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United Kingdom

PROJECT FINANCE

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This country-specific Q&A provides an overview of project finance laws and regulations applicable in United Kingdom.

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UNITED KINGDOM
PROJECT FINANCE

1. What are the typical ownership structures for project companies in your jurisdiction? Does this vary based on the industry sector?

In the UK a project company is commonly incorporated as a private limited company, often owned by a holding company whose only function is to hold shares in the project company and to act as a conduit for the provision of equity to the project. This structure allows the project's owners (commonly referred to as sponsors) to limit their future liability if a project fails to perform commercially and the project company becomes insolvent. In the UK it is common for a nominal amount of share capital to be subscribed for in a project company, with equity contributions effectively being made by way of shareholder loan(s). Joint venture participants frequently use a project company or holding company as this structure allows joint ventures to be managed cleanly pursuant to agreed contractual arrangements using shareholders' agreements. The use of a holding company facilitates the granting of share security over a project company's shares to a project's lenders, while allowing the sponsor group more freedom to transfer shares at the level of the holding company. However, it is common for lenders to include contractual restrictions on sponsors' disposal of their interests in a holding company, party to ensure that the project company is being managed by a sponsor with experience of the project, but also because they need to comply with regulatory 'know your client' requirements in the event of a change of control.

One advantage of using a holding company structure is that sponsors may have more flexibility to transfer portions of the equity in a project indirectly at the holding company level than they would have at the project company level, since the holding company's shares are outside the security ring fence which exists around the project company. Holding companies are also popular for sponsors who plan to develop a pipeline of projects and wish to bring the project company for each future project under common ownership. Although lenders may include contractual restrictions on the proportion of a sponsor's interest that may be transferred without lender consent, it is common for some portion of a minority interest to be transferable to an approved investor subject to 'know your client' approval from the lenders.

2. Are there are any corporate governance laws or accounting practices that foreign investors in a project company should be aware of?

Holding companies and special purpose vehicles are subject to the same legal framework as other commercial companies in England and Wales.

Since 4 January 2022 the National Security and Investment Act 2021 (the **NS&I Act**) established a new regime for government approval of transactions that may give rise to a risk to national security. There are 17 designated sectors, ranging from energy, transport and advanced robotics to cryptographic authentication and synthetic biology to which the NS&I Act applies. The NS&I Act is primarily targeted at acquisitions of qualifying entities or assets but it could have implications for financing, especially secured lending transactions such as project finance. Funders and borrowers will need to carry out analysis of their security package (including security over shares and key contracts) to manage the risk of enforcement triggering a breach of the NS&I Act provisions relating to notification.

The NS&I Act contains both a mandatory notification regime and a voluntary notification regime. It also grants the secretary of state for Business, Energy and Industrial Strategy (**BEIS**) (the **SoS**) the power to call-in a transaction for review if they reasonably suspect that a change of control (which could include the acquisition of 'material influence') over a target may give rise to a national security risk.

Under the mandatory notification regime, a potential investor must notify BEIS before they acquire an interest

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(which may be as low as a shareholding of 25%) or increase their interest in a qualifying entity or asset.

An investor may make a voluntary notification to the ISU before it acquires or increases its interest in an entity or asset outside of the 17 sensitive sectors in order to obtain approval for the transaction and avoid the risk of a transaction being called-in by the SoS. The SoS is able to make an interim order or a final order under the NS&I Act to prevent or prescribe aspects of a proposed transaction if a risk to national security would arise from it or otherwise approve the transaction.

Breach of the NS&I Act may result in criminal and civil sanctions. It is a criminal offence for an investor to complete an acquisition that is subject to the mandatory notification regime without approval from the SoS, unless they have a reasonable excuse. Failure to notify BEIS of a transaction that falls within the mandatory notification regime will result in that transaction being deemed void. An investor may apply to the SoS for a validation notice in relation to such a transaction which, if it is granted, will mean the transaction is approved by the SoS and not void. Breaches of the NS&I Act may also result in imprisonment of up to 5 years and fines of the higher of 5% of total worldwide turnover of the investing business or £10 million.

There are *de-facto* local content requirements in some sectors of the UK economy. Commonly for renewable energy projects over 300MW a supply chain plan is required. Delivery of a supply chain plan is a requirement for sponsors who bid for a contract for different (**CfD**), which is one of the main routes to market for large renewables energy projects such as off-shore wind farms. A sponsor's supply chain plan must set out how they will use domestic UK products in their project and it must pass scrutiny from the BEIS as part of the CfD allocation process.

3. If applicable, what forms of credit support from sponsors or host governments are typically provided?

Project sponsors may be required to provide bonds or letters of credit and/or parent company guarantees to support the obligations of a project company generally or their own obligation to contribute equity to a project specifically.

Private investment opportunities in UK infrastructure are generally found in consumer funded sectors of the economy such as energy and digital infrastructure rather than schools, hospitals and prisons as used to be the case when the UK promoted the Private Finance Initiative (**PFI**). PFI is no longer used for new projects although legacy projects continue to operate.

One area in which project finance is still commonly used in UK infrastructure projects is in the renewable energy space. The main route to market for large renewable energy projects is a contract for difference (**CfD**) between a generator and an entity called the Low Carbon Contracts Company (**LCCC**).

A CfD is a contract designed to provide a generator with price certainty for the power it sells over a long period of time, such as 15 years. The CfD is awarded through a competitive process between bidders to determine a strike price for a given CfD. Project finance lenders and sponsors need certainty that payments due under the CfD will be made and that the LCCC, as a private company, will always have the resources needed to satisfy its obligations.

The LCCC is private limited company, wholly owned by the Secretary of State for Business, Energy and Industrial Strategy but its creditworthiness, as a contractual counterparty, does not come from any direct form of credit support to LCCC or to the generator it contracts with. Instead, payments due from the LCCC under CfDs are funded by electricity suppliers pursuant to regulations they are subject to. The LCCC sets the levy due from electricity suppliers on a quarterly basis, as well as a reserve amount, and this structure ensures that no form of additional credit support is required by generators or their lenders.

In addition to CfDs for renewable energy projects, investors in UK infrastructure should be aware of the UK Guarantee Scheme which is a form of guarantee historically provided by the UK Treasury to guarantee a project company's repayment obligations but which is now administered by the recently created UK Infrastructure Bank (which is owned by the UK Treasury). Only nine guarantees were issued under the UK Guarantee Scheme between 2012 and 2021 when responsibility was moved to the UK Infrastructure Bank and whereas the scheme was previously open to a wide range of infrastructure projects (provided they were deemed to be nationally significant) it is worth noting that it will be subject to the UK Infrastructure Bank's investment principles, the second of which states that they "will prioritise in particular clean energy, transport, digital, water and waste". As noted above, these are consumer funded sectors.

4. What types of security interests are available (and suitable) for a project

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financing in your jurisdiction?

English law allows for a trustee to hold security and it is common on project finance transactions to appoint a security trustee to hold security for the benefit of a single lender or a group of lenders. Generally, a project company will grant a composite debenture to the security trustee, for the benefit of its lenders, containing a fixed and floating charge over all of its assets, including its bank accounts and a mortgage over its real estate (described in the Law of Property Act 1925 as a "charge by deed expressed to be by way of legal mortgage") together with an assignment of its contractual rights. In addition, the project company's shareholder(s) will generally grant a charge over the project company's shares in favour of the lenders and assign or charge their rights under any shareholder loan agreement between themselves and the project company. Guarantees are frequently used to provide credit support and are often coupled with indemnities to reduce the risk of a guarantor avoiding liability on technical grounds under the guarantee.

5. How are the above security interests perfected?

Because the creation of a legal mortgage requires a transfer of title under English law it is more common for security to be taken by way of a charge or legal assignment. Mortgages over land are an exception to this rule because, due to the Law of Property Act 1925, there is usually no transfer of title, instead, a charge by way of legal mortgage is created. Charges and mortgages must be registered pursuant to the Companies Act 2006. This requirement also applies to assignments by way of security. Although registration may be argued to constitute constructive notice, it is in the beneficiary's best interest for a notice of charge to be served on the counterparties to charged or assigned contracts. Legislation also requires the registration of charges and mortgages over certain classes of asset (eg, land, ships and aircraft) in asset registers. A guarantee is a contractual agreement and there is no requirement for a guarantee to be embodied in a deed, but it is relatively common for parties to do so in order to avoid any arguments about the enforceability of the guarantee on the grounds of lack of consideration. There is no requirement to register a guarantee.

6. Please identify how security is enforced (notably the enforcement options available for secured parties) both pre and post insolvency/bankruptcy of the project company?

The purpose of security in a project finance context is primarily defensive as well as to set out the lenders' rights on enforcement. By taking first ranking security, lenders can frustrate the efforts of unsecured creditors who would otherwise seek to bring claims against a project company in a way that would harm the lenders' long-term prospects. Enforcement action may ultimately be required in some cases and the security documents in a project finance transaction will set out the lenders' remedies including:

- appointing an administrator or administrative receiver (where permitted – see below);
- taking possession of or selling the assets of the project company; or
- exercising rights of set-off.

The Financial Collateral Arrangements (No 2) Regulations 2003 permit the beneficiaries of security over cash and financial instruments, including shares, to enforce their security interests without needing the consent of an administrator or the permission of the court.

More generally, the lenders' ability to appoint an administrator out of court, as qualifying floating charge holders, gives them the power to trigger an enforcement freeze which, subject to the provisions of the regulations, applies to all creditors.

There are specific statutory provisions that apply in the event of the insolvency of a project company, known as the 'project finance exceptions'. They are exceptions to the general regime of administration, which is one of the standard ways of dealing with an insolvent company. When an administrator is appointed to control a company, its objective is to rescue the company or achieve the best outcome for its creditors as a whole. Where the project finance exceptions apply, the lenders to an insolvent project company may appoint an administrative receiver and block the appointment of an administrator, allowing them to prioritise their interests over other creditors and control the insolvency process to realise the value of their security. The project finance exceptions are limited in scope and normally apply only to larger projects with debt requirements of £50 million or more; but they provide a degree of comfort to lenders that would otherwise struggle with the risk profile of a non-recourse project finance structure.

7. What are other important considerations in relation to the security regime in the jurisdiction that secured parties should be

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aware of?

The beneficiaries of security (usually lenders in a project finance context) and their advisers must observe the statutory time limits for registration of security, as failure to do so may result in security being invalid. It is important to correctly identify the thing over which security is being taken, to avoid any risk of security being circumvented through misidentification of the thing it was intended to cover. It is also essential to review the lenders' security arrangements in the event of any material change to the financing of a project – for example, following an increase to the amount of a loan facility. This is because a significant change to the financing arrangements could result in the charges or guarantees being deemed to be discharged if it is determined that increasing the secured obligations took them outside of the purview of the original security documents or guarantees. It is advisable for the lenders to obtain confirmation of security or retake security in the event of any significant change to the secured obligations.

8. What key project risks should lenders be aware of in project financings in your jurisdiction? This may include, but may not be limited to, the following risks: force majeure, political risk, currency convertibility risk, regulating or permitting risk, construction/completion risk, supply or feed stock risk or legal and regulatory risk).

During the construction phase of a project the key risks are:

- delays;
- cost overruns;
- sub-standard performance;
- new technology risk; and
- ground risk.

The mitigants for these risks include:

- comprehensive due diligence by a technical adviser;
- use of proven technology and an experienced contractor;
- use of a turn-key contract;
- risk allocation to insulate the project company from risk;
- liquidated damages and bonus payments to incentivise the contractor;
- staged payments; and

Other key risks include:

- interest rate risk, which may be hedged; and
- key counterparty credit risk, especially for a long-term offtaker, which may be managed by including a ratings trigger and termination rights allowing for their replacement if their financial status deteriorates or credit support in the form of bonds or letters of credit and/or parent company guarantees.

Some risks – such as a change in law resulting in the removal of subsidy support – is harder to mitigate effectively and lenders will have to take a view on the likelihood of such an event taking place. The United Kingdom is historically not prone to retrospective removal of subsidies, although it has cut subsidies in relation to renewable energy generation on a prospective basis.

To the extent that a force majeure event renders performance under a contract impossible, through no fault of the parties, the English common law doctrine of frustration may in certain circumstances be invoked, resulting in the immediate termination of the frustrated contract. In a project finance context, the allocation of risk relating to force majeure is commonly dealt with by negotiated agreement between the project company and the entities it contracts with. Sponsors and lenders are broadly aligned in wishing to insulate the project company from the risk of immediate termination of a contract due to the occurrence of a force majeure event. It is therefore normal if force majeure occurs for performance obligations to be suspended (for a limited period of time) while the parties try to find a way to remedy the situation, after which the contract may be terminated if no remedy is found. Force majeure provisions do not generally apply to payment obligations.

There is always the possibility in the UK that a government will pass legislation to nationalise a project or take it into public ownership. In 2017 the UK Labour Party manifesto proposed to take rail companies, energy companies and water companies into public ownership. Historically, this kind of nationalisation has taken place before, notably between 1946 and 1951, when the Bank of England, hospitals, coal mines, electricity companies, railways, gas companies and iron and steel companies were all nationalised. In these cases, the owners of the companies were compensated by reference to the market value of their companies.

The impact on investors in a nationalised project may differ depending upon whether they are British or foreign. The United Kingdom has signed bilateral investment treaties (**BITs**) with over 100 other countries

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providing the people from those countries with protection from illegal nationalisation and expropriation of foreign assets in the UK. As such, foreign owners or investors whose assets were nationalised would be entitled to compensation pursuant to the terms of their applicable BIT. UK investors would not benefit from the same protection as investors from countries that had signed a BIT and their compensation would be calculated pursuant to the legislation under which their assets were nationalised. As such, sponsors consider the jurisdiction of any holding company or investment vehicle not just from a tax perspective but also to provide BIT protection.

The United Kingdom has no exchange controls. As a general rule, an English company can maintain an offshore bank account, provided that doing so is not otherwise prohibited by law, such as by UK sanctions regimes.

9. Are any governmental / regulatory consents required and are any financing or project documents requirement to be filed with any authority in order to be admissible in evidence in a court of law, valid or enforceable?

Project finance is widely used by the sponsors of projects in regulated industries such as energy generation, digital infrastructure, water and waste. Those project companies will be subject to the regulatory regimes applicable to their industry.

For example, a project company generating electricity from a grid-connected onshore wind farm will be regulated by the Gas and Electricity Markets Authority via the Office of Gas and Electricity Markets (Ofgem), who have the power to impose financial penalties and prosecute companies that commit certain offences. Ofgem is also responsible for administering schemes such as:

- the Renewables Obligation, under which it was historically responsible for accrediting generating stations and issuing certificates; and
- the Offtaker of Last Resort scheme, which enables eligible renewable energy generators to enter into a backstop power purchase agreement with a licenced supplier if they are unable to enter into a power purchase agreement otherwise.

There are similarly regulators for telecoms (Ofcom), water services (Ofwat) and nuclear (Office for Nuclear Regulation), and others that are responsible for specific industries in which project financed projects may operate.

10. Are there are any specific foreign exchange, royalties, export restrictions, subsidies, foreign investment, that are relevant for project financings (particularly in the natural resources sectors)?

As noted in question 3 above, UK Government policy has moved away from using PFI to deliver infrastructure for public services in the areas of health, transport, education, prisons and housing. These areas were previously ones in which PFI were commonly used, but they have fallen out of favour and the UK government is now actively encouraging private capital into consumer-funded projects, principally green energy and digital infrastructure.

As such, the principal areas for project finance in the United Kingdom are:

- wind farms (principally offshore, but with onshore returning in importance);
- solar photovoltaic;
- battery energy storage systems;
- energy from waste;
- fibre networks; and
- potentially hydrogen projects in future.

The UK oil and gas fiscal regime taxes profits earned by companies from the production of oil and gas in the UK and on the UKCS. The regime is kept separate to other taxes on commercial profit by the operation of a “ring fence” which prevents losses from other activities being imported into the regime. Following an increase in oil and gas prices after Russia’s invasion of Ukraine in early-2022, in mid-2022 an additional 25% levy was applied to the ring fenced profits of oil and gas companies. Such companies are also subject to an additional rate of corporation tax (of 30%) and a supplementary charge (of 10%) in relation to ring fenced profits. Some of these additional taxes may be set off against qualifying investments.

11. Please set out any specific environmental, social and governance issues that are relevant. For example, are project companies subject to certain ESG laws, reporting requirements or regulations?

Within their finance documents some lenders place an obligation on borrowers to comply with requirements

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known as Equator Principles to manage environmental and social risks.

The environmental regulator for England is the Environment Agency (**EA**), which was created under the Environment Act 1995. The EA regulates major industry and waste, treatment of contaminated land and water management, including flood risk. The EA has wide-ranging investigatory powers as an environmental regulator and enforcement powers, including the power to issue fines, stop notices, compliance notices and restoration notices. The EA also has the power to prosecute environmental offences.

The Health and Safety at Work etc Act 1974 sets out the principal legal framework for occupational health and safety in the United Kingdom. Health and safety infringements are primarily enforced through criminal law. The Health and Safety Executive is responsible for the enforcement of employers' obligations to provide a safe work environment. Since project companies generally do not employ staff directly, the obligations relating to health and safety are placed on the companies employed by the project company. The directors of a project company should still ensure that all activities at the site of the project are carried out in accordance with health and safety laws. There is the potential risk of individual liability for a company director whose company is found guilty of a health and safety offence.

12. Has any public-private partnership models or laws been enacted in the jurisdiction, and if so, are they specific to certain industry sectors?

Since the United Kingdom no longer uses PFI as a means to procure infrastructure for public services (see question 3 above) the role of the state in most project financings is limited to matters of planning and regulatory compliance of the project company. There are exceptions such as in relation to the negotiation of contracts for difference (**CfDs**), which are used to provide stable predictable revenue streams to energy projects that would otherwise not be economically viable, such as the Hinkley Point C nuclear power station. The main route to market for large renewable energy projects is a CfD between a generator the Low Carbon Contracts Company (**LCCC**). Similar concepts to the CfD are being used in areas beyond low carbon electricity generation such as carbon capture utilisation and storage and low carbon hydrogen projects.

The LCCC will be used in much the same way as for low carbon power generation to contract with owners of gas fired power stations to facilitate the installation of carbon capture plants to their power stations. They will also contract with owners of industrial plant in energy intensive sectors such as cement, steel and petrochemical manufacturing to do the same. LCCC is also developing a similar scheme for the production of low carbon hydrogen.

13. Will foreign judgments, arbitration awards and contractual agreements to arbitrate be upheld?

Pursuant to the Civil Jurisdiction and Judgments Act 1982, judgments from courts in Scotland or Northern Ireland can be enforced in England and Wales.

The enforcement of judgments from the European Union, European Free Trade Association states, Mexico, Singapore and Montenegro is governed by the Hague Convention on the Choice of Court Agreements, where applicable. Judgments from other countries, and judgments to which the Hague Convention does not apply may be enforceable in English courts pursuant to the Administration of Justice Act 1920, the Foreign Judgments (Reciprocal Enforcement) Act 1933 and under the common law. However, the judgment debtor may be required to commence fresh proceedings before an English court to enforce the foreign judgment as a debt.

The United Kingdom has been a signatory to the Convention on the Recognition and Enforcement of Foreign Arbitral Awards, also known as the New York Convention, since 1975. The New York Convention provides a regime for the enforcement of arbitral awards in contracting states. Over 157 states are signatories to the New York Convention. In light of the uncertainty around the enforcement of foreign judgments, there are considerable advantages to the use of arbitration as a means of dispute resolution in cross-border commercial contracts.

14. Is submission to a foreign jurisdiction and waiver of immunity effective and enforceable?

If an English company enters into a contract that is governed by foreign law and is subject to foreign jurisdiction, the validity or enforceability of that contract will be a matter for the applicable foreign jurisdiction. Enforcing a foreign judgement against an English company is addressed in the paragraph above. Security documents are generally governed by the law of the jurisdiction in which the thing that is being secured is located (the *lex situs*), although there are complicating

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factors to be considered in relation to cross-border security. EU Regulation 593/2008 (**Rome I**) continues to apply following the United Kingdom's departure from the European Union as retained EU law. Rome I provides that the applicable law of a contract is without prejudice to the overriding mandatory provisions of the law of the forum. 'Overriding mandatory provisions' are defined as "provisions the respect for which is regarded as crucial by a country for safeguarding its public interests, such as political, social and economic organisation, to such an extent that they are applicable to any situation falling within their scope, irrespective of the law otherwise applicable".

So-called 'asymmetric jurisdiction' clauses – under which a borrower is required to bring proceedings in only one jurisdiction, whereas the lenders have the choice to bring proceedings in other jurisdictions – are common in project finance agreements.

English courts will give effect to the consensual waiver of immunity by a state. Where a state entity enters into a commercial arrangement, it will not generally be entitled to sovereign immunity. Under the State Immunity Act 1978, there are a number of exceptions to the general proposition that UK courts have no jurisdiction to adjudicate disputes against sovereign states, as follows:

- The state has submitted to the jurisdiction of the UK courts;
- The proceedings relate to a commercial transaction entered into by the state;
- The proceedings relate to a contractual obligation on the state to be performed in the United Kingdom; and
- The state has agreed to submit the dispute to arbitration.

15. Please identify what you consider to be (a) the key current issues for project financing in your jurisdiction; and (b) any emerging trends or topics which should be considered or focused on by project financing stakeholders.

Following the phase-out of the London Inter-Bank Offered Rates (LIBOR) for Sterling at the end of 2021, the Sterling loan market has transitioned to the Risk-Free Rate (RFR) known as the Sterling Overnight Index Average (SONIA). Although US Dollar LIBOR will not be phased-out until 30 June 2023 it is no longer recommended for new loans for which the applicable RFR for US Dollar loans is the Secured Overnight Financing Rate (SOFR). The Sterling loan market has established norms for the calculation of interest in arrears for UK projects. The US Dollar debt market in the UK is moving in a different direction to that which is taken by many lenders and borrowers in the US (and in many emerging markets). US Dollar loans in the UK are largely following the approach of the Sterling market by calculating interest in arrears whereas in the US such loans are commonly structured to calculate interest on a forward-looking basis using Term SOFR. It is possible that the UK's US Dollar loan market will also move over time to follow the approach taken in the US.

Following the project financing of the first battery storage projects in the United Kingdom, we expect to see the number of such projects grow rapidly as contractual routes to market proliferate.

The use of blockchain as a technology to facilitate the management of corporate power purchase agreements for renewable energy, especially in the context of a club deal, will be interesting to watch, as automation will inevitably increase efficiencies and improve competitiveness for market participants.

The inclusion of onshore wind and solar in the contracts for difference (CfD) auctions going forward is anticipated to result in highly competitive pricing and may paradoxically stimulate the merchant market for both technologies depending upon how the CfD strike compared to wholesale power prices. Structuring such merchant power projects to ensure bankability will be a key element in such a development.

Floating offshore wind is still in its infancy but it is growing up rapidly. It has moved beyond being theoretical and new projects are being built. In 2022 BW Ideol, TotalEnergies and Qair reached the final investment decision for the EolMed project, a 30MW offshore floating wind farm in the French Mediterranean. Further afield, in Japan, the first floating wind farm in that region will feature eight hybrid spar-type floating foundations delivering 16.8MW of power.

2022 was a tumultuous year for the energy sector and, although renewable energy is more important than ever, the market remains unstable. The large rise in oil and gas prices, driven by geopolitical shocks, caused a sharp increase in electricity prices and a regulatory response in the form of new taxes on oil and gas companies' profits as well as a new tax on the revenues (above a threshold of £75/MWh) of some renewable electricity generators. The rationale for taxing renewable electricity generators is that they are unduly profiting from much higher revenues from the electricity they are selling whilst not incurring any additional fuel costs in the case of wind and solar power. The government initially sought to persuade renewable generators to switch to fixed price contracts for difference (CfDs) to bring electricity prices

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down but were unsuccessful in doing so. It is noteworthy that the new tax on renewable electricity generators can be avoided by generators who agree to a CfD in future.

16. Please identify in your jurisdiction what key legislation or regulations have been implemented (or will / plan to be) for projects in connection with the energy transition?

As noted in question 12 above, the Low Carbon Contracts Company (**LCCC**) will enter into contracts called Dispatchable Power Agreements (draft terms of which were published in November 2022 by the Department for Business, Energy and Industrial Strategy) in much the same way as LCCC enters into CfDs for low carbon power generation to contract with owners of gas fired power stations to facilitate the installation of carbon capture plants to their power stations. LCCC also plan to contract with owners of industrial plant in energy intensive sectors such as cement, steel and petrochemical manufacturing to do the same and they are developing a similar scheme for the production of low carbon hydrogen.

A Bill (The Energy Security Bill) is currently passing through the UK Parliament and is (at the time of writing) expected to be passed into law during 2023. This legislation will cover energy production and security and the regulation of the energy market including provision about: the licensing of carbon dioxide transport and storage; commercial arrangements for industrial carbon capture and storage; hydrogen production; new technologies, including low-carbon heat schemes and hydrogen grid trials. The new act is expected to regulate an Independent System Operator and Planner and amend gas and electricity industry codes, make provision for heat networks, energy smart appliances and load control and the energy performance of premises. The new law is also likely to contain provisions relating to the resilience of the core fuel sector, offshore energy production (including environmental protection, licensing and decommissioning) and the civil nuclear sector including the Civil Nuclear Constabulary.

17. Please identify if there are any material tax considerations which need to be taken into account for a project financing in your jurisdiction, and if so, how such tax issues can be mitigated.

There are no project finance specific taxes in England and Wales. Subsidies have historically been made available to support certain types of project, the economics of which would not otherwise have been sustainable e.g. for renewable power generation. Although these subsidies were not directly linked to the structure of a project they were well suited to project finance and it is likely that they were tailored at least in part to take account of the needs of sponsors and lenders who would be likely to use project finance.

As with any kind of corporate endeavour there have been examples of sponsors and their advisers seeking to deploy aggressive tax schemes on project finance transactions. However, in our experience, lenders will be wary of funding projects that use such schemes both for reputational reasons and because of the risk associated with such schemes being successfully challenged by the UK's tax authorities.

As noted in question 14 some of the kinds of projects that are commonly project financed in the UK, such as wind and solar power projects operate in a politically sensitive sector and when external shocks take place, such as large increases in power prices, the regulatory response may be to tax their profits more highly than was anticipated when the projects were originally structured.

18. What types of funding structures (e.g. debt, equity or alternative financing) are typical for project financing in your jurisdiction. For example, are project bond issuances, Islamic finance and – in the context of mining deals – streams or royalties, seen as attractive (and common) options for stakeholders?

The key structuring considerations for sponsors developing a project include:

- maximisation of tax efficiency;
- limitation of liability;
- ease of realisation of profits; and
- the ability to transfer ownership of a project at a later date.

Lenders will be keen to ensure that they have security over all of the assets and rights relating to a project.

It is common for sponsors to incorporate a special purpose vehicle (SPV) for a project that it will project finance. The SPV share capital is often nominal (there are no "thin cap" restrictions in England and Wales) with equity contributions effectively being made by way of shareholder loan(s). The use of a holding company facilitates the granting of share security over a project

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company to the project's lenders protecting the lenders and this also insulates the sponsor from downside risks the project company may incur.

A number of models are favoured by sponsors, including:

- traditional project finance from commercial banks;
- private placements or project bonds issued to institutional investors such a life insurers and pension funds; and
- hybrid products combining the use of commercial bank debt and funding from non-bank lenders.

19. Please explain if there are any regional development banks or export credit agencies, and if so, what is their role in project financing in your jurisdiction and beyond.

As noted in question 3 above, the UK Infrastructure Bank (which is wholly owned by the UK Treasury) provides funding and guarantees for infrastructure projects subject to its investment principles, the second of which is that they "will prioritise in particular clean energy, transport, digital, water and waste".

The British Business Bank is a state-owned economic development bank established by the UK Government. Its aim is to increase the supply of credit to small and medium enterprises as well as providing business advice services. It is owned by the UK's Department for Business, Energy and Industrial Strategy.

The UK government has announced a £105 million funding package through its Net Zero Innovation Portfolio to act as a first step towards building the UK's low carbon hydrogen economy. The funding package takes the form of various grants to businesses and developers to support, for instance, the development and trials of solutions to switch industry from high to low carbon fuels such as natural gas to clean hydrogen.

In addition, in April 2022, the British Energy Security Strategy was published which outlined the government's plan to double its hydrogen production target from 5GW to 10GW by 2030. In order to meet this target, the Net Zero Hydrogen Fund ("NZHF") was announced whereby £240 million of available funding will be distributed to eligible low carbon hydrogen projects across four strands – which strand a project can apply for depends on its maturity and the level of support required:

- Strand 1: DEVEX support for early projects to cover front end engineering design (FEED) studies and post-FEED studies
- Strand 2: CAPEX for projects that do not need a hydrogen business model ("HBM") – a project applying for this strand must exist on its own merit and solely require CAPEX support
- Strand 3: CAPEX for projects requiring an HBM
- Strand 4: CPEX for carbon capture usage and storage ("CCUS") projects requiring an HBM

The HBM is a financial support mechanism incorporated into strands 3 and 4 and is designed to subsidize operational costs to encourage and support the hydrogen market – it is provided together with funds granted through the NZHF as a long-term revenue support contract.

20. Please explain if there are any important insurance law principles or considerations in connection with any project financing in your jurisdiction.

During the construction phase of a project, the following insurances are generally required:

- construction all risks insurance;
- delay in start-up insurance;
- third-party liability insurance;
- directors' and officers' liability insurance; and
- compulsory insurance such as vehicle insurance (if applicable).

During the operating phase of a project, the following insurances are generally required:

- property all risks insurance;
- business interruption insurance;
- third-party and products liability insurance;
- directors' and officers' liability insurance; and
- compulsory insurance such as vehicle insurance (if applicable).

Lenders generally require to be named as co-insured beneficiaries under the construction all risks insurance, delay in start-up insurance, property all risks insurance, business interruption insurance and third-party and products liability insurance.

Warranty and indemnity insurance is relatively commonplace in the UK M&A market. There are times when a project financing transaction runs parallel with the acquisition of a project company that lenders seek to introduce exceptions to the non-recourse project finance structure. If the sponsor, in its capacity as the buyer of a project company, successfully claims damages from the developer which sold them the project company under a

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sale and purchase agreement, those damage may be paid by the insurer that provided warranty and indemnity insurance. The project finance lender may argue that those insurance proceeds should be used to pre-pay the project company's loans because the damages represent compensation for the reduction in value of the project company and therefore their exposure to the project company as a borrower should be reduced by that amount. Sponsors may argue that this goes against the principle of non-recourse project finance, since the proceeds of the warranty and indemnity insurance are not paid to the project company, and there may be no connection between the damages payable to the sponsor under a sale and purchase agreement and the ability of the project company to operate its business.

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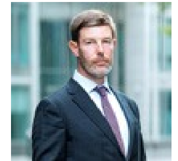

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