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Project Finance 2017

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USA

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1 Overview

1.1 What are the main trends/significant developments in the project finance market in your jurisdiction?

As with any transition to a new administration, there will be uncertainty as to priorities and policy direction. Transitions involving a change in political party bring an extra degree of uncertainty, and a transition to an administration headed by a President with no previous government experience brings a quantum jump in uncertainty. It is still too early to discern the full impact of the new administration's policies on the energy, electric power and infrastructure sector; however, some general outlines have emerged. President Donald Trump is expected to prioritise the scaling back of environmental regulations that particularly affect the energy and electric power sectors. Notably, most industry observers predict the demise of the far-reaching Clean Power Plan, the Environmental Protection Agency rule announced during the Obama administration, designed to reduce carbon pollution from power plants. There is also substantial uncertainty as to whether the United States under President Trump will withdraw from the Paris Climate Agreement. Beyond reducing environmental regulation, the new administration is widely expected to actively promote traditional fossil fuels by opening more government-controlled land to exploration and production and expediting government approvals for energy exports and energy projects that require Federal approvals.

Such new policies may be capable of increasing energy supplies; however, many experts believe that the limiting factors are more closely associated with the demand side. Energy Information Administration ("EIA") data show the total generation of electric power in the U.S. reached a peak in 2007 at around 4,156.7 Terawatt-hours ("TWh") and never again approached this level. Given the stagnation of electric demand (partially due to the proliferation of distributed generation (e.g. rooftop solar)), the competition among primary energy sources for market share has become intense.

I. Declining Market Share for Coal and Nuclear

The year 2007 also marked the highest amount of U.S. electricity derived from coal, at 2,015 TWh. The most recent figures (still incomplete for 2016) show total U.S. generation of electricity from coal at 1,211 TWh (rolling 12 months, ending in October, 2016); a decline of 40%. Competition from inexpensive natural gas, increasingly sourced from shale, is responsible for most of coal's lost market share. In the year that coal reached its peak, electricity generated from natural gas totalled 896.6 TWh. The most recent figure is 1,401.9 TWh, representing an increase of 56%. Electric power derived from renewables is also a factor in the decline of coal-fired market share. Wind energy contributed 5.5% of total U.S. electric energy, at 223.9 TWh (rolling 12 months, ending in October, 2016) and is expected to continue growing. Solar electric production from utility-scale facilities (1 MW and larger) is approaching 1% of total U.S. output, and exceeds that level, at 53.4 TWh (if estimated generation from distributed solar facilities are included).

President Trump has stated his desire to encourage domestic production of fossil fuels and reduce the regulatory burdens on the energy sector. Skeptics have noted that removing barriers for shale gas production will only contribute to the decline of the domestic coal industry, as these two fuels compete directly for power generation. The ability of the new administration to increase gas and coal production simultaneously would appear to require either an increase in export markets, an increase in total domestic demand, or both. Export markets for U.S. coal are currently under pressure from such diverse factors as slow global economic growth, environmental concerns and regulations in host nations, competition with other energy sources and the strength of the U.S. dollar. On balance, it appears doubtful that U.S. production of both gas and coal can be increased, absent a large boost in domestic economic growth. Most experts are expecting some increase in U.S. GDP, but not in the range of what has been proposed by the President. The outlook for gas appears to be for continued growth in supplies and exports as newly constructed liquefied natural gas ("LNG") export terminals are completed and (perhaps) a modest increase in prices. The outlook for coal appears to be, at best, a degree of stabilisation of market share.

Along with coal-fired electric plants, nuclear power has also been stressed by flat demand and competition from inexpensive gas and renewable energy. The U.S. currently has 100 operating nuclear power plants, down from 104 a few years ago. Four nuclear units are currently under construction at two sites in southern states, but several others have been scheduled for shut-down. Nuclear operating costs have been increasing, partly as a function of the aging of the nuclear fleet and also from increased safety regulations implemented after the Fukushima Daiichi accident. In both California and New York, where large nuclear plants have been proposed for shut-down (e.g. the Indian Point Nuclear Power Plant in New York), the thinking on replacement energy (still unofficial as of this time) seems to be focusing on more renewables (solar in California and offshore wind in New York), strengthening the transmission grid (for imports of wind power into California and imports of Canadian hydroelectric power into New York), demand-side management and innovations such as battery energy-storage facilities. Expanded reliance on gas does not seem to be favoured. New York and Illinois have attempted to bolster nuclear generation by instituting zero-emissions credits to nuclear assets. In response, non-utility generators are pressing the Federal Energy Regulatory Commission ("FERC") to overturn

these state subsidies that the generators claim distort FERC's wholesale electricity markets. Overall, we expect nuclear power to decline slightly, as the limited number of new plants will not quite compensate for planned closures. The "nuclear renaissance" of the prior decade today seems like science fiction.

II. Prospects for the Oil and Gas Industry

While global oil prices rebounded sharply last year (to approximately $53 per barrel in December 2016), prices remain low in comparison to historical levels (and the levels necessary to support the oil-dependent economies of many petroleum-exporting nations (e.g. Russia, Venezuela and Nigeria). In the U.S., excess supplies of crude oil persist due to U.S. shale oil production remaining at near record levels. U.S. producers have cut costs and improved production efficiencies with advanced drilling and hydraulic fracturing technologies. New policies of the Trump administration, including expanded leasing of Federal land for exploration and production, will likely have the effect of increasing domestic production and further depressing prices in the absence of significant growth in demand. While oil prices may be boosted by OPEC's proposed production cuts, U.S. shale producers and other non-OPEC producers may not follow OPEC's lead. Notably, the U.S. demand for gasoline has not responded significantly to the substantial price declines of the past few years.

The impact of the price decline and falling demand continued to ripple through the entire energy value chain and highly-leveraged exploration and production companies were hit hardest as they faced difficulty satisfying their debt payment obligations. Hedges became expensive to renew. U.S. banks heavily exposed to the oil and gas industry (e.g. Wells Fargo in 2015 derived 15% of its investment banking fee revenue from the oil and gas industry and Citigroup in 2015 derived 12% from the same according to industry statistics) and finding that the value of their collateral had sunk, nevertheless, seem poised to weather the downturn. U.S. banks reacted quickly by increasing loan loss reserves, renegotiating borrowing base determinations and consenting to extensions and amendments of existing credit facilities. It should also be noted that banks with a large consumer banking business should benefit from falling prices as consumers find themselves with more disposable cash to obtain mortgages and open credit cards.

III. The U.S. as a Net Natural Gas Exporter

According to the EIA, as of November 2016, the U.S. became a net exporter of natural gas on a monthly basis for the first time since 1957. Natural gas storage inventories were at or near record levels throughout most of the year due to continued strong production and reduced demand arising in part from mild winter weather at the start of 2016. We expect to see increasing exports of U.S. crude, natural gas/LNG, ethane, propane and refined products as the U.S. markets remain largely oversupplied.

While U.S. LNG exports increased from almost zero in 2015 to an average of 0.5 billion cubic feet per day ("Bcf/d") in 2016 – largely due to the commercial operation of Cheniere's Sabine Pass LNG liquefaction plant in Louisiana – export markets for U.S. LNG face competition from other LNG sources (notably Australia), the strength of the U.S. dollar and economic pressure from low oil prices, which form the basis of LNG prices in Asian markets. However, EIA forecasts LNG exports to average 2.6 Bcf/d in 2018, driven by the Cove Point LNG export terminal in Maryland, which is expected to come online in December 2017, and the Cameron LNG and Freeport LNG terminals on the Gulf Coast, which are each expected to come online in the second half of 2018.

Pipeline exports of gas to Mexico have been booming, as a number of new gas pipelines have come online. With domestic natural gas production at an all-time high and oil prices remaining low, 2016 saw much activity around pipeline infrastructure to move natural gas from production centres to consuming markets or export terminals. U.S. pipeline exports to Mexico continued to grow throughout 2016, comprising 87% of all U.S. natural gas exports. A number of new gas pipeline projects to Mexico reached financial close last year, including the Fermaca La Laguna–Aguascalientes, Fermaca Villa de Reyes–Aguascalientes–Guadalajara Gas, Nueva Era and Samalayuca–Sasabe pipelines. However, the outlook for expanded gas exports to Mexico could be jeopardised by the recent sharp drop of the Mexican peso and also by political friction between the Trump administration and the Mexican Federal government.

Given that the new administration has indicated a decidedly different view from the Obama administration regarding pipeline infrastructure development, including over the Dakota Access Pipeline and the Keystone XL Pipeline, some suggest that the new administration, with Republican control over Congress, has the potential to change course radically to unclog projects and accelerate energy and infrastructure development (e.g. the Executive Order issued on January 24, 2017 and the Presidential Memoranda issued on January 24, 2017). We should note, however, that oil pipelines are largely under state jurisdiction, and while interstate gas pipelines are under FERC jurisdiction, FERC is an independent Federal regulatory commission that follows existing precedents established by the courts in performing its environmental reviews of proposed gas pipeline projects.

IV. Regional Electricity Markets

The combination of depressed demand, particularly due to warmer-than-normal winter temperatures, large amounts of natural gas in storage and low natural gas prices has driven down regional spot electric energy prices and placed stress on capacity prices, as generation project developers have come to rely more on capacity revenues needed to support project financing. While, typically, summer weather drives electric power demand, which should translate into higher power prices, this was generally not the case for regional energy markets in 2016. Platts reported that peak demand in the Electric Reliability Council of Texas ("ERCOT") hit record levels several times during August 2016. ERCOT North Hub day-ahead on-peak power prices in August 2016 averaged roughly $50.25 per megawatt hour ("MWh"), 15% below where day-ahead prices averaged in August 2015. On August 11, 2016, the ERCOT electric load peaked above 71 gigawatts ("GW"), a new record. However, on August 11, 2016, peak power prices only averaged near mid-$40s/MWh. According to Platts, ERCOT had not issued any conservation notices or warnings about low physical responsive capability. Similarly, on July 21, 2016, the Midcontinent Independent System Operator ("MISO") experienced a generation shortage event. However, MISO power prices that day peaked lower than anticipated (approximately mid-$30s/MWh). In respect of ERCOT, some industry observers attribute strong wind output on the system as helping to reduce price spikes which typically coincided with periods of peak demand.

V. Continuing Shift in Project Finance Activity Towards Renewables, Transport and Gas-fired Power Projects

As part of this cycle, we are witnessing a greater shift in project finance activity towards renewables, transport and gas-fired power projects – a trend that we expect to persist throughout 2017. Especially notable in 2016 was the growing significance of hybrid structures in financing large-scale energy and infrastructure projects. Partially as a result of the financial crisis in 2008, which led to U.S. banks facing stiffer banking regulations, project finance sponsors have increasingly turned to the institutional private placement market for their financing needs and, since then, we have seen a growing appetite from institutional investors (particularly insurance companies and pension funds) in infrastructure and project financings. Notable bank/bond hybrid financings in 2016 include the approximately $1 billion financing of the gas-fired Lackawanna

Energy Center in Jessup, Pennsylvania, the approximately $230 million financing for the 150 MW nameplate capacity Alta Wind VIII power project in the Tehachapi/Mojave area of Kern County, California and the approximately $250 million financing for the Argo Black Hills Energy Project in Pueblo, Colorado.

a. Continued Growth for the Renewables Sector

According to recent EIA statistics (relying on planned capacity additions for the last two months of 2016), approximately 63% of utility-scale capacity additions in 2016 were renewables technologies – almost exclusively wind and solar – and a continuation of the trend over the prior two years in which renewables accounted for more than half of added electrical capacity. Despite the new administration's professed focus on conventional power generation technologies and fossil fuels, renewable energy has garnered economic momentum and bipartisan support. A number of states, including California, New York, Oregon and Washington, DC, have expanded mandates for renewable electric generation to reach 50% of each state's total electricity generation. After years of technological improvements leading to the dramatic decline in capital costs and favourable regulatory policy, the renewables sector has demonstrated that it has passed its adolescence to the point that it can sufficiently sustain itself. We expect this trend to continue despite predictions that the new administration might seek to accelerate the scheduled phase-out of tax incentives for renewable energy development.

The first offshore wind project in the U.S. (Deepwater Block Island) reached commercial operation by the end of 2016. Although this project is only 30 MW, it represents a breakthrough in project development. Additional offshore wind projects are planned, especially off the coast of Massachusetts and New York. In a related development, Statoil was declared the provisional winner of the Bureau of Ocean Energy Management ("BOEM") offshore wind energy area lease sale auction for a site off the coast of Long Island, New York. While offshore wind is still significantly more expensive than other U.S. electricity sources, it is still seen as economically viable in places like Block Island (in the state of Rhode Island), where residents were previously reliant on diesel generators or near markets where electricity prices are high.

In 2016, we witnessed a wide-scale restructuring of the solar industry as the industry faced headwinds from declining oil and gas prices, coupled with weak demand. Abengoa, SunEdison, First Solar and SunPower each either announced bankruptcies or restructuring plans in 2016. These companies were typically highly-leveraged in order to undertake ambitious expansion programmes to acquire companies and develop large project portfolios. As a result, we anticipate that there could be distressed sales of these companies' solar and wind farm assets over the next year. One example is the acquisition last year by J.P. Morgan Asset Management from SunEdison and its affiliates of interests in 29 utility-scale wind and solar projects totalling approximately 1.2 GW.

Nevertheless, 2016 remained a strong year for wind and solar, with a number of projects reaching financial close last year, including the 276 MW Bethel Wind Farm in Castro County, Texas, the Broadview Wind Project in Curry County, New Mexico and Deaf Smith County, Texas, the 230 MW Electra Wind Project in Haskel County, Texas, the 230 MW Mariah North Wind Project in northern Texas and the 45 MW Sandstone Solar Plant in Arizona.

The renewables industry could face headwinds from the President's proposed tax reforms. Even if the wind energy production tax credits and the solar energy investment tax credits are left untouched, one potential consequence of the new administration's tax reform proposals is that corporate tax rates are expected to decline significantly from 35% to perhaps a range of 15% to 20%. This reduction in corporate tax rates will have the effect of reducing the size of the tax equity component of many renewable energy financings and may require that these transactions increase reliance on debt financing rather than tax equity. In certain instances, where deals have been structured under assumptions agreed prior to the implementation of the said tax reforms, there may be adverse economic impacts on project developers and/or certain construction lenders that expected to be repaid from the proceeds of tax equity investments that may now be downsized. Reducing corporate tax rates may lead to fewer active tax equity investors in renewables financings, as corporations will have significantly lower effective tax rates and many may conclude that further efforts to reduce taxes may not be worth the effort. Nevertheless, we anticipate that the renewables sector will adapt quickly to such tax proposals and develop new financing structures that will support the industry's substantial capital requirements.

b. Prospects for Infrastructure Investment and Privatisation

Many analysts suggest that the Trump administration's stated goals of undertaking infrastructure investment, coercing American manufacturing jobs back to the United States and attempting to jumpstart U.S. manufacturing will lead to increased domestic GDP growth, although the scope for such growth will be limited by structural factors, including an aging population and low growth in productivity. To the extent that domestic GDP can be increased, the correlation (weakened of late, but not eliminated) between aggregate energy demand and GDP may be expected to stimulate domestic energy demand. The magnitude of this demand-side stimulus is subject to great uncertainty.

The new administration released plans to embark on a massive infrastructure building and revitalisation programme. To the extent these plans can be realised, we expect a greater role for state and private sector participation, public-private partnerships and related arrangements. Discussions to date have proposed approximately $137 billion in tax credits to private investors for projects that generate revenue, such as toll roads, toll bridges and airports. Under this preliminary plan, investors would receive a substantial tax credit as an inducement for equity investment in infrastructure projects. The new administration has suggested that conventional municipal financing would be available for projects that lack a revenue stream, but the details are less clear. As with any tax proposal, the Trump administration's plans will have to withstand the Congressional budget process. Deficit hawks from the President's own political party may be expected to oppose any large increase in spending (tax credits are viewed as spending), and members of the opposition party may oppose programmes that appear to offer the prospect of corporate profits and Wall Street financial engineering. Additionally, tax credit proposals may become tied up in a larger debate about reform of the U.S. tax code – another stated goal of the new administration. On the whole, we reasonably expect a significant increase in infrastructure investment. That said, we expect the majority of such investment to be targeted at the transportation sector rather than the energy sector, which in the U.S. is largely privately owned. Some have also expressed concerns that decisions on transportation sector spending are too often driven by political considerations rather than solid economic analysis. The effect of transportation infrastructure spending on GDP growth is subject to considerable uncertainty. Even so, an increase in domestic steel and cement consumption, with a related boost in metallurgical coal production, is possible.

The new administration's plans for streamlining regulations and for privatisation of government-owned infrastructure assets are certain to face opposition from Congressional Democrats. But the President may find opposition within his own party for some proposals. The electricity transmission system in the U.S. is an excellent example. The U.S. transmission network is fragmented, consisting of three largely separate power grids, with key parts of the system owned by private companies, but other parts owned by Federal, state and local

governmental authorities, and some parts owned by diverse entities such as state irrigation districts and cooperative utilities. Parts of the system are overseen by seven independent system operators/ regional transmission organisations, but these do not encompass the entire country. FERC has authority over economic regulation of the power grid (with certain notable exceptions) and state-level regulatory commissions have authority over siting and construction of transmission lines. The respective authority of FERC and the state commissions has been the subject of many court decisions over the years and new areas of dispute continue to emerge. Any proposal to change the existing system is certain to threaten vested interests. Past proposals for increased Federal authority over the siting and construction of high-voltage transmission lines have encountered stiff resistance from state authorities. Given that the Republican Party generally favours less Federal authority, any plans for building a revamped, "modern" national transmission system will likely face questions over Federal versus state jurisdiction. Privatisation of existing Federal entities (such as the Federal power marketing administrations, currently part of the Department of Energy; or the Tennessee Valley Authority, a corporate agency of the U.S. Federal government) would be even more controversial and would almost certainly face opposition from the Congressional delegations in the affected regions. To date, President Trump has not announced any specific plans for the reform of electric transmission system.

c. Continued Activity for Gas-fired Power Generation

In 2016, we saw continued project finance activity around gas-fired power generation. Notable projects include the approximately $755 million project financing of the 785MW gas-fired CPV Towantic Energy Center in Oxford, Connecticut, the approximately $1 billion financing of the gas-fired Lackawanna Energy Center in Jessup, Pennsylvania, the $725 million refinancing of the 705 MW Newark Energy Center gas-fired merchant power plant in New Jersey, the $948 million sale by Entegra of a 2,000 MW gas-fired combined cycle power plant in Arkansas and the $500 million sale of the Granite Ridge 745 MW combined-cycle natural gas-fired power plant in New Hampshire to Calpine. We expect this trend to continue, particularly in the Midwest and Great Plains regions.

VI. Physical Security and Cybersecurity of the Electric Grid and Energy Infrastructure

Concerns with both physical security and cybersecurity of critical energy infrastructure have been growing in recent years and this trend is expected to continue. In the U.S., both physical security and cybersecurity of the bulk power system are overseen by the North American Electric Reliability Corporation ("NERC"), which has been designated as the Electric Reliability Organization ("ERO") by FERC pursuant to authority under the Federal Power Act, as amended by the Energy Policy Act of 2005. Under FERC rules concerning Critical Infrastructure Protection, NERC has taken an educational and supporting approach under which entities that are registered as owners or operators of bulk power system components can choose to participate in a confidential review by NERC staff of their physical security and cybersecurity procedures as compared to industry best practices. The results are not disclosed and are not used in subsequent NERC reliability audits, unless an imminent threat is found. FERC itself maintains confidential treatment of Critical Energy Infrastructure Information ("CEII") and has in the last year adopted new rules imposing penalties for release of such information. Although the particulars of security initiatives are, by nature, not public, we understand that efforts have focused on both software security issues (such as firewalls, patches and internal monitoring), and also on human-factor vulnerabilities, such as contractor and supply chain cybersecurity measures.

Looking forward, the outlook for physical and cybersecurity initiatives for the U.S. generally as well as the energy and power sectors is particularly opaque. We note that President Trump recently appointed Rudy Giuliani as cybersecurity advisor. The President has also been vocally critical of the U.S. intelligence community in general, and its cybersecurity abilities in particular, both during the election campaign and afterwards. How this may translate into possible changes in policy or practice is unclear at the present time. But we do not see this subject being ignored under this administration; we – along with many in the American business community – are taking a "wait and see" approach with respect to the new administration's security programmes.

1.2 What are the most significant project financings that have taken place in your jurisdiction in recent years?

See question 1.1 above.

2 Security

2.1 Is it possible to give asset security by means of a general security agreement or is an agreement required in relation to each type of asset? Briefly, what is the procedure?

Several different tools are typically used to provide lenders security in the project assets, including a security agreement covering personal property of the project company.

The Uniform Commercial Code ("UCC") provides a well-developed and predictable framework for lenders to take a security interest in the borrower's personal property assets. Each U.S. state has adopted article 9 of the UCC, which governs secured transactions, with some non-uniform amendments. Under the UCC, a security agreement must, among other elements, describe the collateral and the obligations being secured in order for the lender's security interest in the collateral to attach to a borrower's personal property assets. Filing a UCC-1 describing the collateral in the appropriate filing office perfects the lender's security interest.

Perfection of rights in deposit accounts, money and letters of credit is achieved by control rather than by the filing of a UCC-1. Control in accounts is achieved by the lender (or its collateral agent) taking control of the deposit account under control and funding provisions in the security agreement or entering into an account control agreement.

Lenders usually also require a pledge of the ownership interests in the project company to give them the ability to own the project company (and all of its assets) in the event that they choose to foreclose.

2.2 Can security be taken over real property (land), plant, machinery and equipment (e.g. pipeline, whether underground or overground)? Briefly, what is the procedure?

Security may be taken over real property, subject to the real property laws of the state in which the real property is located, through a mortgage, deed of trust, leasehold mortgage or leasehold deed of trust. If under a certain state's law these instruments do not cover fixtures, a UCC-1 fixture filing may also be required.

To create a security interest in real property by mortgage or deed of trust, such instrument will: (i) identify the legal names of the lender and the borrower; (ii) state the amount of the debt owed by the borrower to the lender and identify the promissory note evidencing the indebtedness; (iii) contain a granting clause conveying the

mortgage to the lender; (iv) describe the secured property; and (v) be signed and notarised. In most states, a security interest is perfected when the instrument is recorded in the recorder's office of the county where the real property is located.

2.3 Can security be taken over receivables where the chargor is free to collect the receivables in the absence of a default and the debtors are not notified of the security? Briefly, what is the procedure?

Yes, a consent to collateral assignment by the project company to the lenders provides the lenders with the right to collect receivables under an underlying assigned agreement.

2.4 Can security be taken over cash deposited in bank accounts? Briefly, what is the procedure?

Please see question 2.1 above.

2.5 Can security be taken over shares in companies incorporated in your jurisdiction? Are the shares in certificated form? Briefly, what is the procedure?

Please see question 2.1 above.

2.6 What are the notarisation, registration, stamp duty and other fees (whether related to property value or otherwise) in relation to security over different types of assets (in particular, shares, real estate, receivables and chattels)?

Depending on the relevant state, city and county laws, recording fees and taxes for perfecting a security interest in real property will typically comprise a significant percentage of the debt obligations secured.

2.7 Do the filing, notification or registration requirements in relation to security over different types of assets involve a significant amount of time or expense?

Please see question 2.6 above.

2.8 Are any regulatory or similar consents required with respect to the creation of security over real property (land), plant, machinery and equipment (e.g. pipeline, whether underground or overground), etc.?

Requirements for regulatory consents are specific to the location and nature of the project and the identity of the project parties.

3 Security Trustee

3.1 Regardless of whether your jurisdiction recognises the concept of a "trust", will it recognise the role of a security trustee or agent and allow the security trustee or agent (rather than each lender acting separately) to enforce the security and to apply the proceeds from the security to the claims of all the lenders?

In New York law-governed security documents where there are at least two lenders, a collateral agent is nearly always appointed to act on behalf of the lenders with respect to the collateral.

3.2 If a security trust is not recognised in your jurisdiction, is an alternative mechanism available (such as a parallel debt or joint and several creditor status) to achieve the effect referred to above which would allow one party (either the security trustee or the facility agent) to enforce claims on behalf of all the lenders so that individual lenders do not need to enforce their security separately?

New York law recognises the concept of a security trust, although it is not typically used.

4 Enforcement of Security

4.1 Are there any significant restrictions which may impact the timing and value of enforcement, such as (a) a requirement for a public auction or the availability of court blocking procedures to other creditors/the company (or its trustee in bankruptcy/liquidator), or (b) (in respect of regulated assets) regulatory consents?

Regulatory approval varies greatly, as such elements are dependent on the type of collateral involved. For example, a direct or indirect change in control over electric power assets subject to the jurisdiction of FERC must be approved by FERC. FERC has jurisdiction over most sellers into wholesale electric markets and electric power transmission facilities in the contiguous U.S. states other than in the ERCOT region, which is subject to state jurisdiction. Certain small power generators known as "qualifying facilities" may qualify for exemption from FERC approval of changes in control. Moreover, if the remedies to be exercised involve direct taking of assets subject to FERC hydro-electric licensing rules, or an interstate natural gas pipeline or underground gas storage facility that holds a FERC certificate of public convenience and necessity, transfer of the licence or certificate may be required. Certain state laws and regulations may also require approvals, such as New York State, which generally parallels FERC regulations. Most states, however, require approval only if the assets are in the nature of a "traditional" public utility serving captive customers under cost-based rates or are subject to a certificate of public convenience and necessity issued under state law.

Similar considerations arise with nuclear facilities, for which the operator will hold a licence from the Nuclear Regulatory Commission ("NRC"), and any transfer of such licence that might need to accompany an enforcement action would require separate NRC approval, recognising that only the licensed operator may operate a nuclear power plant. It should be noted that foreign entities are not allowed to hold an NRC nuclear power plant operating licence or to exercise control over the licensee.

Many energy facilities include a radio communication system licensed by the Federal Communications Commission ("FCC"), and a transfer of ownership of the FCC licence related thereto will require prior approval from the FCC. In addition, there are restrictions on the grant of a security interest in an FCC licence; generally, such security interests are limited to an interest in the proceeds thereof rather than the licence itself.

Any foreclosure or enforcement action is also subject to the possible imposition of: (i) the automatic stay under the Federal bankruptcy code, title 11 of the United States Code ("Bankruptcy Code"), if the title-holder commences a case under the Bankruptcy Code; and (ii) more generally, for any non-judicial foreclosure, the obtaining of a specified injunction halting the auction or other proceeding.

4.2 Do restrictions apply to foreign investors or creditors in the event of foreclosure on the project and related companies?

See section 6 below.

5 Bankruptcy and Restructuring Proceedings

5.1 How does a bankruptcy proceeding in respect of the project company affect the ability of a project lender to enforce its rights as a secured party over the security?

Once a bankruptcy case is commenced under the Bankruptcy Code in respect of a project company, the Bankruptcy Code imposes an "automatic stay", or statutory injunction, which immediately stops all enforcement actions outside of the Bankruptcy Court against the debtor project company or its property. The automatic stay applies to secured creditors, although it is possible for a secured creditor to obtain relief from the automatic stay in certain circumstances, but only through an order of the Bankruptcy Court. In addition, in certain limited circumstances, the Bankruptcy Court may extend the automatic stay to protect entities that are not debtors in a bankruptcy case, or assets of such non-debtor entities.

A secured creditor is not, however, without protection in a case under the Bankruptcy Code. For instance, a secured creditor is generally entitled to "adequate protection" of its interest in a debtor's collateral, and there are limits on the ability of the project company to use some types of collateral, or to dispose of collateral, without the secured creditor's consent. In particular, the project company will not be permitted to use cash collateral (cash and cash equivalents) without the agreement of the secured party or an order of the Bankruptcy Court. In any sale of collateral (other than ordinary-course-of-business sales, such as sales of inventory in normal business operations) during a bankruptcy case, the secured creditor generally has the right to "credit-bid" its claim against the debtor, although that right can be limited by the Bankruptcy Court for cause. The determination of cause is fact-intensive, and in several recent cases Bankruptcy Courts have found that such cause existed, in order to facilitate an auction with active, competitive bidding. It should also be noted that in the context of a plan of reorganisation, a secured creditor cannot be compelled to accept a plan through a "cramdown" when the plan provides for the auction of the secured creditor's collateral without giving the secured creditor the right to credit-bid. But it is still possible to cramdown a secured creditor by providing it with the indubitable equivalent of its secured claim, which can include substitution of collateral.

5.2 Are there any preference periods, clawback rights or other preferential creditors' rights (e.g. tax debts, employees' claims) with respect to the security?

Generally speaking, the holder of a perfected security interest is entitled to payment from its collateral ahead of all other creditors (other than the holder of a security interest that is prior in right to it). Although particular creditors, such as taxing authorities or employees, may be entitled to priority claims under the Bankruptcy Code, such claims do not come ahead of a secured claim with regard to the collateral. Under certain circumstances, a debtor (or trustee) may surcharge collateral for the costs of preserving or disposing of it.

Under the Bankruptcy Code, the term "transfer" is broadly defined, and includes the grant or perfection of a security interest. The grant of a security interest to a lender may be "avoided", or set aside, if the security interest is unperfected. In addition, a lender's perfected security interest may be avoided as either a "preference" or a "fraudulent transfer". It is important to note that there is no requirement for there to be actual fraud or wrongdoing for a transfer to be avoided under either of these theories. A lender's security interest in a project company's property may be avoided as a preference if (i) the lender perfects the security interest during the 90 days (or one year, if the lender is an "insider" of the project company) preceding the commencement of the project company's bankruptcy case, (ii) that transfer is made for or on account of an antecedent debt owed by the project company to the lender, (iii) the transfer enables the lender to receive more than it otherwise would have received in a liquidation of the project company, and (iv) the lender has no affirmative defence (which include that the transfer was a contemporaneous exchange for new value, that the lender gave subsequent new value, or that the transfer was in the ordinary course of business) to such preference. Under the Bankruptcy Code and applicable state laws, a constructive fraudulent transfer claim can be asserted to avoid a transfer that the project company made to the lender if both (i) the project company made the transfer in exchange for less than reasonably equivalent value, and (ii) the project company at the time of the transfer was, or was thereby rendered, insolvent, inadequately capitalised, or unable to pay its debts as they matured. For this purpose, the securing or satisfaction of a present or antecedent debt of the project company will generally constitute reasonably equivalent value (although it may be an avoidable preference). Under the Bankruptcy Code, the look-back period for constructive fraudulent transfer claims is two years before the commencement of the bankruptcy case. Under state laws, the look-back period can vary, depending on the state, and can be up to six years. If a transfer is avoidable as either a preference or a fraudulent transfer, the project company may be able to cancel the security interest and force a return of the property, which may be used to pay all creditors. It should be noted that not all transfers made during the applicable look-back period are avoidable, and these inquiries are generally fact-intensive.

5.3 Are there any entities that are excluded from bankruptcy proceedings and, if so, what is the applicable legislation?

The Bankruptcy Code excludes from the category of entities that are eligible to be debtors in a bankruptcy case: governmental entities (other than municipalities); domestic insurance companies; domestic banks; foreign insurance companies engaged in such business in the U.S.; and foreign banks with a branch or agency in the U.S. In addition, the Bankruptcy Code has special provisions for particular types of eligible entities, such as railroads, municipalities, stockbrokers and commodity brokers.

5.4 Are there any processes other than court proceedings that are available to a creditor to seize the assets of the project company in an enforcement?

Outside of court proceedings, creditors may be permitted to exercise self-help remedies depending upon the nature of the collateral, provisions of the applicable security agreements, and the governing law. For example, the UCC generally authorises a secured creditor, after default, to take possession of, to collect on, and to dispose of (such as by public or private sale), personal-property collateral without first commencing a court proceeding, provided that the secured creditor complies with particular formalities and proceeds without breach of the peace.

5.5 Are there any processes other than formal insolvency proceedings that are available to a project company to achieve a restructuring of its debts and/or cramdown of dissenting creditors?

One possibility is a consensual, out-of-court debt restructuring, which can be used to recapitalise or reorganise the capital structure (debt and/or equity) of an entity and its subsidiaries outside of a bankruptcy case. Under such a debt restructuring, cramdown of dissenting creditors is not available.

5.6 Please briefly describe the liabilities of directors (if any) for continuing to trade whilst a company is in financial difficulties in your jurisdiction.

The United States does not impose personal liability on directors for insolvent trading. Under the law of some states, however, directors of an insolvent company may be found to have fiduciary duties not only to the company's shareholders, but also to its creditors, and a director's breach of those fiduciary duties may give rise to personal liability.

6 Foreign Investment and Ownership Restrictions

6.1 Are there any restrictions, controls, fees and/or taxes on foreign ownership of a project company?

While the United States generally has a liberal policy toward foreign direct investment, there are certain restrictions with respect to ownership of land with energy resources, as well as energy production facilities, assets and transmission infrastructure, under both state and Federal laws. For instance, mining of coal, oil, oil shale and natural gas on land sold by the Federal government is permitted by U.S. citizens, corporations and other U.S. entities only. Ownership and control of nuclear power facilities and leasing of geothermal steam and similar leases of Federal land, or licences to own or operate hydroelectric power facilities, are also generally restricted to U.S. persons only. However, a U.S.-registered corporation that is foreign-owned or -controlled may own hydroelectric power facilities.

Under the Exon-Florio Act of 1988, as amended ("Exon-Florio"), which is administered by the Committee on Foreign Investment in the United States (an inter-agency committee coordinated by the Department of Treasury), the President may block an investment or acquisition (or order that such investment or acquisition be unwound) after conducting an investigation that establishes that a foreign interest exercising control or influence on relevant U.S. resources, assets, infrastructure or technology "might take action that impairs the national security" that cannot be adequately addressed by any other provision of law.

As noted above in question 4.1, a foreign entity cannot hold a U.S. nuclear plant operating licence issued by the NRC or otherwise control the licensee. A foreign entity cannot directly hold a FERC hydro-electric licence, but may own or control a U.S. company that holds such a licence.

6.2 Are there any bilateral investment treaties (or other international treaties) that would provide protection from such restrictions?

The United States has concluded a number of bilateral treaties that protect investor rights to establish and acquire businesses, freedom from performance requirements, freedom to hire senior management without regard to nationality, rights to unrestricted transfer in convertible currency of all funds related to an investment, and, in the event of expropriation, the right to compensation in accordance with international law.

6.3 What laws exist regarding the nationalisation or expropriation of project companies and assets? Are any forms of investment specially protected?

Under the doctrine of eminent domain, the U.S. Federal government or any of the U.S. state governments may take private property without the property owner's consent, so long as just compensation is paid to the property owner.

7 Government Approvals/Restrictions

7.1 What are the relevant government agencies or departments with authority over projects in the typical project sectors?

Regulatory jurisdiction over the electric power sector in the United States is bifurcated between Federal and state authorities. State regulatory authorities retain jurisdiction over the siting of electric power generation, transmission and distribution facilities. In most of the United States, FERC has authority over wholesale sales of electric power, and power may not be sold at wholesale until FERC has granted authority to sell at negotiated, "market-based rates" ("MBR Authority"). The owners of certain small (not larger than 20 MW) qualifying facilities are exempted from the need to obtain MBR Authority, although owners of facilities larger than 1 MW must file a form with FERC in order to qualify. As noted in question 4.1, FERC lacks jurisdiction in the non-contiguous states (Alaska and Hawaii) and in the intrastate-only ERCOT region.

Dams and hydroelectric facilities on navigable waters are also subject to licensing by FERC, subject to exemption for very small projects. Interstate natural gas pipelines and underground natural gas storage projects are subject to FERC certificate authority.

Nuclear energy projects and the operators of such projects are subject to licensing by the NRC.

The Environmental Protection Agency ("EPA") governs the issuance of most Federal environmental permits. Environmental permits can also be required by state, local and other Federal governmental authorities.

7.2 Must any of the financing or project documents be registered or filed with any government authority or otherwise comply with legal formalities to be valid or enforceable?

There are a number of registration and filing requirements for financing or project documents that depend on the nature of the project and identity of the parties. For example, FERC requires approval of issuances of securities or assumptions of liabilities (e.g. incurrence of debt), subject to certain exceptions, for companies subject to its electric power jurisdiction. FERC customarily grants electric power generators with MBR Authority blanket approval for jurisdictional financings, and the owners of qualifying facilities that are exempt from FERC rate regulation are also exempt from FERC regulation of financings.

Please refer to question 18.2 for SEC-related requirements.

7.3 Does ownership of land, natural resources or a pipeline, or undertaking the business of ownership or operation of such assets, require a licence (and if so, can such a licence be held by a foreign entity)?

Please see questions 6.1 and 7.1 above. In addition, the operation of certain U.S. telecommunications infrastructure that is licensed by the FCC may be subject to direct or indirect foreign ownership restrictions, and, with the exception of broadcast radio and television assets, in many cases waivers of such foreign ownership restrictions are available for investors that are domiciled in countries that provide reciprocal market access for U.S. investors to own or invest in similar telecommunications infrastructure.

7.4 Are there any royalties, restrictions, fees and/or taxes payable on the extraction or export of natural resources?

Federal, state and private royalties are payable on the extraction of natural resources, as applicable.

In general, no specific Federal taxes are imposed on the extraction of natural resources, although income taxes are imposed on profits from sales. Domestic crude oil used in or exported from the United States is also subject to Federal tax. Income taxes may apply to sales outside of the United States to the extent such sales are related to business conducted in the United States.

7.5 Are there any restrictions, controls, fees and/or taxes on foreign currency exchange?

The United States does not generally impose controls or fees on foreign currency exchange. However, U.S. persons, which include U.S. companies and their foreign branches, are prohibited from engaging in transactions with individuals or entities that the Office of Foreign Assets Control of the U.S. Department of Treasury designates as individuals or entities owned or controlled by countries against which the United States has imposed sanctions, or that the United States has designated as terrorists, narcotics traffickers, cybercriminals, transnational criminal organisations or proliferators of weapons of mass destruction. In addition, U.S. persons and foreign persons engaged in business in the United States are subject to U.S. Federal and state income taxes on foreign currency exchange gains.

7.6 Are there any restrictions, controls, fees and/or taxes on the remittance and repatriation of investment returns or loan payments to parties in other jurisdictions?

Other than the withholding taxes discussed in question 17.1, there are no such generally applicable restrictions.

7.7 Can project companies establish and maintain onshore foreign currency accounts and/or offshore accounts in other jurisdictions?

Yes, they can.

7.8 Is there any restriction (under corporate law, exchange control, other law or binding governmental practice or binding contract) on the payment of dividends from a project company to its parent company where the parent is incorporated in your jurisdiction or abroad?

Apart from the withholding taxes discussed under question 17.1, New York law financing documents, which often impose restricted payment conditions on the issuance of dividends, and shareholders' agreements, typically contain restrictions. In addition, project companies subject to FERC regulation of issuances of securities and assumption of liabilities under Section 204 of the Federal Power Act, other than blanket authority under MBR Authority (discussed at 7(a) above), are subject to certain restrictions, such as restrictions requiring parent debt obligations to follow up to the parent company if a project company borrows at the public utility level and "dividends up" the proceeds to its non-public utility parent.

7.9 Are there any material environmental, health and safety laws or regulations that would impact upon a project financing and which governmental authorities administer those laws or regulations?

The Clean Air Act and the Clean Water Act are generally the most material Federal statutes that would impact power projects. Permits related to air emissions and water discharges under these statutes and similar state laws may be required prior to the start of construction by the EPA or by state or local governmental authorities.

Any major Federal action or decision, including the granting of certain permits by the U.S. Fish and Wildlife Service and the U.S. Army Corps of Engineers, or the approval of a loan guarantee by the DOE, is subject to comprehensive environmental review under the National Environmental Policy Act. Some states, notably California, require similar state-level comprehensive environmental review of discretionary governmental actions relating to power project permitting and siting.

In terms of international frameworks, the Equator Principles are voluntary and would only be used with respect to a project if required by the applicable financial institution. Since the U.S. has comprehensive environmental laws and is a designated country, covenants to comply with environmental law in conjunction with the performance of standard due diligence are often deemed sufficient. As a result, representations and warranties and covenants expressly related to the Equator Principles are often not included in the applicable project agreement.

7.10 Is there any specific legal/statutory framework for procurement by project companies?

Outside of the nuclear industry, privately owned and financed project companies are not subject to governmental oversight for procurement.

8 Foreign Insurance

8.1 Are there any restrictions, controls, fees and/or taxes on insurance policies over project assets provided or guaranteed by foreign insurance companies?

Such restrictions are applicable on a case-by-case basis depending on the location and nature of the project, the type of project and the identity of the project parties.

8.2 Are insurance policies over project assets payable to foreign (secured) creditors?

Such restrictions are applicable on a case-by-case basis depending on the location and nature of the project, the type of project and the identity of the project parties.

9 Foreign Employee Restrictions

9.1 Are there any restrictions on foreign workers, technicians, engineers or executives being employed by a project company?

Foreign workers employed by a project company within the United States are required to have work authorisation in accordance with U.S. immigration laws. This can be achieved via various "non-immigrant" or temporary visa categories which are typically based on employer sponsorship. In addition, work authorisation might be obtained via permanent resident status (also known as green card or immigrant status), often through sponsorship from an employer (which can be a difficult and lengthy process) or from sponsorship by an immediate family member who is a U.S. citizen (which may be less difficult than employer sponsorship but is generally a lengthy process).

10 Equipment Import Restrictions

10.1 Are there any restrictions, controls, fees and/or taxes on importing project equipment or equipment used by construction contractors?

There may be customs duties on imported project equipment, which are determined based upon the country of origin of the equipment unless a relevant trade agreement eliminates or reduces certain of these tariffs.

10.2 If so, what import duties are payable and are exceptions available?

The Harmonized Tariff System provides duty rates based on the classification of the imported equipment.

11 *Force Majeure*

11.1 Are *force majeure* exclusions available and enforceable?

Yes, *force majeure* exclusions are available and enforceable and are applied such that one or both parties are excused from performance of the project agreement, in whole or in part, or are entitled to suspend performance or claim an extension of time for performance. Invocation of a *force majeure* clause can trigger *force majeure* across other related project agreements, and thus it is important to ensure that the *force majeure* provisions "mesh" with those found in related project agreements. Some *force majeure* provisions, however, typically will not excuse parties from any monetary payments that mature prior to the occurrence of the *force majeure* event.

A typical *force majeure* provision will set forth a non-exhaustive list of events that constitute *force majeure*, which often include natural *force majeure*, such as acts of God, and political *force majeure*, such as war or terrorism, as well as the effect on the parties' rights and obligations if a *force majeure* event occurs.

12 Corrupt Practices

12.1 Are there any rules prohibiting corrupt business practices and bribery (particularly any rules targeting the projects sector)? What are the applicable civil or criminal penalties?

The Foreign Corrupt Practices Act of 1977 ("FCPA") prohibits the bribery of foreign government officials. The law contains two sets of provisions: (i) it prohibits corrupt payments to officials and agents of foreign governments by U.S. persons; and (ii) it requires accounting practices to accurately reflect payments to foreign officials and agents.

Among other penalties, (i) for violations of the FCPA's anti-bribery provisions, the U.S. Department of Justice ("DOJ") may impose criminal penalties of up to $2 million against offending firms and fines of up to $250,000 and imprisonment for up to five years for offending officers, directors, stockholders, employees and agents, and (ii) for violations of the FCPA's accounting provisions, the DOJ and the Securities and Exchange Commission may bring civil and criminal actions, which include criminal penalties of up to $25,000,000 against offending firms and of up to $5,000,000 and imprisonment for up to twenty years for offending directors, officers, employees or agents of such firm.

13 Applicable Law

13.1 What law typically governs project agreements?

Project agreements may be governed by the law of any state but may be subject to the doctrine of *lex situs* (i.e. the rule that the law applicable to proprietary aspects of an asset is the law of the jurisdiction where the asset is located).

13.2 What law typically governs financing agreements?

New York law typically governs financing documents since the commercial laws and legal precedents in the state of New York tend to be more settled than in other states, making lenders more comfortable. Security documents, such as the mortgage, may be legally required to be governed by the law of the state in which the collateral is located.

13.3 What matters are typically governed by domestic law?

Please see questions 13.1 and 13.2 above.

14 Jurisdiction and Waiver of Immunity

14.1 Is a party's submission to a foreign jurisdiction and waiver of immunity legally binding and enforceable?

Yes, foreign law may govern a contract. However, the Foreign Sovereign Immunities Act provides an exception to immunity through waiver, which may be explicit or implicit.

15 International Arbitration

15.1 Are contractual provisions requiring submission of disputes to international arbitration and arbitral awards recognised by local courts?

Yes, they are typically recognised by local courts.

15.2 Is your jurisdiction a contracting state to the New York Convention or other prominent dispute resolution conventions?

Yes, the United States is a contracting state to the New York Convention, which requires courts of contracting states to give effect to arbitration agreements and recognise and enforce awards made in other states, subject to reciprocity and commercial reservations. The United States made a reservation that it will apply the New York Convention only to awards made in the territory of another contracting state and only to disputes arising out of legal relationships (whether contractual or not) that are considered commercial under the relevant national law.

The United States is also party to: (i) the Inter-American Convention on International Commercial Arbitration ("Panama Convention"), which governs international arbitral awards where expressly agreed by the parties or where "a majority of the parties to the arbitration agreement are citizens of a state or states that have ratified or acceded to the Panama Convention and are member States of the Organization of American States" only; and (ii) the International Convention on the Settlement of Investment Disputes ("Washington Convention"), which is applicable to disputes between a government entity and a national of another signatory state.

15.3 Are any types of disputes not arbitrable under local law?

Yes, certain disputes involving family law and criminal law are not arbitrable. Claims under securities laws, Federal antitrust laws and the civil provisions of the Racketeer Influenced and Corrupt Organizations Act have been found by the U.S. Supreme Court to be arbitrable.

15.4 Are any types of disputes subject to mandatory domestic arbitration proceedings?

With few exceptions, such as small disputes at the local court level, there are no broad categories of commercial disputes that must be resolved by arbitration, absent an agreement of the parties to that effect.

16 Change of Law / Political Risk

16.1 Has there been any call for political risk protections such as direct agreements with central government or political risk guarantees?

Generally, no.

17 Tax

17.1 Are there any requirements to deduct or withhold tax from (a) interest payable on loans made to domestic or foreign lenders, or (b) the proceeds of a claim under a guarantee or the proceeds of enforcing security?

Withholding of U.S. Federal income tax at a rate of 30% is generally required on payments of interest, dividends, royalties and other amounts (not including principal on loans or distributions by corporations that are treated as returns of capital) to foreign persons unless attributable to a branch office maintained by the recipient within the United States. The United States maintains treaties with numerous jurisdictions that reduce or eliminate these withholding taxes on amounts paid to qualified residents of the counterparty treaty country. In addition, interest paid to foreign persons, other than banks on loans made in the ordinary course of business, is exempt from this withholding tax if certain requirements are satisfied, including that the loan is not in bearer form and the lender is unrelated to the borrower.

Even where an exemption may be available, under the Foreign Account Tax Compliance Act ("FATCA"), interest paid and, beginning after December 31, 2018, the gross proceeds of a sale or other disposition of any loan that can produce U.S.-source interest paid to a foreign financial institution (whether such foreign financial institution is a beneficial owner or an intermediary) may be subject to U.S. Federal withholding tax at a rate of 30% unless: (x) (1) the foreign financial institution enters into an agreement with the U.S. Internal Revenue Service to withhold U.S. tax on certain payments and to collect and provide to the U.S. Internal Revenue Service substantial information regarding U.S. account holders of the institution (which includes, for this purpose, among others, certain account holders that are foreign entities that are directly or indirectly owned by U.S. persons), or (2) the institution resides in a jurisdiction with which the United States has entered into an intergovernmental agreement ("IGA") to implement FATCA, and complies with the legislation implementing that IGA; and (y) the foreign financial institution provides a certification to the payor for such amounts that it is eligible to receive those payments free of FATCA withholding tax. The legislation also generally imposes a U.S. Federal withholding tax of 30% on interest paid and, beginning after December 31, 2018, the gross proceeds of a sale or other disposition of loans that can produce U.S.-source interest paid, to a non-financial foreign entity (whether such non-financial foreign entity is a beneficial owner or an intermediary) unless such entity (i) provides a certification that such entity does not have any "substantial United States owners", or (ii) provides certain information regarding the entity's "substantial United States owners", which will in turn be provided to the U.S. Internal Revenue Service.

From a U.S. tax perspective, amounts received from a guarantor or from the proceeds of property pledged as collateral are characterised and taxed in the same manner as amounts paid on the underlying claim would have been taxed.

17.2 What tax incentives or other incentives are provided preferentially to foreign investors or creditors? What taxes apply to foreign investments, loans, mortgages or other security documents, either for the purposes of effectiveness or registration?

There are very few Federal incentives targeted at foreign investors or lenders.

No Federal taxes are required for the effectiveness or registration of an agreement. Various documentary recording and transfer taxes apply at the state level.

18 Other Matters

18.1 Are there any other material considerations which should be taken into account by either equity investors or lenders when participating in project financings in your jurisdiction?

The above questions and answers address most of the main material considerations for project financings governed by New York law in the United States.

18.2 Are there any legal impositions to project companies issuing bonds or similar capital market instruments? Please briefly describe the local legal and regulatory requirements for the issuance of capital market instruments.

Project bonds are securities and therefore are subject to the various U.S. securities offering and fraud laws (principally the Securities Act of 1933 ("Securities Act") and the Securities Exchange Act of 1934). Under the Securities Act, securities in the United States must be sold pursuant to an effective registration statement filed with the U.S. Securities Exchange Commission ("SEC") or pursuant to an exemption from filing. Very few, if any, project bonds are sold in SEC-registered offerings. The most common exemptions are offerings pursuant to Section 4(a)(2) of the Securities Act and Rule 144A and Regulation S thereunder. Rule 144A project bond offerings require a comprehensive offering document that describes in detail the project, the project and finance documents, the risks associated with the project along with a summary of the bond terms, a description of project modelling, limited information about the sponsors and offtakers and various other disclosures. The underwriters and their legal counsel perform due diligence (in order for counsel to provide 10b-5 statements) to mitigate securities law fraud liability. Offerings solely under Regulation S and Section 4(a)(2) typically have much less disclosure and diligence and the disclosure is more similar to that used in a typical bank deal.

19 Islamic Finance

19.1 Explain how *Istina'a*, *Ijarah*, *Wakala* and *Murabaha* instruments might be used in the structuring of an Islamic project financing in your jurisdiction.

While Islamic project financing is relatively new to the U.S. market, there are generally three types of financing structures used in Islamic project financing globally: (i) *Istisna'a* (or *Istina'a*)-*Ijarah* (construction contract-lease); (ii) *Wakala-Ijarah* (agency-lease); and (iii) *Sharikat Mahassa-Murabaha* (joint venture-bank purchase and sale) structures.

Under the *Istisna'a-Ijarah* structure, which is believed to be the more popular structure in Islamic project financing, an *Istisna'a* instrument (similar to a sales contract) is usually applied to the construction phase and an *Ijarah* instrument (similar to a lease-to-own agreement) is usually applied to the operations phase. During the construction phase, the borrower procures construction of project assets and then transfers title to assets to the lenders. As consideration, a lender makes phased payments to the borrower (equivalent to loan advances). During the operations phase, the lenders lease project assets to the borrower. The borrower, in turn, makes lease payments (equivalent to debt service). Unlike in traditional project financing, the lender, as the owner of the underlying assets, can be exposed to a number of potentially significant third-party liabilities, including environmental risk.

The *Wakala-Ijarah* structure differs from the *Istisna'a-Ijarah* structure as the borrower is employed as the lender's agent *per* an agency (*Wakala*) agreement. The borrower/lender relationship is different from the *Istisna'a-Ijarah* structure in that the borrower procures the construction as the lender's agent.

A less commonly used structure is the *Sharikat Mahassa-Murabaha* structure. Under this structure, the borrower and the lenders enter into a joint venture (*Sharikat Mahassa*) agreement which is not disclosed to third parties. A *Murabaha* transaction is one in which a bank finances the purchase of an asset by itself purchasing that asset from a third party and then reselling that asset at a profit to the borrower pursuant to a cost-plus-profit agreement, akin to a loan. Each member of the joint venture holds *Hissas* (shares) in the joint venture purchased by capitalising the *Sharikat Mahassa*. The *Murabaha* portion of the transaction involves sales of *Hissas* from time to time by the lenders to the borrower in compliance with *Shari'ah* law.

19.2 In what circumstances may *Shari'ah* law become the governing law of a contract or a dispute? Have there been any recent notable cases on jurisdictional issues, the applicability of *Shari'ah* or the conflict of *Shari'ah* and local law relevant to the finance sector?

Generally, under U.S. state and Federal law, contracting parties may select any law as the governing law of the contract so long as it is sufficiently defined and capable of enforcement. However, there is limited case law and no conclusive rulings by U.S. courts on whether *Shari'ah* law would be recognised as a system of law capable of governing a contract.

In the U.S. bankruptcy court case of *In re Arcapita Bank, B.S.C.(c), et al.*, Case No. 12-11076 (SHL) (Bankr. S.D.N.Y.), an investor of the debtors objected to the debtors' motion to approve debtor-in-possession and exit financing, asserting, among other things, that the financing was not *Shari'ah*-compliant. In statements made on the record, the court noted that the financing agreement was governed by English law and expressly provided that no obligor was permitted to bring a claim based on *Shari'ah* compliance of the finance documents. The court then appeared to adopt the English courts' approach of avoiding ruling or commenting on compliance of an agreement with *Shari'ah* law, citing a recent English court case that found that, irrespective of *Shari'ah* compliance, *Shari'ah* law was not relevant in determining enforceability of a financing agreement governed by English law, and that *Shari'ah* principles are far from settled and subject to considerable disagreement among clerics and scholars. However, the precedential value of the *Arcapita* bankruptcy court's refusal to consider whether the financing was *Shari'ah*-compliant may be limited, given that the district court dismissed the objector's appeal of the bankruptcy court's approval of the financing (along with an appeal asserted by the objector of confirmation of the debtors' chapter 11 plan of reorganisation) as equitably moot.

19.3 Could the inclusion of an interest payment obligation in a loan agreement affect its validity and/or enforceability in your jurisdiction? If so, what steps could be taken to mitigate this risk?

Generally, no.

Acknowledgment

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