



Negotiating Direct Agreements

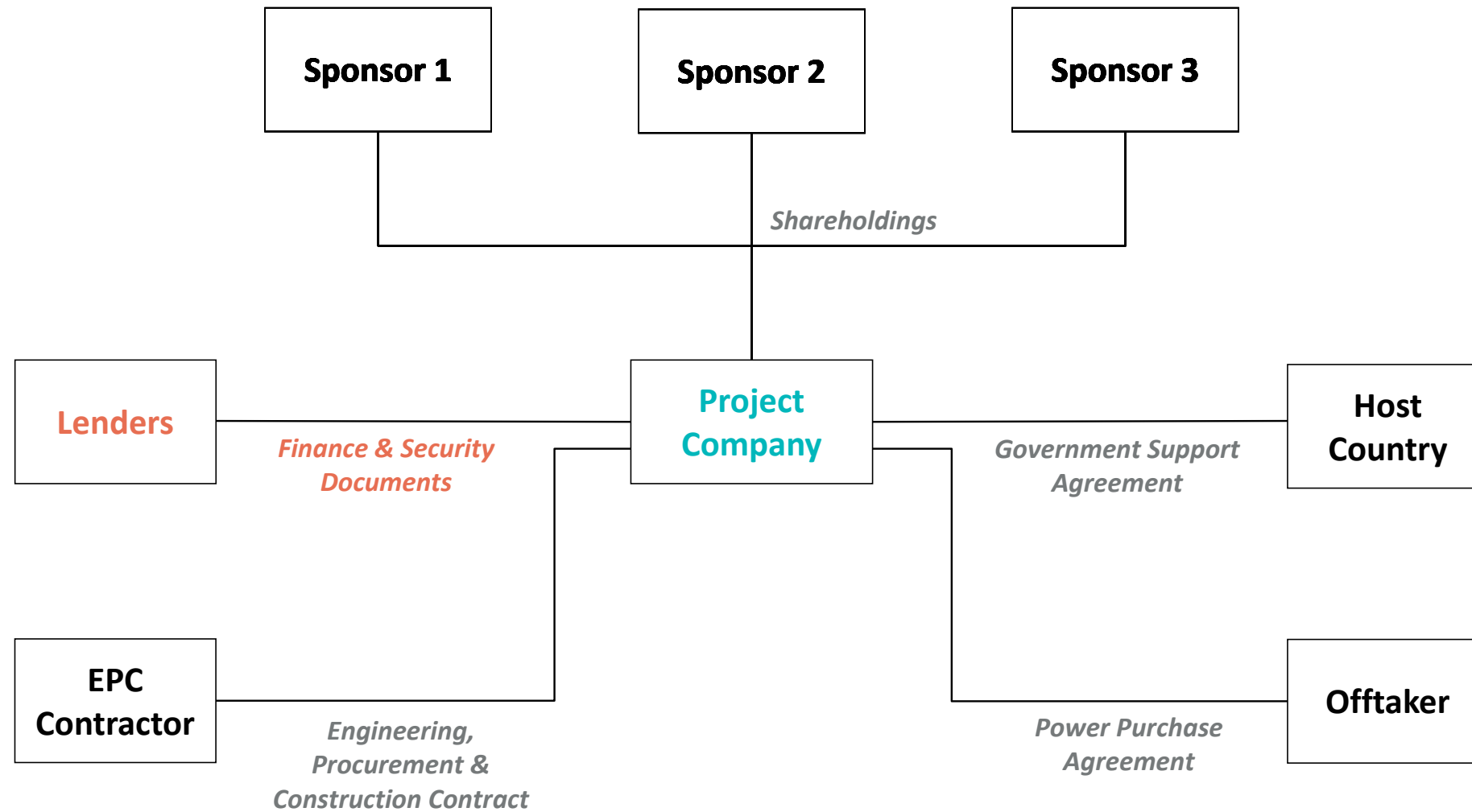
Topics

- 1. The purpose of direct agreements**
- 2. Key provisions in direct agreements**
- 3. Step-in and novation rights**
- 4. When to require a (long-form) direct agreement**
- 5. Key negotiation points**

1. The purpose of Direct Agreements

- **Used to enhance a lenders' security in a project-financed transaction**
 - Project finance
 - Financing provided on a non-recourse or limited recourse basis
 - Lenders look to the revenues and assets of a special purpose vehicle or **project company** to repay the loans

1. The purpose of Direct Agreements



1. The purpose of Direct Agreements

- A Direct Agreement **perfects** and **supplements** the security granted over a project agreement that would be difficult to replace
- **Perfecting asset-level security**
 - Notice to, and the consent of, a counterparty is required to perfect the collateral assignment of contract rights.
- **Supplementing asset-level security**
 - Provide a defensive framework in relation to asset-level security.
 - Enable lenders to exercise control over a distressed project (by exercising step-in rights).
 - If the lenders ultimately enforce their security, a direct agreement facilitates the sale of the project by allowing the lenders to transfer key project agreements to a replacement project company.
 - Amend onerous provisions in the underlying project agreement.

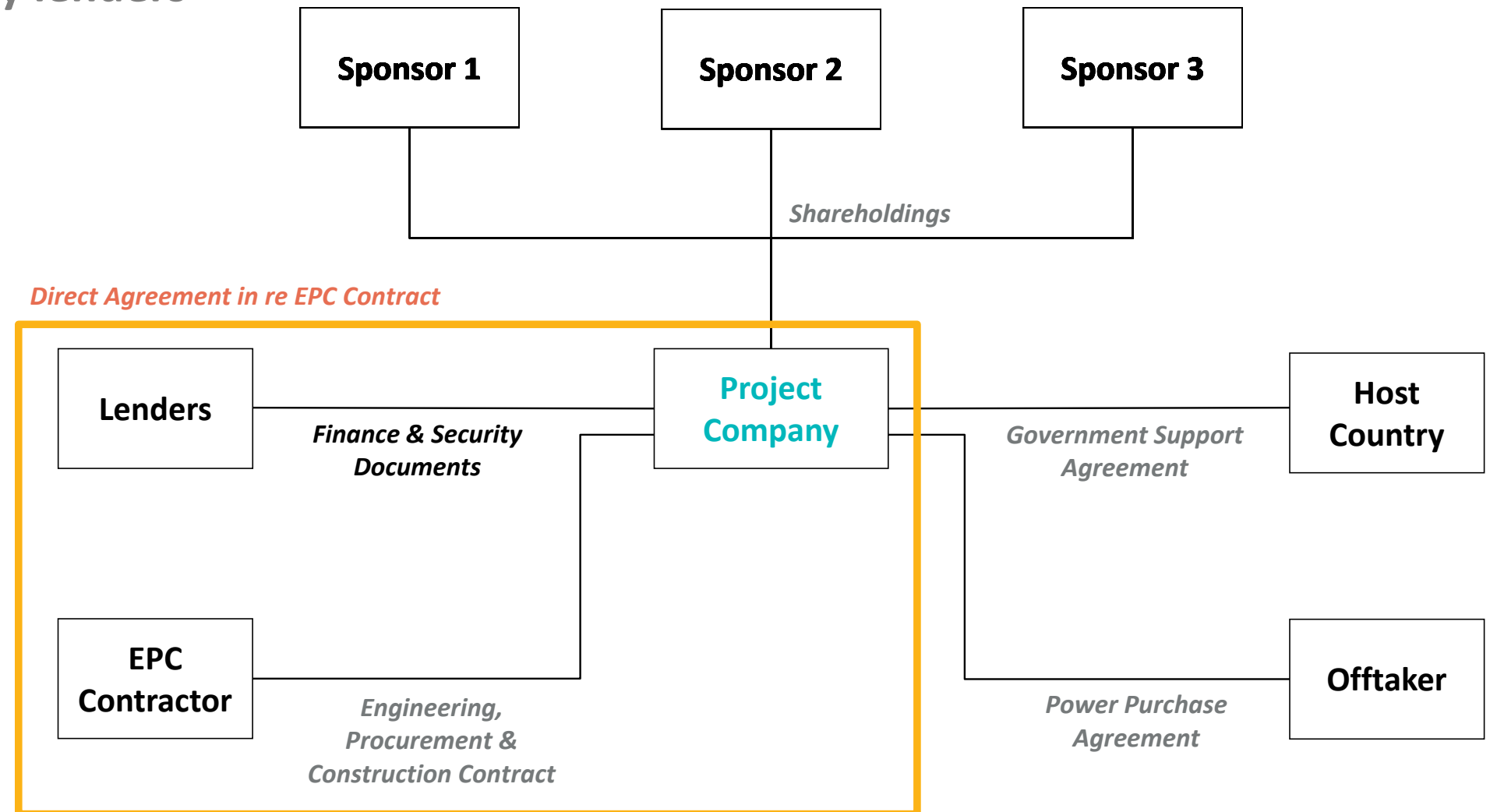
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2. Key provisions in Direct Agreements

- **Parties to a Direct Agreement:**

- Security agent appointed by lenders
- Project company
- Counterparty to the assigned contract



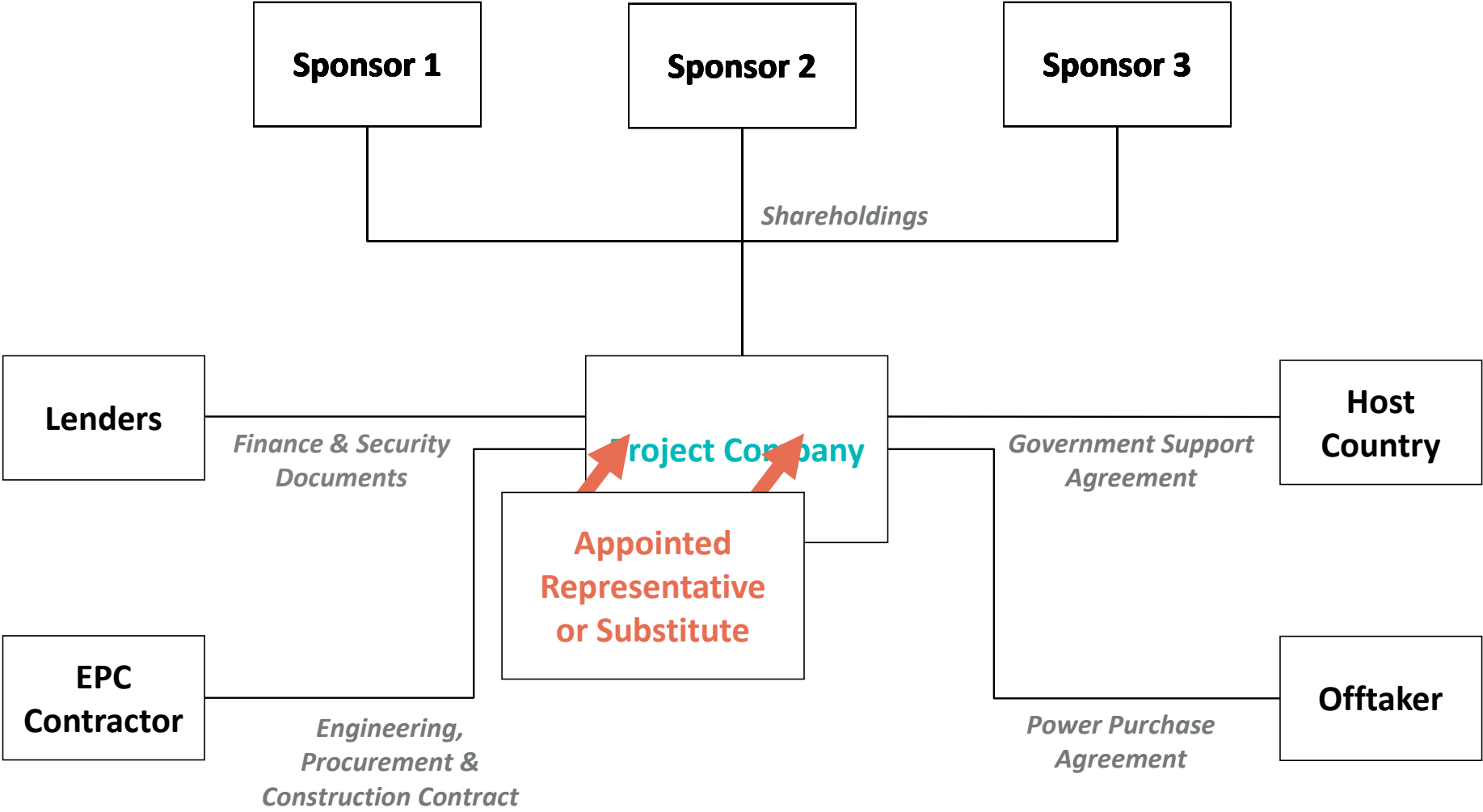
2. Key provisions in Direct Agreements

- **Acknowledgement and consent to collateral assignment**
- **Notice from counterparty to lenders of defaults by project company**
- **Standstill (suspension) period during which lenders consider whether to exercise step-in rights**
- **Step-in rights to**
 - cure project company defaults, and
 - exercise the rights and discretions of the project company
- **Transfer provisions to facilitate novation of the project agreement to a new project company**
- **Amendments to the project agreement required to address issues identified during lenders' due diligence**

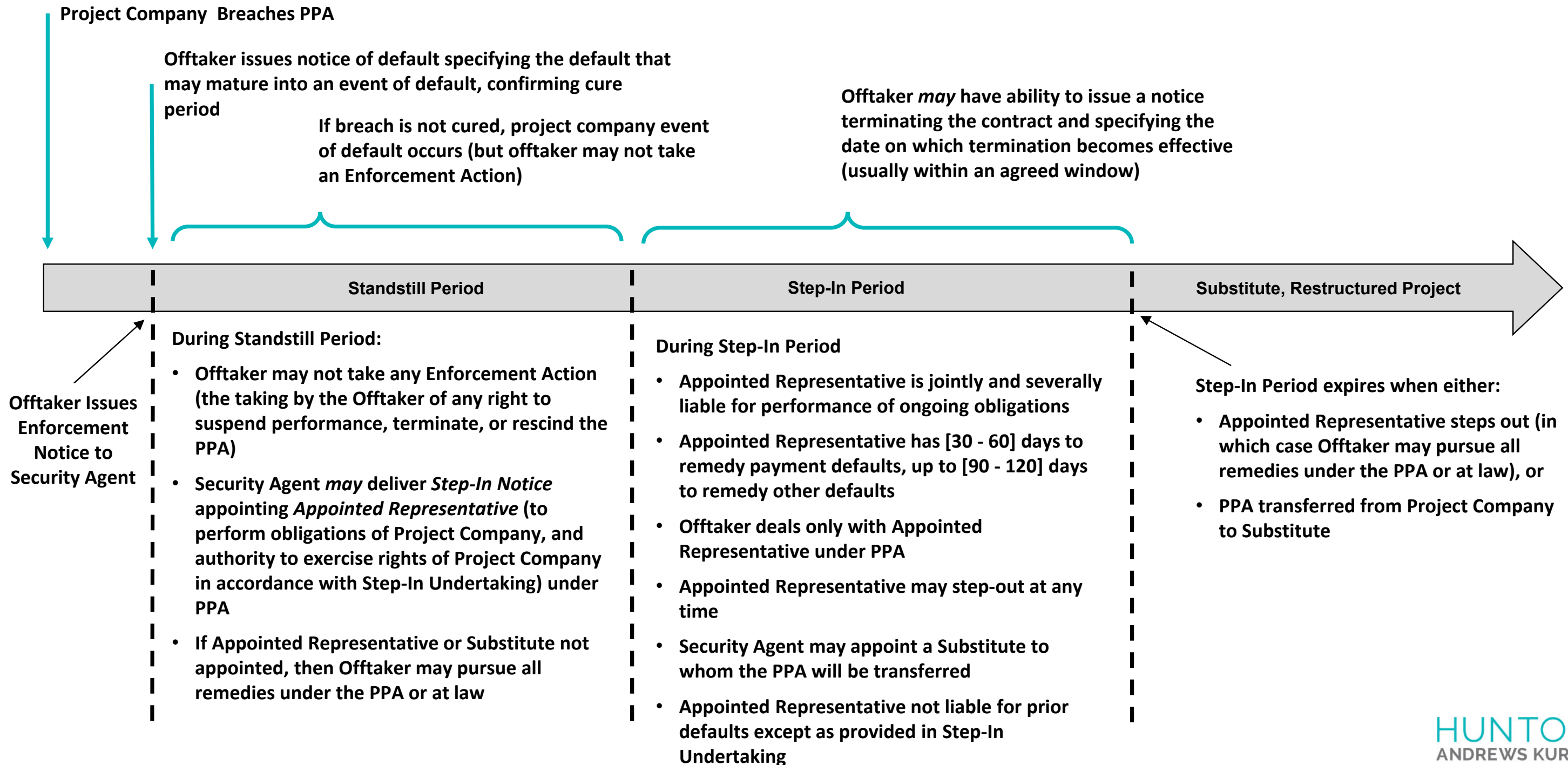
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3. Step-in and novation rights



3. Step-in and novation rights



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4. When to require a (long-form) Direct Agreement

- **We generally recommend direct agreements in relation to:**
 - significant revenue generating contracts
 - key fuel supply agreements
 - any material construction contract
 - any interconnection or interface agreement
 - any significant O&M contract
 - any other commercial contract that is fundamental to the performance of the project
- **If negotiating a direct agreement proves overly difficult, consider the following.**
 - Would it be difficult to find a replacement contract on equal or better terms?
 - Are the contractual provisions highly tailored to the project?
 - Does the project agreement relate to essential goods or services?
 - Is the term of the project agreement long enough to warrant the effort?

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5. Key negotiating points

- **Information in the Enforcement Notice**

- Lenders seek detailed information in enforcement notice, including:
 - sufficient information to enable Security Agent to identify material facts
 - steps required to remedy specific breaches
 - time within which specific steps are expected to be taken
 - relief sought, including estimate of project company's liabilities to counterparty
- Counterparties seek to limit notice to the information they would provide to the Project Company, and to limit any warranty of accuracy

- **Obligation to update information statements**

- Lenders may ask counterparties to regularly update them on the project company's obligations to the counterparty.
- Counterparties seek to limit obligations to update, but may ask for an affirmative right to update.

5. Key negotiating points

- **Waiver of un-notified claims**

- Lenders typically seek a provision that waives claims the counterparty did not include in information statements
- Counterparties seek to limit the waiver to the Appointed Representative (not the Project Company)

- **Length of Suspension Period**

- 90 days (or more) is typical
 - Lenders ask for longer periods, counterparties for shorter periods
 - Length of period ultimately determined by the realities on the ground
 - Lenders ask for period to begin when notice received, not when dispatched
- Counterparty will resist obligation to standstill for long periods
 - Less of an issue in jurisdictions with an automatic stay for insolvent companies

5. Key negotiating points

- **Remedy Periods**

- If Lenders appoint an Appointed Representative, it must cure defaults
- Lenders ask for longer cure periods, counterparties ask for shorter cure periods

- **Choosing the Substitute**

- Typical lender position
 - a party that, in the Lenders' reasonable opinion, has sufficient legal capacity, power and authority, appropriate experience, technical competence and financial standing to replace the project company
- Typical counterparty positions
 - consent rights
 - objective standard regarding financial and technical capabilities
 - may desire to exclude competitors or potential litigants
- Rating requirements not typically appropriate in project finance context

5. Key negotiating points

- **Amendments to project documents**
 - Direct Agreements often correct errors or omissions in project agreements
 - Amendments should survive expiration or termination of Direct Agreement
 - Third party transferee will want amendments to survive
- **Restriction on Amendments**
 - Restriction on amendments should not prohibit variation under EPC contracts
 - Caps on dollar amount of variations are useful
- **New Direct Agreement**
 - Lenders ask for undertaking from counterparty to enter into new direct agreement on substantially the same terms in connection with:
 - a refinancing, or
 - a transfer to Substitute

5. Key negotiating points

- **Security Agreement**

- Counterparty may ask to review underlying security agreement
- Consider stand alone security document for relevant material project document

- **Cure of non-monetary defaults**

- Curing non-monetary defaults may require Lenders to take possession of the project
- Lenders will request a longer standstill and cure period to allow for foreclosure or novation
- Counterparty will insist on cure of monetary defaults upon completion of foreclosure proceedings

5. Key negotiating points

- **Cure of Defaults existing prior to Step-in**
 - Counterparties are successful in securing Lender's obligation to cure (notified) defaults existing prior to the Step-in Date as a condition to (or within agreed period after) stepping-in
 - Counterparty is receiving a benefit as a result of the Lender's step-in (continued payments, deliveries, survival of the project company) and its rights against the project company arising as a result of the Default are preserved
 - Lenders may limit exposure to post step-in obligations as counterparty is no worse off and recovery of defaulted amounts would be additional benefit
- **Availability of Borrower funds**
 - Lenders should ensure that borrower funds (reserve accounts) are available to lender to cure payment defaults
 - Requires alignment of loan agreement defaults with defaults under project documents

5. Key negotiating points

- **Suspension Rights**

- Counterparties may:

- negotiate for suspension rights if Step-in Period exceeds a defined period, or
- require separate stand alone right to suspend performance

- **Transfer restrictions arising by law**

- Consider restrictions on transfer of project agreement in the context of

- licenses and permits
- procurement law

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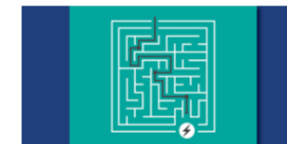
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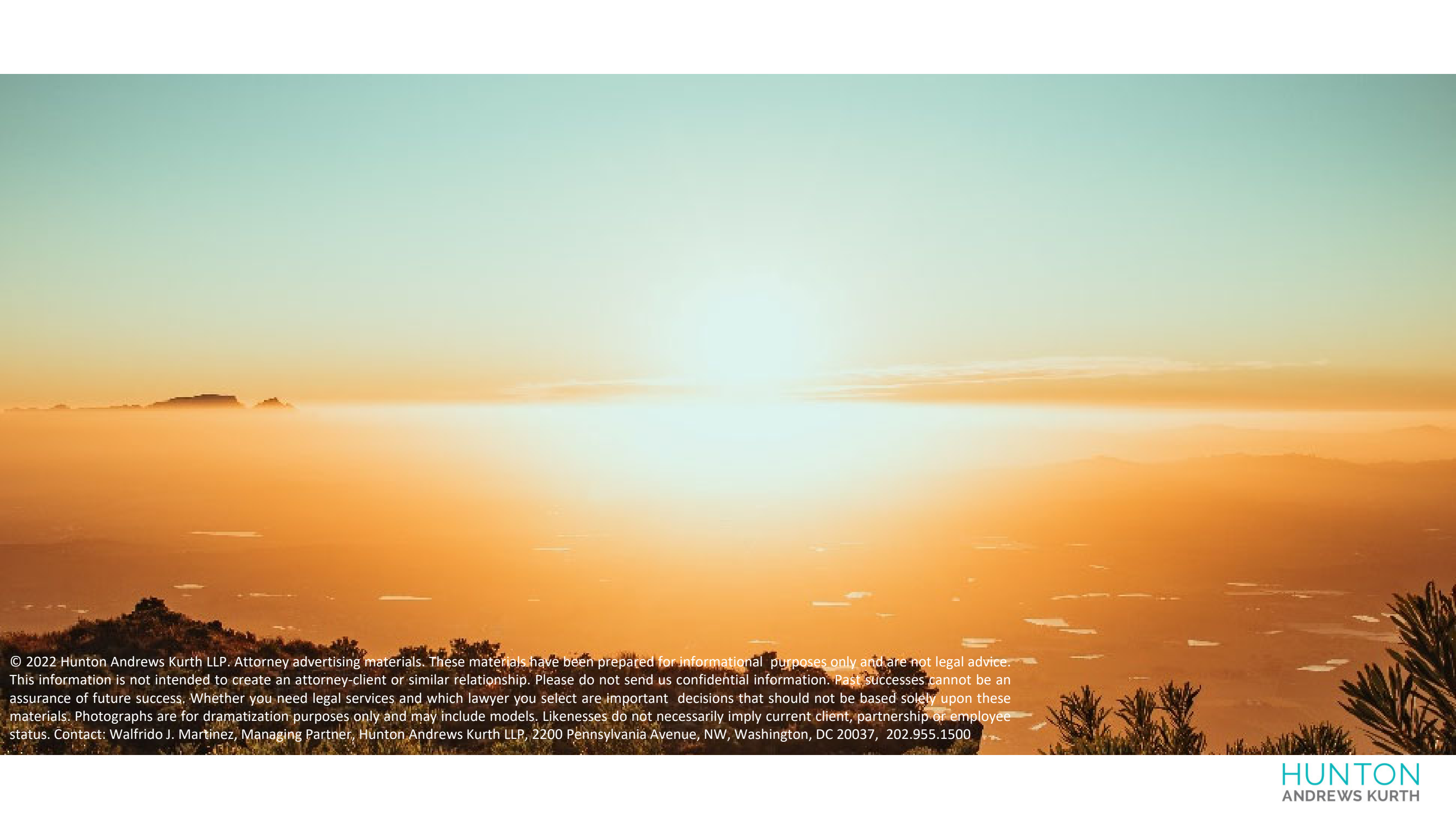


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