

GEDİK & ERAKSOY

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New Debt Assumption Regulation

Speed read

The Regulation on Debt Assumption by the Treasury (the **Regulation**) was published in the Official Gazette dated 19 April 2014. Under the Regulation, the Undersecretariat of Treasury (the **Treasury**) may enter into debt assumption arrangements with lenders to certain PPP projects. Under such debt assumption agreements, the Treasury can agree to assume the debt obligations owed by project companies to their senior debt providers in circumstances where the underlying concession is terminated. The Regulation applies to projects tendered under:

- Law No. 3996 on Procurement of Certain Investments and Services through Build-Operate-Transfer Model;
- Law No. 6428 on Construction, Renovation and Procurement of Services by the Ministry of Health under Public Private Partnership Model and Amendment of Certain Laws and Decree Laws; and
- Decree Law No. 652 on the Organisation and Duties of the Ministry of Education.

To be eligible for debt assumption by the Treasury, the investment amount of: (i) BOT projects tendered under Law No. 3996 must be at least TL1,000,000,000; and (ii) healthcare and educational PPP projects must be at least TL500,000,000.

However, the Regulation does not extend the scope of applicability of debt assumption by the Treasury and would not be applicable to the new airport project and the healthcare PPP projects which were tendered in accordance with Law No. 3359 since Treasury debt assumption is not provided under their tender specifications.

Such understanding is confirmed by the Treasury in its press release dated 28 April 2013. In the press release the Treasury clarifies that it is not possible for the Treasury to extend debt assumption for the projects implemented by the state owned enterprises and local administrations because, the Treasury is entitled to assume the debts in the projects where the contracting authority is either general or special budgeted institutions. The Treasury also emphasises that as the draft implementation contracts are part of the tender specifications which are known by all bidders, the bidders are informed whether or not there will be debt assumption by the Treasury at the tendering stage. Consequently, any debt assumption (i) which is not provided at the tender stage and (ii) which may cause unjust advantages by altering terms of the tender cannot be committed by the Treasury.

Finally, the procedures and principles set forth under the Regulation do not apply to assumption of debt by any authority other than the Treasury.

The most notable provisions of the Regulation relate to the assumption limits and the parties' notification and monitoring obligations. Many of the procedures and principles set forth under the Regulation have already been implemented by the Treasury in practice; however, compiling these procedures and principles under a single piece of legislation would help to clarify the debt assumption process.

Main Provisions

Assumption Limits and Scope of Assumption

The first assumption limit specified under the Regulation relates to the debt assumption undertaking of the Treasury. As per the Regulation, the Treasury can undertake to assume: (i) 85% of the senior facility, in cases of termination of concessions due to project company's fault; and (ii) 100% of the senior facility, in cases of events of default resulting from events other than the project company's fault.

The second limitation relates to the exposure of the Treasury under derivatives. Although Law No. 4749 on Regulation of Public Financing and Debt Management, which is the primary piece of legislation governing debt assumption, does not provide any limits with respect to the type and cost of derivatives, the Regulation caps the amount of derivative costs at a maximum of 10% of the senior facilities. Moreover, the Treasury would only assume the costs of currency and/or interest rate derivatives.

The Regulation also excludes loans to be obtained for the financing of (i) equity; and (ii) cost increases occurred due to the project company's fault, or the cash shortfalls of the project company incurred by the scope of the assumption. In addition, loans utilised by the sponsors to fulfil equity requirements are excluded from the scope of debt assumption. By this provision, the Regulation implicitly accepts the utilisation of shareholder loans, or other types of loans, by the sponsors to satisfy their equity injection obligations in project agreements, which has historically been a commonly debated subject in concession-based project finance transactions in Turkey.

The Regulation also enables assumption under successive facility agreements executed for amendment or refinancing of the senior facility although this would be subject to Council of Ministers' decision on a case by case basis.

Pre-conditions of Debt Assumption

As per the Regulation, the following are the main conditions for debt assumption by the Treasury:

- (i) the project agreement annexed to the tender specifications should clearly provide for debt assumption and set out the necessary provisions mentioned in the Regulation;
- (ii) the authority launching the project should not have any overdue liabilities to the Treasury; and,
- (iii) the assumption should be within the debt assumption undertaking limits determined in the relevant year's budget law.

Necessary Approvals

The Regulation introduces a more detailed procedure with respect to the steps to be taken in order for the Treasury to enter into debt assumption arrangements. Accordingly, the authority launching the project should seek the approval of the Treasury with respect to the draft project agreement twice; once before launching the tender and again after the tender. In addition, the Council of Ministers also approves the debt assumption twice; once for determining the Treasury as the "authorised authority" for debt assumption and to negotiate the terms and conditions of the assumption and again at the end of negotiations to confirm the terms and conditions and to authorise the Treasury to execute the relevant debt assumption agreement.

Joint and Several Guarantee

The Regulation also introduces provision of a joint and several guarantee (*kefalet*) by the shareholders of the project company. Accordingly, in order for the Treasury to assume the principal/default interest and other related financing costs which were not paid on time due to the failure of the project company as of the date of the debt assumption, the shareholders must provide a guarantee to the Treasury. The amount of such guarantee cannot be lower than 110% of the largest repayment instalment due by the project company to its lenders.

Payment Methods

Pursuant to the Regulation, in line with its former implementations, the Treasury will have the absolute right to decide either to pay the assumed amount in the original repayment schedule or to make a bullet payment. Debt assumption agreements cannot provide anything to the contrary. In addition, in case the Treasury elects to make a bullet payment, the date of such payment cannot be shorter than two months starting from the notice of the Treasury to the creditors in this respect.

Monitoring and Notification

A project company with debt assumption agreement will now be required to obtain an external financing number (*dış finansman numarası*) from the Treasury at the time of first borrowing under its loan. The Regulation also requires any project company which is already party to a debt assumption agreement, to apply to the Treasury within 15 business days after publication of the Regulation, to obtain an external financing number.

The Regulation also requires the authorities to provide information to the Treasury regarding their potential projects in which debt assumption by the Treasury is envisaged.

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