Schedule 26	Employee Information

