

The UK Guarantees Scheme for Infrastructure Projects

A brief overview of the standard documentation

ALLEN & OVERY

Introduction

Further to Her Majesty's Treasury (**HMT**) making available £40bn¹ of financial guarantees for certain infrastructure projects in the UK (the **UK Guarantees Scheme**), Infrastructure UK (**IUK**) (a unit within HMT) and Allen & Overy LLP (**A&O**, as legal adviser to IUK) have prepared a short background and overview of the key documentation, for the benefit of interested parties.

Expenditure incurred by HMT in connection with the UK Guarantees Scheme is authorised by the Infrastructure (Financial Assistance) Act 2012, which received Royal Assent on 31 October 2012 (the **Infrastructure Act**). The Infrastructure Act envisages that HMT may provide financial support for a wide range of UK infrastructure projects, including utilities, railway facilities (including rolling stock), roads or other transport facilities, health or educational facilities, court or prison facilities, and housing. Support may be provided not only for greenfield/construction phase projects, but also for the acquisition, design, conversion, improvement, operation or repair of infrastructure assets.

Financial guarantee

HMT's support will take the form of an unconditional and irrevocable financial guarantee (the **UK Guarantee**) of scheduled principal and interest in favour of a lender to/investor in a UK infrastructure project (a **Beneficiary**) and on behalf of the relevant borrower/issuer of debt (the **Company**). The UK Guarantee will be issued in return for the payment of a guarantee fee to be charged at market rates. Each UK Guarantee will, to a varying extent, need to be tailored to the underlying project and the particular Beneficiary. It is designed, though, to be as simple and as flexible as possible. As further detailed below each UK Guarantee will be structured such that, from the Beneficiary's perspective, the UK Government (and its credit rating) is effectively "substituted" for the Company. As a result, the relationship between HMT and the Beneficiary is very straightforward - as is, more importantly, the relationship between the Beneficiary and the Company. For example, a Beneficiary may conclude that it needs little to no contractual recourse against the Company. It is hoped that the simplicity of this structure (both in terms of concept and execution) will greatly assist the overall commercial imperative of stimulating UK infrastructure.

While the pro-forma documents referred to below are drafted to relate to an underlying bond financing, the wording may be adapted to accommodate a wide range of underlying instruments, ranging from the very simple to the complex, as further discussed below.

Notwithstanding the above, the Company and HMT will enter into further documentation to detail certain bilateral rights and obligations, such as those relating to reimbursement (should the UK Guarantee be called upon), together with appropriate representations and warranties. On financings which involve other creditors and/or the sharing of security, it will be appropriate for HMT to enter into certain intercreditor arrangements dealing with the interaction of the wider group of creditors of the Company.

Focus

This note provides a high level overview of the UK Guarantees Scheme only. As noted, the scheme may be applied not only in relation to a range of financing structures, but also a range of project structures. The Company may, for example, be the counterparty of a concession agreement entered into with a public authority or may be the holder of a right or licence to develop a particular project or exploit a particular asset. These details and some associated consequences would be project specific but the key documentation (the UK Guarantee and Guarantee and Reimbursement Agreement), and certain bilateral and/or intercreditor rights that HMT may have, would remain.

¹ The Infrastructure Act makes available a total of £50bn for financial guarantees, £10bn of which has been specifically allocated for housing guarantees.

The UK Guarantee document suite: general observations

A&O has worked with IUK to develop a standard suite of documentation for the UK Guarantees Scheme, while acknowledging that the documentation will be tailored to the specific underlying transaction. The key agreements are the UK Guarantee itself and the Guarantee and Reimbursement Agreement, each as further described below. Depending on the transaction further documents may be entered into, including agreements which may contain representations, warranties and covenants given by the Company to HMT or, alternatively, HMT may become party to certain underlying intercreditor arrangements. Furthermore, it is intended that the UK Guarantees Scheme could be adaptable to any financing structure.

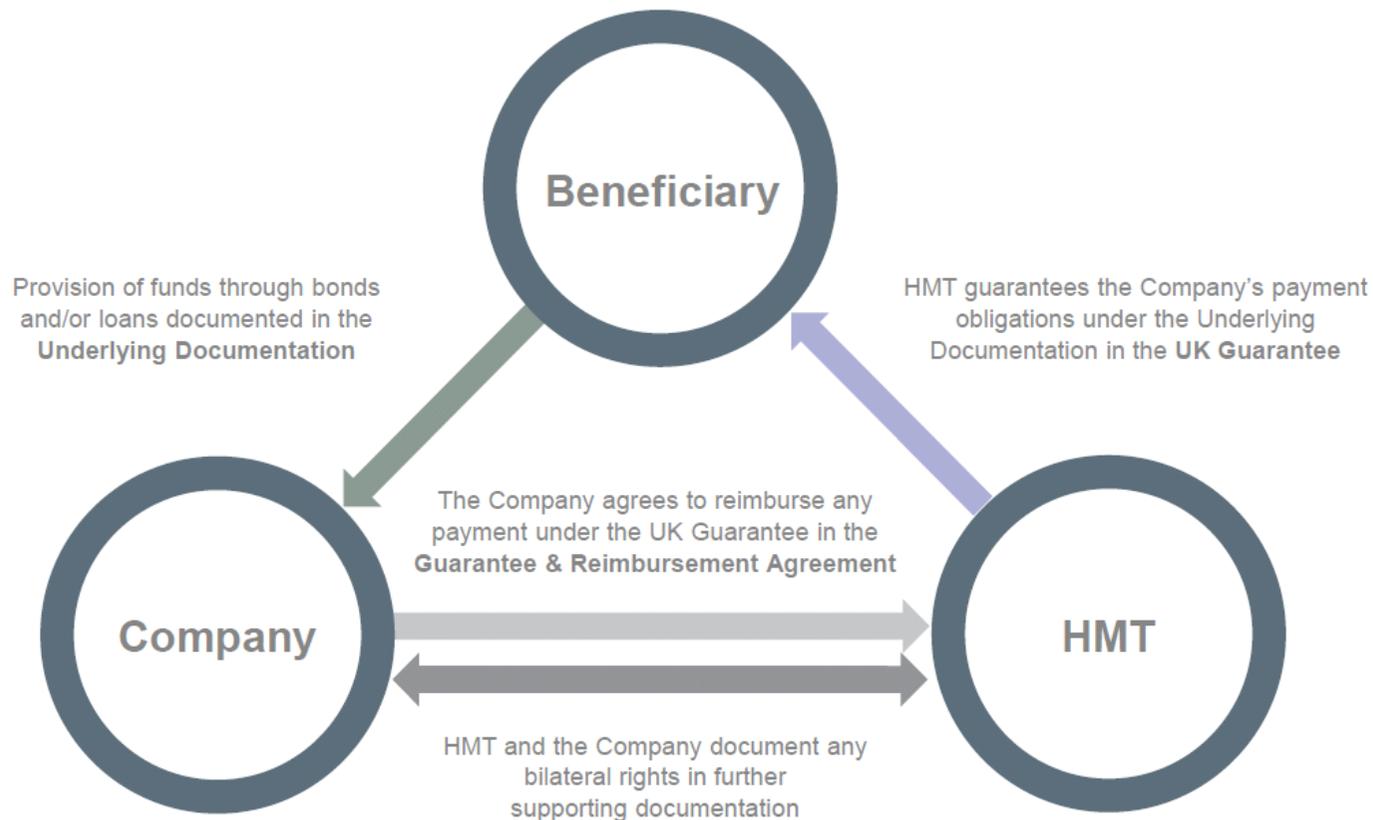


Diagram: a simplified view of the key documentation

Key documents

UK Guarantee

Guaranteed amounts and obligations

In return for the payment of guarantee fees charged at market rates (pursuant to a fee letter between HMT and the Company), HMT will provide an unconditional and irrevocable financial guarantee in favour of a Beneficiary and on behalf of the Company, capable of demand in the event of non-payment of scheduled principal and interest owing from time to time under the underlying document (be that a loan, a bond, or other financial instrument). To this end, HMT will unconditionally and irrevocably agree to pay to the Beneficiary any such amounts which have become due for payment but are unpaid by reason of nonpayment. HMT will also cover payments that are subsequently set aside for being contrary to the prevailing UK insolvency legislation (defined as "Avoided Payment Amounts" in the UK Guarantee). To the extent that the default amount owed by the Company exceeds the Guaranteed Amounts, payment of such excess is not guaranteed by HMT under the UK Guarantee.

It is envisaged that, where amounts are required to be prepaid by the Company under the underlying documentation, these amounts will continue to be paid out over time by HMT in accordance with the terms of the UK Guarantee. There may be limited negotiated exceptions to this rule where HMT feels that it is appropriate to cover unpaid prepayment amounts in specific situations, such as payments to a specific lender or noteholder becoming illegal. In such cases, HMT will look to document certain controls over these events.

Flexible format

The UK Guarantee will be contained in a deed of guarantee which has been designed to comply with the Guarantee Notice (as defined in footnote 2 below) and may relate to a wide range of underlying instruments which allow a Company to raise funds - for example, the Company may issue debt securities,² for which HMT may guarantee 100 per cent. of the underlying amount. It is also envisaged that, where bonds are guaranteed by HMT, a Prospectus Directive compliant prospectus will not be required to be produced, as those bonds would be securities unconditionally and irrevocably guaranteed by a member state.³

The pro-forma deed envisages the beneficiary of the UK Guarantee being a bond trustee, acting on behalf of the holders of bonds issued by the Company. However, the form is flexible and can be easily amended to reflect a different financing structure. For example, if the deal is a financed by a syndicate of banks through loan documentation, then the definition of "Beneficiary" would be updated to reflect the fact that the beneficiary of the UK Guarantee in that scenario was a facility agent or a security trustee holding the UK Guarantee on behalf of and for the benefit of the syndicate. Similarly, the UK Guarantee could be easily adapted to relate to a very simple bilateral loan or private bond issue.

² "Debt securities" are referenced in the Commission Notice on the application of Articles 87 and 88 of the EC Treaty to State aid in the form of guarantees (2008/C 155/02) (the **Guarantee Notice**); Article 2(1)(b) of Directive 2004/109/EC defines the term as "bonds or other forms of transferable securitised debts, with the exception of securities which are equivalent to shares in companies or which, if converted or if the rights conferred by them are exercised, give rise to a right to acquire shares or securities equivalent to shares".

³ Article 1(2)(d) of the **Prospectus Directive** (2003/71/EC) (as amended).

Termination

HMT does not envisage the UK Guarantee being released until the guaranteed amounts have been paid in full and (to the extent that this would fall on a later date) one day following the last date on which any guaranteed amount may be avoided under relevant insolvency law (or, where applicable, for so long as any insolvency proceedings are continuing or payment of avoided amounts remains outstanding). As a starting point, there will be no covenants or representations within the UK Guarantee itself, nor will there be ratings triggers or other events of default related to the status of HMT, but repudiation by HMT will have contractual consequences.

Cost

The cost to the Company of the UK Guarantee will be the underlying cost charged by the Beneficiary to provide finance under the underlying documentation and also the fees charged by HMT (which will be set out in more detail in a fee letter) in return for making the UK Guarantee available to the Beneficiary.

Payment process

HMT will be required to make payments due under the UK Guarantee to the Beneficiary by 4pm on the fourth business day following receipt by HMT of a duly completed notice of demand (the **Notice of Demand**, the form of which is scheduled to the UK Guarantee) or, if later, the applicable due date for the Company's payment. The Notice of Demand may be submitted in advance of such due date if the Beneficiary has sufficient evidence that payment will not be made. HMT will work with all parties to ensure that such evidence may be provided in sufficient time to enable any payment under the UK Guarantee to be made when contractually due under the underlying documentation. Receipt of a Notice of Demand after noon (London time) or on a day that is not a business day will be treated as receipt on the next following business day.

When making a payment under the UK Guarantee, HMT will credit the account specified in the Notice of Demand and payment in full to such account will discharge HMT's obligations in respect of that claimed amount notwithstanding how the amount is applied after it is credited to the account.

Guarantee and Reimbursement Agreement

Under the terms of the Guarantee and Reimbursement Agreement, the Company will be obliged to reimburse HMT in respect of all payments made by HMT to the Beneficiary under the UK Guarantee. In addition, HMT will be subrogated to the rights of the Beneficiary in respect of any payments made by it under the UK Guarantee, that is to say that HMT will be entitled to "step into the shoes" of the Beneficiary and acquire the rights to use its name to proceed against any third party and/or claim from it any sums received from any third party.

Supporting finance documentation and intercreditor relationships

Other supporting documentation will govern the rights that HMT has *vis-à-vis* both the Company and other parties to the underlying transaction. Such arrangements will vary from project to project, with the degree of control HMT considers acceptable being based on consideration of all the parties and circumstances involved in that project. This documentation might regulate, among other things: (i) the claims of the senior creditors of the Company (the **Senior Creditors**); (ii) the exercise, acceleration and enforcement of rights by the Senior Creditors; (iii) the rights of the Senior Creditors to instruct the facility agent/security trustee; (iv) any entrenched rights or reserved matters of the different classes of Senior Creditors; (v) the giving of consents and waivers and the making of modifications to the underlying finance documents; (vi) the ranking in point of payment of the claims of any hedging providers and the Senior Creditors; and (vii) the subordination of claims against the Company. It is envisaged that there will be no general standstill or deadlock provisions in the intercreditor arrangements.

HMT will generally look to vote all amounts guaranteed under the UK Guarantee and the Guarantee and Reimbursement Agreement and to receive information available to other Senior Creditors from the date of the UK Guarantee, to the extent that this is appropriate for the underlying transaction.

Benefiting from the UK Government's credit rating

The UK Guarantees Scheme is structured so that both the Company and the Beneficiary take advantage of the UK Government's credit rating.

The nature and form of the guarantee is key in achieving this and the pro forma UK Guarantee has been specifically designed to ensure that a prospective Beneficiary is able to rely on the UK Government's rating when pricing its investment in a UK Guarantee supported infrastructure project.

Specifically, the UK Guarantee represents an unconditional and irrevocable obligation to pay guaranteed amounts without any defences, the need to make any demand or to take any action against the Company, and without any requirement for the Beneficiary to exhaust judicial or other remedies. In addition, the UK Guarantee and the mechanic for claiming under it are capable of being structured so that payments are made when due under the underlying document, rather than introducing any delay. The UK Guarantee also contains a number of clauses which are aimed at waiving or disapplying certain rights that guarantors gain by way of law, and which might otherwise prevent the UK Guarantee functioning as commercially intended – for example, the UK Guarantee is irrevocable and is not discharged by any part payment by HMT. We believe that a supporting legal opinion on the enforceability of the UK Guarantee will be an important part of the overall package for an investor and A&O have agreed a form of this with a number of investors.

These key structural aspects of the UK Guarantee are often taken into account by the leading rating agencies when assessing the support offered by financial guarantees pursuant to their methodologies. In our opinion, the UK Guarantee will stand up well to the published rating agency criteria that we are aware of.

Important note regarding reliance

This document is for general guidance only and does not constitute definitive advice. It may not be relied upon by any party for any purpose.

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