

Model Public-Private Partnerships Core Toll Concessions Contract Guide

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1 Introduction

This guide presents key concepts for the structuring and development of legal contracts for highway transportation Public-Private Partnerships (P3) in the United States. It is part of the broader effort by the Federal Highway Administration (FHWA) to promote understanding of P3 transactions, which will include a document similar to this guide on availability payment contracts used in P3 transactions. This guide is designed to provide industry-standard concepts, relevant common tools and mechanisms, and situational examples applicable to P3 transactions.

A glossary of terms is included as Appendix A to assist in understanding the terminology used in this guide.

1.1 Public-Private Partnerships

A P3 describes a contractual arrangement between a Department (public authority) and a Developer (private entity) in connection with the design, construction, financing, operation and maintenance of an asset that will be used by or is otherwise valuable to the public. Unlike conventional methods of contracting for new construction (e.g., design-build), in which discrete functions are divided and procured through separate solicitations, P3 transactions contemplate a single private entity (generally a consortium of private companies comprising the Developer) which is responsible and financially liable for performing all or a significant number of the Project functions, including design, construction, financing, operation and maintenance. In recent years, Departments, including transportation agencies, have turned to P3 transactions to procure new transportation facilities, including highway projects, in an attempt to obtain time savings, cost savings, and more innovative, higher quality Projects with reduced risks. In exchange, the Developer receives the opportunity to earn a financial return commensurate with the risks it has assumed either through the receipt of Toll Revenues (on which the Developer takes both demand risk and toll collection revenue risk) or availability payments (on which the Developer takes appropriations risk) on such terms as may be outlined under the Concession Agreement. This guide focuses on the terms and issues relevant to transactions for which the Developer takes the risk of traffic demand and the resulting Toll Revenues. Transactions based on an availability payment mechanism will be treated in a separate guide.

1.2 Contractual Terms of P3s

The contractual agreement between the Department and the Developer, generally known as the Concession Agreement, lies at the heart of the P3 transaction structure. Traditionally, important contractual terms related to P3 transactions have included the following:

- ▶ The term of the concession, which for highway projects have extended beyond 30 years and up to 99 years.
- ▶ Requisite design-build specifications.
- ▶ Requisite operations and maintenance standards.
- ▶ Requisite hiring and employment standards.
- ▶ Requisite pricing and costing of services to the public.
- ▶ Supervening events, to a large extent defining the risk allocation in the contract.
- ▶ Defaults and early termination of the contract.

Because the Concession Agreement dictates the essential short and long-term dynamics of the P3 transaction, it is critical to the long-term success of the Project that the Department and the Developer are able to develop contracts that effectively exercise the intentions and priorities of the public sector.

1.3 P3s, the Federal Highway Administration, and the Moving Ahead for Progress in the 21st Century Act

The P3 transactions represent a potential option for State and local governments as a form of procuring the development, financing, construction, and operation, and maintenance of transportation facilities, including highway projects. The value to the Department in a P3 transaction is the transfer of costs and subsequent risk related to the design, build, financing, operations, and management of the Project to the Developer. In return the Developer is rewarded via an agreed-upon compensation (e.g., Toll Revenues or availability payments for services performed) for a prescribed term. Whether a P3 transaction is attractive to the Department and offers value-for-money for the public is to be assessed on a case-by-case-basis, and implementation is the prerogative of the State or local level agency responsible for the asset. Through this guide, the FHWA seeks to create a better understanding of P3 market terms and possible contract structures for use in the consideration and development of P3 transactions.

1.4 Background

The development of this guide stems from section 1534 of the Moving Ahead for Progress in the 21st Century Act (MAP-21). This section requires the Secretary of Transportation to compile and disseminate best practices. Upon request, the Secretary may also provide technical assistance to State and local transportation agencies in the development of P3s. The MAP-21 also requires the development of standard model contracts for the most common types of P3 transactions, with a view to encouraging transportation agencies and other officials to use these model contracts as a base template for use in P3 transactions.

In meeting these requirements, the FHWA has already taken several actions prior to the publication of this guide. An initial “listening session” on model contracts used in P3 transactions for the public and stakeholders was held in January 2013. The FHWA received a total of 28 comments following this listening session, and these comments were taken into account when selecting the topics to be covered in this guide.

The P3 transactions are being undertaken by transportation agencies with increasing frequency in order to deliver complex highway projects in the United States. The MAP-21 contains several sections that facilitate the use of P3 transactions for highway projects, including the development of model contracts and best practices focused on protecting the interests of the traveling public, taxpayers, and public agencies, including State departments of transportation (State DOT) and local governments. The focus of this guide is on P3 transactions that involve long-term concessions for designing, building, financing, operating, and maintaining highway projects. This document complements other primers and tools the Office of Innovative Program Delivery (OIPD) developed on the topic of P3s, including the primer, *Establishing a Public-Private Partnership Program*; documents on conducting evaluation of P3 proposals, including risk assessment, value for money analysis, and financial assessment; and the suite of educational tools known as P3-VALUE.

1.5 Objectives/Purpose

Based on public and stakeholder input from the listening session, the FHWA has ascertained that a set of prescriptive, standardized contracts for use in P3 transactions would not be acceptable or desirable to all State DOTs and other public agencies in the United States that are interested in using P3 for highway projects. As such, it is the objective of the FHWA that this guide will assist in educating public agencies and stakeholders on key issues in highway projects procured as P3 transactions, the trade-offs, and ways to

provide protections to the traveling public and State and local governments while continuing to attract private investment. Using the knowledge base of highway projects previously undertaken as P3 transactions, this guide attempts to educate agencies and stakeholders that may be only beginning to approach P3 transactions, while still providing relevant information to more sophisticated and experienced State and local transportation agencies. Overall objectives include the following:

- ▶ Increase State and local agency understanding of standard P3 market terms and possible contract structures, including the rationale behind such terms and structures.
- ▶ Enhance State and local agency understanding of market/investor perspectives, goals, and objectives.
- ▶ Present and analyze current legal and regulatory dynamics relative to highway projects procured as P3 transactions.
- ▶ Present and analyze current tools and mechanisms used in Concession Agreements for P3 transactions.
- ▶ Incorporate international best practices, where relevant.
- ▶ Encourage discussions with State and local agencies and stakeholders (via Webinar discussions to be conducted following the publication of this guide).

1.6 Description of Chapter Topics

This guide provides specific analysis for State and local transportation agency personnel on the following topics related to highway projects procured as P3 transactions, focusing on toll road concessions:

- ▶ Tolling Regulation.
- ▶ Benefit-Sharing.
- ▶ Supervening Events.
- ▶ Change in Law.
- ▶ Changes in Equity Interests.
- ▶ Defaults, Early Termination, and Compensation.
- ▶ Handback.

In addition to these topics, a forthcoming addendum will offer discussions on, among others, the following topics: performance standards, contract length, rebuild triggers (capacity increases), consumer protections, continuing disclosure, Federal requirements, lenders step-in and cure rights, operations and maintenance obligations, Developer indemnities, insurance, assignment/transfer of rights, dispute resolution and performance security.

In addition to this *Chapter 1: Introduction*, this guide includes the following chapters:

- ▶ **Chapter 2: Tolling Regulation** – Topics discussed include toll collection, user classification, toll rate setting, toll collection system and administration, enforcement of collections, management of demand risk, and use of revenue funds.
- ▶ **Chapter 3: Benefit-Sharing** –Topics discussed include the setting of revenue-sharing triggers, financial modeling and structuring of triggers within the P3 model, treatment of operating costs, capital costs, grants, the effects of refinancing on revenue-sharing, and other timing issues.
- ▶ **Chapter 4: Supervening Events** – Topics include the role of insurance in mitigating supervening risks, a definition of supervening events, and the types of contractual relief generally granted in supervening events.

- ▶ **Chapter 5: Changes in Equity Interests** – Topics include the definition of a change in ownership, example contractual provisions related to a change in ownership, permitted and prohibited changes, and participant concerns.
- ▶ **Chapter 6: Changes in Law** – Topics include the concerns of parties, unforeseeable changes in law and relevant considerations, tax-related issues, and compensation due to changes in law.
- ▶ **Chapter 7: Defaults, Early Termination, and Compensation** – Topics include events related to default by the Developer and the Department, cure periods, and termination rights of both parties in the event of a default, as well as all issues related to compensation for early termination.
- ▶ **Chapter 8: Handback** – Topics include handback requirements, inspections, reserve accounts, letters of credit, and payments related to handback.

1.7 Suggested Utilization of the Toll Concession Contracts Chapters

The FHWA encourages States, transportation agencies, and other public entities to use this guide as a resource when developing their own Concession Agreements.

Educational Reference

The suggested primary purpose of this guide is as an educational reference for State and local agencies and is not intended to be used as legal advice. Each chapter contains high level introductions to key topics, example definitions and provisions as well as guidance on contract structuring in respect of those key topics.

This guide is designed to be an informational tool for State and local governments to refer to when considering a P3. Every Project is unique and attention will need to be given to the specific factors relevant to each transaction. This guide introduces and analyzes several areas that have generally required significant consideration in highway projects structured as P3 transactions in the United States to date. Each such P3 transaction may require consideration of more or fewer factors than those covered in this guide. This guide is for informational purposes only and should not be construed as legal advice from FHWA. Transportation agencies are encouraged to retain or utilize their own counsel and other appropriate external expert advisors in any P3 transaction.

Illustrative and Example-Based

Existing Projects and Concession Agreements have informed the structure of this guide. Furthermore, market-standard provisions have been discerned and analyzed for the benefit of the reader. The goal of these inclusions is to provide real-life application of theoretical analysis presented in the guide. They also provide State and local agencies with a broader perspective and understanding of the P3 market and several non-contractual dynamics that may play a significant role in P3 transactions. The example provisions, when taken together with the explanations and descriptions of key issues in each of the chapters, provide insight into best practices and may be utilized to develop solutions for Projects that can protect the interests of State and local governments, tax-payers and the traveling public. It must be noted that the inclusion of specific example provisions that may derive from particular Projects in this guide does not indicate a recommendation or promotion of one particular form of P3 transaction over another. Instead, the examples included illustrate a technique, mechanism, or dynamic that the FHWA views as valuable for the purposes of educating State and local agencies. To reiterate, every P3 transaction is different, and what is applicable for one transaction may not be applicable for another transaction.

Glossary of Terms and Example Provision Definitions

As part of this guide, a glossary of terms has been provided to be used as an educational tool to assist in understanding the guide. The terms provided in the glossary are for informational purposes only and are not designed to be used in legal documentation, even though a number of the terms contained in the glossary

may also be used in example provisions found in this guide. The example provisions contained throughout this guide include bracketed capitalized terms. These terms are commonly used in the industry but both the terminology and substantive meaning of these terms will differ from transaction to transaction. Therefore, use of these terms (and the technical legal definitions that will accompany them in the Concession Agreement) must be considered carefully for each P3 transaction. As noted above, the descriptions contained in the glossary of terms do not represent legal definitions of these bracketed capitalized terms.

1.8 Conclusion

This guide is intended to contribute to a better understanding of P3s and considerations for structuring a highway project procured as a P3 transaction. The FHWA has designed the guide to be as effective as possible in supporting public agencies in their exploration and implementation of successful P3 transactions, in the aim of promoting better and more efficient highway projects.

2 Tolling Regulation

2.1 Introduction

When procuring a new Project by means of a concession, the Department will generally address the threshold question of whether the Developer should bear the economic risk of the Project's performance during the Term, including, in particular, the risk of user demand for the Project. If the Department determines that transferring the risk of user demand for the Project to the Developer is a marketable proposition and is otherwise desirable, the Department will tender a Concession Agreement for the Project that entitles the Developer to tolling rights, being the right to establish, assess, collect, enforce (subject to applicable law), and retain tolls paid by users of the Project. Under such an arrangement, the Developer relies on Toll Revenues, rather than government appropriations, as its principal source of funds for financing the performance of its obligations under the Concession Agreement, paying debt service to its Lenders, and realizing a reasonable return on its equity investment in the Project.

When providing for tolling rights under the Concession Agreement, the Department may establish a series of limitations on the Developer's exercise of tolling rights to address important public policy objectives, including limiting the Developer's pricing power in relation to users, achieving certain mobility and traffic management outcomes, establishing exemptions of certain users from tolls, and producing Toll Revenues sufficient to pay a return on investment that will attract private investment in the Project.

Therefore, where the Concession Agreement establishes tolling rights in favor of the Developer, the Concession Agreement will generally, among other things:

- ▶ Expressly provide for the right of the Developer to establish, assess, collect, and enforce tolls on the Project and retain the related Toll Revenues free and clear of any interest of the Department in such revenue, subject to certain limitations set forth in the Concession Agreement and applicable law.
- ▶ Specify when the Developer's tolling right takes effect and terminates or otherwise expires.
- ▶ Identify the users of the Project who are subject to tolls and set out the procedure for changing the classification of such users.
- ▶ Establish a procedure for changing the limitations on, or methodologies for determining, future toll rates.
- ▶ Specify the mechanism for toll collection and administration of the toll collection mechanism.
- ▶ Identify the circumstances under which the Department or others may suspend the tolling rights of the Developer.

2.2 Right to Collect Tolls

2.2.1 *Granting of the Tolling Right*

The Concession Agreement generally expressly grants to the Developer the right to toll certain specified users of the Project and recites the Department's legal authority for granting such a right to the Developer. To ensure clarity, the Project must be precisely identified (along with relevant geographic dimensions or cartography in an appendix, if necessary), and if defined elsewhere, a reference to that definition should be made.

2.2.2 Duration of Tolling Right

In the case of a newly constructed Project, the start date of tolling is generally the date when the Project is available and open for public use, which is generally defined as either the Substantial Completion Date of the Project or the Service Commencement Date of the Project. In cases where the Concession Agreement relates to both an existing asset and a greenfield project, the start date with respect to the existing asset is the date of transfer of such asset from the Department to the Developer (generally the effective date of the Concession Agreement), while tolling with respect to the newly constructed portion of the Project will generally commence on the date that the newly constructed portion becomes available and open for public use. The date of termination is generally the last day of the Term.

An example provision establishing the tolling rights of the Developer is set forth below.

Pursuant to the [relevant statute or legal provision] and subject to the terms and conditions of this [Concession Agreement] as may be further described in the other [Project Documents], the [Department] hereby grants to the [Developer] the exclusive right from and after the [Substantial Completion Date/Service Commencement Date/effective date of this Concession Agreement] and until the end of the [Term], to manage, operate, maintain, improve, and equip the [Project] and establish, impose, charge, collect, use, and enforce payment of tolls from users of the [Project].

2.3 User Classification

2.3.1 Tolloed and Exempt Users

The various classes of users of the Project, which are subject to tolls, are often identified in the Concession Agreement. Users exempted from tolls, if there are any, are also specifically mentioned. Because the demand risk is generally borne by the Developer in a toll road concession, the Developer generally wants to limit the types of users who are exempt from paying tolls. Ordinarily, vehicles belonging to the Department, subcontractors of the Department working on the Project, law enforcement and emergency services vehicles, and public transportation vehicles are exempt from paying tolls. The Department may also exempt certain users, such as commuter buses, school buses and motorcycles, from paying tolls based on public policy considerations, such as fuel efficiency, space utilization, or congestion relief. The list of exempted users will differ from one Concession Agreement to another based on the context and purpose of the Project. Furthermore, if local laws where the Project is located specifically exempt certain users from being tolled, the Concession Agreement will generally reflect this exemption.

When the Project is a traditional toll road concession, where all users are subjected to tolls, user classification primarily serves to identify the toll rates for various types of users. For managed lanes facilities, the Concession Agreement may require a more detailed definition of users. In the context of a toll road concession, a managed lane facility may be a high-occupancy toll lane, express toll lane or even an exclusive/special-use lane with tolls for certain users. The Concession Agreement contains a detailed definition of the various types of users, including users who are eligible to use the managed lane facility and eligible users who are exempt from tolls. Provisions dealing with user classification can generally be found in the form of an appendix to the Concession Agreement.

An example user classification provision for a managed lane facility is set forth below.

- (a) *Only [Permitted Vehicles] will be allowed to use the [Project/relevant lane].*
- (b) *[High-Occupancy Vehicles] equipped with a transponder will be entitled to use the [Project/relevant lane] at a [X%] discount from otherwise applicable tolls.*
- (c) *[Relevant vehicles e.g., mass transit vehicles, commuter buses, school buses, motorcycles] and [Exempt Vehicles] equipped with a transponder will be entitled to use the [Project/relevant lane] at a [Y%] discount from otherwise applicable tolls.*

(d) *[Permitted Vehicles] (other than vehicles referred to in clauses (b) and (c) above) will be entitled to use the [Project / relevant lane] subject to payment of the applicable tolls.*

2.3.2 Change of User Classification

The Concession Agreement will generally include a provision allowing the Developer to change user classification in the future subject to specific approval from the Department. A procedure is generally set forth for the Developer to apply for a change in the existing classification of users. The Department generally has the right to accept (with or without conditions or modifications) or reject the Developer’s application based on its public policy considerations, and the extent of this right differs from one Concession Agreement to another. Generally, certain conditions are set forth in the Concession Agreement that guide the Department’s decision regarding the application. If there are costs relating to change in the classification of users and/or in integrating such changes into any regional toll collection system, the Developer is generally required to compensate the Department. Changes in the classification of users may potentially impact future projected toll revenues. The Concession Agreement may contain provisions for adjusting the Department’s revenue sharing if the change is projected to increase the Developer’s revenues.

An example change of user classification provision is set forth below.

(a) *The [Developer] may not change, add to or delete any of the classification of users of the [Project] for the purposes of determining toll rates without the [Department]’s express prior written consent.*

(b) *If the [Developer] desires to change classification of users of the [Project] for the purposes of determining toll rates, then the [Developer] shall apply to the [Department] for permission entitling the [Developer] to implement such change at least [X] days prior to the proposed effective date of such change. Such application shall set forth:*

- (i) *the change in classification or category requested;*
- (ii) *the date such change shall become effective;*
- (iii) *the length of time such change shall be in effect;*
- (iv) *the reason the [Developer] requests such change;*
- (v) *the effect such change is likely to have upon users and traffic patterns;*
- (vi) *a proposed schedule of toll rates reflecting such change; and*
- (vii) *such other information and data as the [Department] reasonably may request.*

If the Concession Agreement intends to grant limited power to the Department on whether to accept or deny the Developer’s application and offer the Developer recourse to a Dispute Resolution Mechanism, then the following wording may be used:

(a) *The [Developer]’s application shall be deemed granted unless within [X] days after receipt of a completed application the [Department] advises the [Developer] that it has granted the [Developer]’s application with conditions or denied the [Developer]’s application. If the Department makes such a finding the [Developer] may modify its application and supporting documentation, and resubmit the same to the [Department] or appeal the [Department]’s decision pursuant to the [Dispute Resolution Mechanism] set forth in the [Concession Agreement]. If the [Developer] resubmits an application as aforesaid, the above procedures shall apply to the resubmitted application.*

(b) *The [Department] shall not deny an application or impose conditions unless the [Department] finds that the proposals set forth in the application are not reasonable under the circumstances, the supporting documentation is in error or is insufficient to support the proposal or that the assumptions of projections set forth in the application are unrealistic.*

If the Concession Agreement grants greater power to the Department in the determination of the Developer’s application, then the following wording may be used:

The [Department] may deny an application or impose conditions to granting an application in its sole discretion. The

[Department]'s decision shall not be subject to the [Dispute Resolution Mechanism] under this [Concession Agreement]. If the [Developer] finds the [Department]'s conditions to the grant of an application to be unacceptable, the [Developer] may withdraw the application and continue with the existing classification of users. If the [Developer] resubmits an application after rejection or imposition of conditions, the above procedures shall apply to the resubmitted application.

2.4 Toll Rates

The Concession Agreement may provide details regarding the toll rates that the Developer is permitted to charge and collect from various classes of users; it may also specifically mention how the tolls are to be determined. The toll rates may be fixed or varied based on the time of the day or the amount of traffic on the toll road, either dynamically (based on real-time traffic conditions) or according to a set schedule. The setting of toll rates generally depends on the type of Project and the policy the Department has adopted.

An important element in setting toll rates relates to the increase and escalation of toll rates. To the extent that the toll rates are predetermined in real (constant) dollars and expected to account for inflation, the rates are generally accompanied by a methodology to convert toll rates into nominal (current) dollars. Often toll rate escalation is achieved by linking the rates to a relevant consumer price index (CPI), gross domestic product (GDP) growth rate, or a certain annual percentage escalation. The choice of the escalation factor may be either the lower or greater of the listed escalation factors. In some instances, it is also possible to combine CPI or GDP-based escalation and a certain annual percentage escalation. In contrast to escalation, which is generally linked to an index, toll rate increase is aimed at achieving real increases in toll rates through a certain annual percentage increase or a predetermined schedule. The frequency of toll rate increases or escalation is also generally expressly stated in the Concession Agreement, namely, whether adjustments are semiannual or annual or whether they occur at other intervals. Additionally, the Concession Agreement may also state how the toll increase or escalation may account for maximum allowable toll increase or escalation that was not made in prior years by the Developer.

Where the toll rates are dynamic or variable in relation to user demand, they are generally determined by an algorithm agreed upon by the Developer and the Department. Details of such an algorithm are also incorporated into the Concession Agreement.

The role of the Department in establishing toll rates is often specified. Because the Developer bears the demand risk, it generally would prefer as little restriction on the setting of toll rates as possible. However, given that toll roads and toll rate changes often come under public scrutiny, the Department may wish to retain some control over the setting of toll rates to achieve public policy objectives. These objectives may include protecting the interests of users, achieving certain mobility and traffic levels, preventing the Developer from making unreasonably high profits, and fostering public acceptance of tolling. If the Department envisions certain restrictions on the setting of toll rates, including minimum and/or maximum toll rate, increase or escalation, then such restrictions are expressly included in the Concession Agreement.

The Concession Agreement may also specify whether the Developer is permitted or required to offer discounts on toll rates. It is also common for the Department to prohibit discrimination in charging and collection of toll rates. Consequently, the Developer may be required to ensure that the toll rates are the same for users under like conditions; which may take into consideration type, weight, and occupancy of a vehicle, number of axles, time-of-day and/or day-of-week travel, traffic congestion and other traffic conditions, and type of facilities.

Other related aspects may also be outlined in the Concession Agreement, such as the procedure to establish the toll rates and notification of toll rates to users.

Two example toll rate provisions are set forth below.

The [Developer] shall have the right to establish, and thereafter to modify from time to time, the toll rates applicable to (a) various classes of vehicles; (b) vehicle occupancy levels; (c) times of use; and (d) portion of the [Project] utilized. The [Department] shall have no right to regulate or participate in the setting of toll rates.

Subject to the foregoing paragraph, the maximum toll rate from and after [Substantial Completion Date/Service Commencement Date] will be no more than [X], subject to escalation in accordance with the relevant index agreed between the [Department] and the [Developer].

- (a) The [Developer] shall impose congestion pricing, which may include dynamic tolling with potential toll rate changes at frequent intervals, with a view to maintaining free flow conditions of traffic, and there shall be no restrictions upon toll rates except as set forth in [Exhibit [X]] to this [Concession Agreement].
- (b) The toll rates shall be the same for persons using the [Project] under like conditions, and for this purpose “like conditions” may take into consideration type, weight and occupancy of the vehicle, number of axles, time-of-day and/or day-of-week travel, traffic congestion and other traffic conditions and type of facilities, provided, however, that the [Developer] may adopt and implement discount programs for different classes or groups of persons using the [Project] under like conditions, subject to the provisions of this [Concession Agreement].

Exhibit [X] – Toll Rate Schedule

Vehicle Type	X A.M. – Y A.M.	Y A.M. – Y P.M.	Y P.M. – Z A.M.	Z A.M. – X A.M.
[Axle and/or Occupancy]	\$A	\$D	\$G	\$J
[Axle and/or Occupancy]	\$B	\$E	\$H	\$K
[Axle and/or Occupancy]	\$C	\$F	\$I	\$L

2.5 Toll Collection

2.5.1 Toll Collection System and Administration

The toll collection system that the Department and the Developer agree to institute is documented in the Concession Agreement. This system could be electronic, video-based, or any other system agreed to between the Department and the Developer. This system may be accompanied by an obligation on the part of the Developer to establish and administer such a system by entering into required contractual relationships.

Two widely used technologies for toll collection are (1) electronic tolling and (2) video-based tolling (also referred to as license plate tolling). In the case of an Electronic Toll Collection System, the Department may prescribe that it be interoperable with the system on other toll roads both within and outside the State. Many transportation agencies in the United States have subscribed to a common Electronic Toll Collection System. Broad subscription has made toll collection technology compatible across States and gives users seamless access to toll roads across multiple States. As such, the Department may require the Developer to use a certain technology.

If the Department has subscribed to a particular toll collection technology, the Department may prescribe a form agreement whereby the Developer is allowed access to use that technology on the Project for a certain fee. Similarly, if the Department has delegated toll collection in a particular region to a separate entity, it may require the Developer to use the services of such entity. Typically, a tolling services agreement with such entity, which defines pricing and other terms and conditions, is developed before submission of the bids.

Where the Department conducts tolling of toll roads other than the Project, the Developer and the Department may enter into agreements that make the “back office” functions of the Department’s tolling operations available to the Developer, including, for example, an “Electronic Toll Collection Agreement,” pursuant to which the Department (or a separate entity responsible for toll collection) would provide toll transaction account management services to the Developer.

An example set of provisions on toll collection system and administration is set forth below.

The [Developer] shall have the right, in its sole discretion, to select, install, modify, and utilize vehicle identification, traffic surveillance, and toll collection equipment and technology that meets the published standards of [the Department].

(a) *From and after the [Substantial Completion Date/Service Commencement Date/effect date of this Concession Agreement] through the end of the [Term], the [Developer] will operate and maintain a toll collection system with respect to the [Project] that will be interoperable with the [Electronic Toll Collection System] utilized on [State Highways] at that time. If the [Department] intends to change any State-wide interoperability or compatibility standards, requirements or protocols for toll collection systems, it will coordinate with the [Developer] prior to the implementation of such change so as to minimize the loss of [Toll Revenues], disruption and cost to the [Developer], but the [Department] will not be liable in any event for any loss of [Toll Revenues], disruption, or cost attributable to such change.*

(b) *If the [Developer] selects an electronic toll and traffic management system other than the system then utilized on other [State Highways], it will coordinate with the [Department] prior to the implementation or any change of such system to ensure interoperability and compatibility with [the Electronic Toll Collection System] (or any successor to the [Electronic Toll Collection System] utilized on [State Highways] at that time) or with such other system then utilized on other [State Highways].*

The [Developer] shall implement a toll collection system that charges, debits and collects tolls only at or through electronic toll collection facilities physically located on the [Project] or through global positioning system technologies or other remote sensing technologies that charge, debit, and collect tolls only for actual vehicular use of the [Project] in accordance with the following sub-clauses:

(a) *The [Developer] shall maintain and operate an [Electronic Toll Collection System] for the [Project] that meets applicable State-wide interoperability and compatibility standards, requirements and protocols, if any, including any pertaining to any clearinghouse system that the [Department] participates in, implements, and operates.*

(b) *Interoperability is required as to (i) functionality, enabling use of a single electronic toll collection transponder across all [State Highways], (ii) user account maintenance, management and reconciliation, and (iii) funds transfers among all participant, enabling a user to have a single electronic toll collection transponder to pay for tolled travel on all [State Highways].*

2.5.2 Enforcement of Toll Collection

In a toll road concession, the Developer generally assumes the primary responsibility and risk of toll collection, including the checking/monitoring of user toll violations. In assuming this responsibility, the Developer generally outsources monitoring of toll violations and enforcement of violation fees to law enforcement and other State agencies, although the approach taken for each Project will depend on applicable laws regarding the enforcement of toll violations. Where the Department has existing agreements with law enforcement and State agencies, the Developer may be given the option to enter into an agreement with the Department (or a separate entity, such as a regional authority, responsible for toll collection) to secure toll enforcement and violations processing services, sometimes referred to as a “Toll Enforcement and Violation Processing Services Agreement.” A form of such an agreement is generally provided as an appendix to the Concession Agreement. Such a form of agreement needs to identify the role and

responsibilities of the Developer, the Department, and other State agencies that may be party to that agreement. Usually, such an agreement does not transfer toll revenue risk from the Developer to the respective toll collection entity; it may, in some instances, transfer the risk of processing toll payments or the use of certain technology to the toll collection entity.

An example toll enforcement provision reflecting outsourcing of toll violations monitoring and enforcement of violation fees to the Department by the Developer is set forth below.

- (a) *The [Department] has implemented and maintains a processing system for the enforcement of penalties for toll violations in [name of province] on [State Highways]. The [Developer] may, but is not obligated to, enter into an agreement with the [Department] to obtain the benefits of such enforcement system, in accordance with the [Toll Enforcement and Violations Processing Services Agreement] in the form attached as [Exhibit [X]] to this [Concession Agreement]. In consideration of such services, the [Developer] will pay the [Department] its customary charges for such services in effect from time to time.*
- (b) *For purposes of identifying and apprehending toll violators, provided it is authorized under [Law], and any applicable agreements or arrangements between the Developer and the Department, the [Department] will make available to the [Developer] the benefits of any agreements or arrangements which the [Department] has in place with other State authorities or agencies that provide access to records in their possession relating to vehicle and vehicle owner data, and will coordinate with the regional police in accordance with [relevant clause, if any, with respect to this provision] of policing services, emergency services, traffic patrol, and traffic law enforcement services on the [Project].*
- (c) *The [Developer] understands and agrees that, notwithstanding anything to the contrary in this [Concession Agreement] or any other [Project Document], the risk of enforcement and collection of tolls, and related charges (including user fees and civil penalties and administrative fees) remains with the [Developer], and that the [Department] does not, and will not be deemed to, guarantee collection or collectability of such tolls and related charges to the [Developer]; provided, however, that the foregoing will not limit the [Department]'s obligations or duties under the [Toll Enforcement and Violations Processing Services Agreement] or any other agreement with the [Developer].*

2.6 Use of Toll Revenues

The Concession Agreement may also set forth requirements concerning the use of Toll Revenues the Developer collects to ensure that the Developer does not divert Toll Revenues for unauthorized purposes. Generally, the Department may want the Developer to use the Toll Revenues to meet payment obligations to the Department (if any), operating and maintenance expenses (if applicable), taxes owed to the State agencies, or debt service related to the Project before making payments to Equity Investors. The objective is to ensure continued operation of the Project by ensuring payment to key stakeholders, including the Subcontractors, Lenders, State agencies, the concerned Department, and others owed various monies. To meet this objective, the list of authorized uses of Toll Revenues under the Concession Agreement may follow a certain order of priority. Priority is often given to operating and maintenance expenses, including the funding of major maintenance costs, and debt service payments relating to the Project over distributions to the Developer's Equity Investors and any other noncompetitive payments. While the Department may prescribe a list of authorized uses of Toll Revenues, some Concession Agreements may leave the decision regarding the full order of priority to the Lenders and the Developer. The Financing Documents of a Project often include a flow of funds, known as a cash flow waterfall, and it is common for the uses of Toll Revenues in the Concession Agreement and flow of funds in Financing Documents to mirror each other.

Federal law also imposes certain restrictions on the use of Toll Revenues collected from Projects that have received Federal assistance. These restrictions are generally incorporated into the section of the Concession Agreement dealing with compliance with Federal requirements (see Section 2.7.3 below).

An example provision providing for authorized uses of Toll Revenues is set forth below.

- | | |
|---|--|
| <p>(a)</p> <p>(b)</p> <p>(i)</p> <p>(ii)</p> <p>(iii)</p> <p>(iv)</p> <p>(v)</p> <p>(vi)</p> <p>(c)</p> | <p><i>[Toll Revenues] shall be used first to pay all current and delinquent costs and expenses of operating and maintaining the [Project] (including premiums for insurance, bonds, other performance security) and payments to the [Department] before they are used and applied for any other purpose.</i></p> <p><i>The [Developer] shall not use [Toll Revenues] to make any distribution to the holder of an equity interest in the [Developer] or to pay the noncompetitive fees and charges of its affiliates unless and until the [Developer] first pays:</i></p> <p><i>all current and delinquent costs and expenses of operating and maintaining the [Project] (including premiums for insurance, bonds, other performance security);</i></p> <p><i>current and delinquent debt service, and other current and delinquent amounts, due under any [Project Debt];</i></p> <p><i>all taxes currently due and payable or delinquent;</i></p> <p><i>all currently required or delinquent deposits to the [Major Maintenance Reserve Account];</i></p> <p><i>all current and delinquent costs and expenses of major maintenance not capable of funding from the [Major Maintenance Reserve Account]; and</i></p> <p><i>all current and delinquent amounts due to the [Department] under this [Concession Agreement] that are being contested in good faith and by appropriate proceedings and with respect to which adequate reserves as required by generally accepted accounting principles consistently applied have been established by the [Developer].</i></p> <p><i>The [Developer] shall have no right to use [Toll Revenues] to pay any debt, obligation, or liability unrelated to this [Concession Agreement], the [Project], or the [Developer]'s services under this [Concession Agreement].</i></p> |
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2.7 Other Matters Related to Toll Regulation

2.7.1 Suspension of Tolling

The Department generally reserves the right to suspend tolling in case of certain types of emergencies expressly declared pursuant to law and to divert the use of the Project to meet the needs of such an emergency or any other alternate purpose. Such suspension of tolling is primarily intended to be temporary to enable the Department and other Governmental Authorities to deal with emergent situations.

Concurrently, the Concession Agreement also details the rights of the Developer when tolling is suspended for an emergency, including any compensation that the Department is liable to pay for loss in Toll Revenues or an increase in costs incurred by the Developer. Generally, the Developer is not entitled to compensation when the Department has concurrently ordered the suspension of tolling on all other toll roads in the region or if the suspension has been declared by a government agency other than the Department, such as the Federal Government. Such suspension is generally called for during natural disasters. If the underlying reason for suspension of tolling persists, it is possible for it to be dealt with as one of the supervening events discussed in Chapter 4 (Supervening Events).

Where the Department has ordered suspension of tolls only on the Developer's Project to deal with incidents or emergencies (of a limited nature), the Department is commonly required to compensate the Developer for loss of Toll Revenues or higher costs the Developer incurred provided that the order of suspension extends beyond a certain duration (hours/days).

Finally, the right to order a suspension of tolling generally comes with an obligation on the part of the Department to lift the suspension as soon as the need for such suspension ceases to exist. This obligation is critical as it seeks to protect the Developer from unduly extended or unwarranted suspension of tolling by the Department.

An example suspension of tolling provision is set forth below.

- (a) *In addition to its rights granted pursuant to law, the [Department] shall have the right to order immediate suspension of tolling in the event the [Project] is designated for immediate use as an emergency mass evacuation route. The [Department] shall have no liability to the [Developer] for the loss of [Toll Revenues] or the increase in costs and expenses attributable to such order, provided that the [Department]:*
- (i) *concurrently suspends tolling on all other [Department]-operated facilities that are located within the area designated for evacuation or facilitation of evacuation;*
 - (ii) *concurrently orders suspension of tolling on all other facilities operated by others within such area and over which the [Department] has the authority to order such suspension; and*
 - (iii) *lifts such order over the [Developer] concurrently with the lifting of such order for all other facilities.*
- (b) *The [Department] shall lift such order as soon as the need for emergency mass evacuation ceases. The [Department] shall have no liability to the [Developer] for the loss of [Toll Revenues] or the increase in costs and expenses attributable to any order to suspend tolling to facilitate emergency mass evacuation issued pursuant to applicable law by the [Department] or any other [Governmental Authority].*
- (c) *In the event the [Project] is designated for immediate use as the alternate route for diversion of traffic from another [State Highway] temporarily closed in one or both directions due to an incident or emergency, the [Department] shall have the right to order immediate suspension of tolling in the direction(s) of diversion. The [Department] shall have no liability to the [Developer] for the loss of [Toll Revenues] or the increase in costs and expenses attributable to the duration that such order is in effect, except that if such order remains in effect for more than [X] days, the [Department] shall compensate the [Developer] for the financial impact of such order beyond the first [X] days. The [Department] shall lift such order as soon as the need for such order ceases.*

2.7.2 Demand Risk

For the avoidance of doubt, the Concession Agreement may expressly provide that the Developer bears the risk of traffic volume not meeting projections or a shortfall in Toll Revenues.

An example provision providing for transfer of demand risk to the Developer is set forth below.

Except for its specific obligations to the [Developer] under the terms and conditions of this [Concession Agreement], the [Department] will not have any risk or liability related to actual traffic volume and toll revenue, including but not limited to the risk that actual traffic volume is less than the traffic volume projected in the [Base Case Financial Model].

2.7.3 Compliance with Federal Requirements Related to Tolling

As will be discussed in Chapter 6 (Change in Law), Concession Agreements often contain a compliance with laws provision obligating the Developer to comply with all applicable laws. Of specific importance is Title 23 of the United States Code (U.S.C.), which is applicable to highways.

Under section 301 of Title 23, tolling is generally prohibited on highways, bridges, and tunnels that have received Federal-aid funding for their construction. However, Federal law has also carved out a limited number of exceptions to this general prohibition through special programs and provisions, including the following:

- ▶ Section 129 of Title 23, which relates to toll roads, bridges, and tunnels (also referred to as the General Toll Program).
- ▶ Section 166 of Title 23, which deals with high-occupancy vehicle (HOV) facilities, including charging of tolls on certain users of HOV lanes.
- ▶ The Interstate System Reconstruction and Rehabilitation Pilot Program.
- ▶ The Value Pricing Pilot Program.

▶ The Express Lanes Demonstration Program.¹

If the Project is a Federal-aid highway, bridge, or tunnel, then the authority to toll must be obtained from one of these programs, which have certain requirements with which the Department with responsibility for the Project is obligated to comply. These requirements vary from program to program, but generally include such items as limitations on the use of Toll Revenues (including the submission of audits to document compliance); certifications of adequate maintenance; and monitoring and reporting on the performance of the facility. These and other commitments may be memorialized in a tolling agreement between the responsible Department and the FHWA. The Concession Agreement will generally require the Developer to comply with the applicable requirements of the relevant Federal tolling program and to provide supporting documentation demonstrating such compliance to the Department for reporting to the FHWA.

If any Project procured by the Department receives Federal assistance, then, except to the extent that the terms of an applicable tolling or pricing program require otherwise, the use of the revenues from the operation of such facility will be subject to the restrictions set forth in Section 129(a)(3). In the event that such Project is procured by the Department pursuant to a Concession Agreement, the Department may include in the Concession Agreement an undertaking from the Developer to comply with Section 129(a)(3) and to assist the Department with documentation of such compliance.

Section 129(a)(3) also requires that a Department with jurisdiction over a Title 23-assisted Project use “all toll revenues received from operation of the toll facility” exclusively for “(i) debt service with respect to the projects on or for which the tolls are authorized, including funding of reasonable reserves and debt service on refinancing; (ii) a reasonable return on investment of any private person financing the project, as determined by the State or interstate compact of States concerned; (iii) any costs necessary for the improvement and proper operation and maintenance of the toll facility, including reconstruction, resurfacing, restoration, and rehabilitation; (iv) if the toll facility is subject to a public-private partnership agreement, payments that the party holding the right to toll revenues owes to the other party under the public-private partnership agreement; and (v) if the Department certifies annually that the tolled facility is being adequately maintained, any other purpose for which Federal funds may be obligated by a State [under Title 23, U.S.C.]”

Two observations are noteworthy in the context of the Concession Agreement. First, Section 129(a) expressly reserves for the States (and agencies existing under interstate compact) the right to determine what constitutes payment of a reasonable return on investment from Toll Revenues. Second, Section 129(a) does not establish an order of priority among permitted uses of proceeds from Toll Revenues. For example, it is not a requirement of section 129(a) that the payment of a reasonable return on investment be made prior to paying costs necessary for the improvement or proper operation of the facility. Similarly, it is not a requirement that the payment of financing costs takes priority over payment of maintenance costs. Such flexibility permits the Developer and the Department to determine the priority of uses of toll revenue in the Concession Agreement, provided that the uses are otherwise eligible uses of toll revenue under Section 129.

An example provision providing for compliance with Federal requirements is set forth below.

The [Developer] agrees, at all times, to comply with the provisions of [Section 129(a)(3), Title 23 of the United States Code/applicable law], and its successor provisions, all regulations promulgated thereunder, in the performance of its obligations under this [Concession Agreement]. The [Developer] shall coordinate its compliance efforts with the [Department] so as to enable the [Department] to provide the certifications required by [USDOT].

¹ The FHWA’s authority to enter into new tolling agreements under the Express Lanes Demonstration Program expired on September 30, 2012.

3 Benefit-Sharing

3.1 Introduction

Departments often seek to minimize the potential for excess or windfall profits under the Concession Agreement. Departments may do so by including provisions in the Concession Agreement that require the Developer to share certain financial benefits with the Department during the Term. Generally, benefit-sharing is known by a number of terms, including concession fee, permit fee, or revenue-sharing payments. Such benefit-sharing provisions support the public credibility of the Project.

The benefit-sharing provisions of the Concession Agreement also serve to ensure that the Developer receives a financial benefit that reflects the risk-adjusted return on its investment in the Project. These provisions should make clear that the Developer is entitled to a financial return within certain parameters. These provisions should also provide justification for toll setting and toll rate increases based on the overall risk-return calculation of the Concession Agreement. Departments may refer to these provisions if they are subject to public criticism about toll rates or rate increases.

A third reason for benefit-sharing is the Department's need to receive a return on its effort to help defray the cost of the Project, if the Department made a financial contribution, or to pay for other related or other regional transportation projects. However, Departments rarely seek an actual return on grants provided or other in-kind contributions in Concession Agreements in the same sense that Developers do.

3.2 Revenue-Sharing Triggers

Generally, Concession Agreements have thresholds, or triggers, which require revenue-sharing when revenues or investment returns exceed prescribed levels.

3.2.1 Types of Triggers

There are two main types of triggers. One is based on Gross Revenues, known as revenue triggers, and the other is based on the Equity Internal Rate of Return (IRR) of the Developer, known as return triggers.

Revenue Triggers

Revenue triggers are generally thresholds established in the Concession Agreement, such that if revenues collected are above certain pre-agreed levels, the Developer must pay a percentage of the excess revenues to the Department. Revenue triggers do not take account of costs (whether higher or lower than originally expected) given their assumptions regarding the approximate correlation between revenues and return. Revenue triggers are generally considered easier to calculate and administer because there is generally less dispute about what constitutes Gross Revenues in a Project with limited revenue sources.

An example of a revenue trigger provision is set out in section 3.2.2.

Return Triggers

Return triggers generally refer to triggers based on some measure of return on equity or invested capital. The calculation of such returns generally relies on the Equity IRR concept used widely in finance that compares an outflow (the investment) with the stream of inflows (dividends, interest payments, or other forms of compensation), taking into account the timing of such outflows and inflows. While the underlying math used in these calculations is widely understood, return calculations are often more complex because identifying the inflow is not always transparent. Unlike a revenue trigger, which uses a simple measure of Gross Revenue, the inflow calculation used in a return trigger must take into account a number of the costs

paid by the Developer, such as operating and maintenance expenses, capital costs, and sometimes taxes. This leads to an auditing requirement and the potential for abuse, disputes and increased monitoring costs in comparison to revenue triggers.

Return triggers directly address the concern that the Developer might receive excessive profits and/or charge excessive toll rates, and prevent the Developer from not only receiving excess profits but also being unfairly penalized when the profits are lower than expected. However, given the complexities associated with the calculation of return triggers, careful consideration should be given to the way in which revenues, costs, and profits are treated.

An example Equity IRR-based trigger provision is set forth below.

- (a) *Following completion of an annual update to the [Base Case Financial Model], at which the actual [Equity IRR] exceeds the cash flow sharing thresholds, a cash flow sharing amount payment will be due from the [Developer] to the [Department].*
- (b) *If the actual [Equity IRR] as of the cash flow review date exceeds the cash flow sharing threshold, the [Developer] shall pay to the [Department] cash flow sharing amounts based on the incremental amount of revenue above the cash flow sharing threshold times the cash flow sharing rate of [X%].*

The Department may use a “Total Return on Investment” concept in the Concession Agreement, reflecting various forms of debt and equity. The Concession Agreement would establish bands representing certain total Equity IRR percentages and for each band, the Department may require sharing of allocated percentages of Gross Revenues.

Departments should analyze the approach they wish to take to determine the trigger that is most appropriate for the specific Project, taking into account the oversight costs and public perception impact of each approach. Departments should also consider the legal requirements applicable to the specific Project. Some P3 authorizing statutes may call for a sharing arrangement based on concepts such as a reasonable Equity IRR for the private sector, which will favor the use of a return trigger as opposed to a revenue trigger. Other statutes may similarly state that the Concession Agreement can provide for a reasonable Equity IRR without expressly contemplating a sharing mechanism. Where these statutes apply, Departments should consider the extent to which benefit-sharing mechanisms can assist them in achieving these statutory mandates and the extent to which the potential Developer should be provided with guidance during the procurement phase of a Project in relation to the applicable requirements.

3.2.2 Using One or Multiple Triggers

The triggers derived by the Department or its advisors are generally based on research of comparable investments in the financial markets. Calculating the appropriate Equity IRR can be more of an art than a science. As extensive rate making of public utility commissions has shown, public advocates and private companies continually argue about the appropriate rates of return. It is rare that both sides agree on a public utility commission rate decision, underscoring the challenge of identifying the appropriate Equity IRR.

A solution to this challenge is the application of multiple triggers in the Concession Agreement. An example is the structuring of one trigger occurring at a specified level of return with the next trigger occurring at a higher-level return. In such structures, the amounts generally shared with the Department increase with each progressive trigger, or band.

Another reason for multiple triggers is to incentivize the Developer to continue to perform well and for the Department to receive its share of benefits above the trigger levels. However, such a benefit-sharing provision incentivizes the Developer only if the alternative is a categorical cap on the Developer’s revenue or

return (see Section 3.2.4 below) and the benefit of any incremental revenue or return the Developer retains under the provision is not unduly small.

An example benefit-sharing trigger provision is set forth below.

The amount of revenue paid to the [Department] shall be calculated at the end of each calendar year, commencing at the end of the calendar year in which the [Substantial Completion Date] occurs and continuing for each calendar year until the end of the [Term]. The revenue payment amount shall equal the sum of the following amounts (calculated based on the bands and revenue payment percentages reflected in [Exhibit [X]]):

- (a) the portion of the cumulative [Toll Revenues] to date above the band 1 band floor and up to the band 1 band ceiling as reflected in attachment 1 for the current year multiplied by the band 1 revenue percentage; plus*
- (b) the portion of the cumulative [Toll Revenues] to date above the band 2 band floor and up to the band 2 band ceiling as reflected in the attachment for the current year multiplied by the band 2 revenue percentage; plus*
- (c) the portion of the cumulative [Toll Revenues] to date above the band 3 band floor as reflected in the attachment for the current year multiplied by the band 3 revenue percentage; less*
- (d) any amounts paid by [Developer] to [Department] in previous calendar years; less*
- (e) any amounts that were deferred from a previous period and are now available.*

Exhibit [X] – Bands and Revenue Payment Percentages

Band	Toll Revenues Band Floor	Toll Revenues Band Ceiling	Revenue Payment Percentage
1	[A]	[B]	x%
2	[C + 1 cent]	[D]	y%
3	[D + 1 cent]		z%

3.2.3 Deriving Triggers through a Financial Model

As discussed, deriving a revenue trigger is relatively easy as it entails comparing the actual revenue in a period, such as a quarter, semiannual period, or year, to estimated revenue figures provided during the Project procurement process.

Deriving the return triggers generally requires using a financial model, which takes into account initial investments and the subsequent dividends to Equity Investors, interest payments to Lenders, and other forms of compensation, as well as operating costs. Many Concession Agreements rely on a “Base Case Financial Model” that is attached to the Concession Agreement or required to be placed into escrow. When the Developer’s actual return on equity exceeds the threshold contained in the Concession Agreement (which is generally set at a percentage above the Equity IRR projected in the Base Case Financial Model), the Concession Agreement’s benefit-sharing provisions will often be triggered.

Departments have many ways to ensure the integrity of the Base Case Financial Model. The Base Case Financial Model is generally developed and operated by the Developer and generally should be audited by an independent third party initially or regularly. The Department and its advisors often have full access to the Base Case Financial Model because a copy will have been placed into escrow at the outset of the Project. In addition, the accounts of the Developer are generally subject to regular audits, which are provided to the Department.

The revenue or return trigger calculations may be carried out periodically and the Concession Agreement may require a reporting function to alert the Department when the trigger thresholds have been reached. At that point, the Developer may be obligated to pay the Department its share of any revenue or return in excess of the trigger to the extent contemplated in the Concession Agreement.

The trigger calculations may show that the Department is owed sharing compensation in future periods. To the extent the Developer pays these amounts to the Department in advance of actually receiving the revenue (such as a lump sum payment), the Concession Agreement will generally incorporate mechanisms that ensure that the Department does not have to return any sharing compensation should the actual revenue or return the Developer receives be below the respective triggers.

3.2.4 *Sharing Caps and Collars*

In some European jurisdictions, some Concession Agreements establish caps and floors that limit both the upside and downside revenues of the Developer. Together they create a band that is generally set at the time of the signing of the Concession Agreement based on forecasted traffic levels or revenues. If traffic or revenues are lower than the band, then the Department may compensate the Developer based on a predetermined formula. If the band is exceeded, the Department may require the Developer to share much or all of revenues above the band, as established in the Concession Agreement, again leaving enough incentive for the Developer to continue to perform at the highest levels. These arrangements have been used in Europe but have not been adopted in the United States to date, and Departments that see a potential benefit in such an arrangement should carefully consider the extent to which applicable laws in their jurisdiction may prohibit them. In particular, the provisions providing for downside protection may be limited by statutes that prohibit guarantees of private obligations.

3.3 Revenue-Sharing Mechanics

3.3.1 *Treatment of Operating Costs, Capital Costs, and Grants*

As discussed above, revenue-sharing mechanics can be more complex when a return trigger is involved. One issue that often must be considered is that Departments are concerned that the Developer might “game” the calculation by creating operating costs that are not directly related to the operation of the Project, but are essentially substitute forms of dividends. This action would have the effect of transferring funds to Equity Investors without the amounts being counted as a return on equity for purposes of the return trigger. Unsubstantiated overhead charges may constitute such payments. For example, a parent company may charge each of its subsidiaries a portion of the cost of headquarters facilities, which may not be appropriate or allowable in the Concession Agreement. In theory, third-party auditing and the right to “see the books” at any time provides comfort to the Department that such expenses will be prevented.

The Department may also have concerns that certain operating expenses may not be in the public interest. For instance, many Departments prohibit contractors from invoicing for alcoholic beverages, donations, or entertainment costs. To provide guidance on ensuring that operating costs do not become a way for the Developer to earn returns from such costs, some Concession Agreements refer to using the Federal Contract Cost Principles and Procedures, 48 C.F.R. 31.205, as nonbinding guidance, or in cases in which Federal funding is contributed as a source of financing, then they are a requirement. The manner in which Federal requirements in this respect are incorporated varies from one Concession Agreement to another.

An example of such guidance provision is set forth below.

At the request of either party from time to time (but not more than once per year), the [Developer] and the [Department] will discuss in good faith possible adjustments to the operating costs, using the Federal Contract Cost Principles and Procedures, 48 C.F.R. 31.205, as nonbinding guidance to ensure that only reasonable and customary costs are included as operating costs.

Furthermore, if the Department is not satisfied with how the Developer has treated certain costs or calculated the benefit-sharing, it can revert to the dispute resolution provisions under the Concession

Agreement. Depending on the terms of the Concession Agreement, the Department can also revert to legal remedies.

An example of such dispute resolution provision is set forth below.

The [Department] shall have the right to dispute the [Developer]'s calculation of the [Concession Fee] or to request additional information, clarification or amendment of such calculation, at any time for a period of one year following the submission of the audit and other data referenced above. The [Developer] shall deliver to the [Department] such information, clarification or amendment within [X] days following the delivery of the [Department]'s request. If the [Department] does not agree with the calculation of the [Concession Fee], the dispute shall be resolved according to the dispute resolution procedures of the [Concession Agreement].

3.3.2 Timing Issues

Concession agreements have a variety of mechanisms when the revenue-sharing payment is made once a threshold has been reached and/or notice has been made that the Department is due a payment. Some payments may be made immediately in a lump sum; for others, the payments are made in the next major accounting period. Some may even allow for Refinancing Gain payments (see Section 3.3.3 below) to be paid over a period of time, subject to the requirement that the net present value of those payments is equal to as if the payment were made immediately.

3.3.3 Refinancing

A Developer may choose to refinance outstanding Project Debt and/or substitute its equity with additional debt during the Term. Such a refinancing may result in a large cash payment to the Developer or a reduction in debt service, thereby improving the Developer's cash flows.

An example provision providing for Department compensation in a refinancing is set forth below.

The [Developer] agrees to pay the [Department] such amount as compensation to the [Department] in exchange for the [Department]'s grant to [Developer] of rights to impose and receive tolls pursuant to this [Concession Agreement]. If the [Refinancing Gain] is greater than zero, the [Developer] shall pay to the [Department] an amount equal to [X%] of any such [Refinancing Gain].

Because a refinancing can generate substantial economic benefits to the Developer, Concession Agreements often require that such benefits are shared with the Department. Furthermore, such a refinancing may reduce the amount of equity, or “skin in the game” of the Developer, which may be contrary to the goals of the public entity and would need to be considered within context of Federal credit program requirements that borrowers have capital at risk in their business for the duration of the Federal loan.² Where the Developer is able to replace its existing debt with new debt having better than expected interest rates or where the Developer is able to raise additional debt to finance a cash payment to its Equity Investors, the Concession Agreement will generally require the Developer to share a percentage of the resulting financial benefit with the Department, subject to certain conditions (in some Concession Agreements, for example, the Developer may not be required to share any gains if it has not yet achieved its Equity IRR).

A refinancing may be contemplated in the original Base Case Financial Model for a Project. In these circumstances, the resulting financial benefits are integrated into the Developer's bid that is placed for the Project during procurement, and the Department will generally be deemed to have already taken the benefit. As a result, the resulting gain is not generally shared once the refinancing is actually undertaken.

²⁴Circular No. A-129: Credit Programs and Non-Tax Receivables”, Executive Office of the President, Office of Management and Budget, January 2013, Sections II C 1.b and III A.3.b.

If, however, the benefits were not expected at the signing of the Concession Agreement or they were uncertain, then sharing may be appropriate. This sharing may be required where a refinancing of the existing debt occurs that was not contemplated in the original Base Case Financial Model or if the Developer receives a TIFIA loan or is allowed to issue private activity bonds (PAB) under the U.S. Department of Transportation's (DOT) program that was not originally expected. These instruments result in lower debt service costs.

The Department may require the Developer to share a percentage of the Refinancing Gains not previously contemplated and such Refinancing Gains may also be required to be shared with other Project Debt providers.

An example of such sharing provision is set forth below.

The [Department]'s portion of the [Refinancing Gain] shall be calculated as if realized entirely in the year in which the refinancing occurs and the [Developer] shall pay to the [Department] the [Department]'s portion of the [Refinancing Gain] concurrently with the close of the refinancing; provided, however if the [Developer] demonstrates that it will only be able to actually make distributions on account of such [Refinancing Gain] over future years, then (a) the calculation of the [Refinancing Gain] shall be made on a net present value basis and (b) the [Department] shall reasonably approve and the parties shall set for in writing a payment schedule spreading payment of such portion of the [Refinancing Gain] over such future years corresponding with the anticipated timing of such future distributions such that these payments yield the same net present value to the [Department].

As throughout the Guide, these refinancing provisions refer to toll concessions. Refinancing provisions may vary for availability payment transactions.

4 Supervening Events

4.1 Introduction

During the Term, the Developer may encounter events or circumstances that negatively impact its ability to perform its obligations under the Concession Agreement within the time and/or cost originally projected for the Project. Some of these risks may be beyond the control of the Developer; others may be best managed by the Department. Accordingly, one of the key exercises in the preparation of any Concession Agreement is to allocate risk appropriately between the parties. To the extent that a risk allocated to the Department under the Concession Agreement arises during the Term, the Concession Agreement will generally provide contractual protection to the Developer.

As the global P3 market has developed (including in the United States), three different categories of these supervening events have broadly evolved. Terminology for each category of these events varies from jurisdiction to jurisdiction (and from State to State), but for the purposes of this guide, these three categories of supervening events can be described as follows:

- ▶ **Compensation Events** – a discrete set of events for which the Department broadly accepts the risk. To the extent that a Compensation Event arises during the Term, the Developer will typically be afforded sufficient protection in the Concession Agreement to ensure that, as result of the Compensation Event occurring, the Developer is not left in a better or worse position than it would have been had that Compensation Event not occurred. The aforementioned protection typically manifests itself in the form of compensation, relief from any failure by the Developer to comply with its obligations under the Concession Agreement as a direct result of the Compensation Event and (where necessary) extensions to deadlines that the Developer is required to meet under the Concession Agreement and is delayed in achieving as a direct result of the relevant Compensation Event.
- ▶ **Delay Events** – a discrete set of events typically outside of the Developer’s control, the risk of which the Developer is (relative to the Department) best placed to manage. Although the Concession Agreement would not typically require the Department to pay compensation to the Developer if a Delay Event occurs, the Concession Agreement would typically relieve the Developer from any failure to comply with its obligations under the Concession Agreement that arise as direct result of the Delay Event and (where necessary) extend deadlines that the Developer is required to meet under the Concession Agreement and is delayed in achieving as a direct result of the relevant Delay Event.
- ▶ **Force Majeure Events** – Force Majeure Events are generally a subset of Delay Events that are likely to have a catastrophic effect on the Project if they occur. In practice, their occurrence is highly unlikely, but termination rights can arise if they do occur.

4.2 The Role of Insurance to Mitigate Against Risk

Insurance is a key risk mitigant in any Project and for this reason it is not unusual for the Department to retain external insurance advisors in respect of a Project. The Developer will generally be able to take out advance loss of profit or business interruption insurance to mitigate against certain risks or events that arise during the Term, thereby providing a replacement revenue stream for Lenders and other parties dependent on the revenue of the Project. Such insurance will generally be subject to a deductible, so the occurrence of any such event may result in a material cost to the Developer. It should be noted, however, that such insurance is generally only available where there is physical damage to the Project and for the period that the Project is being reinstated.

Of the P3 transactions that have closed in the United States to date, several have categorized events that are either insurable or best managed by the Developer as Force Majeure Events, meaning that the Developer has the ability to terminate the Concession Agreement if the relevant Force Majeure Event continues for an extended period of time. Additionally, some Projects have included insurable events as Compensation Events, albeit that the level of compensation payable by the Department in the event that such risk arises is generally paid net of any Insurance Proceeds that are capable of being recovered. These approaches generally run contrary to international best practice for two reasons:

- 1) Except in exceptional circumstances (which are generally value-for-money driven), deductible risk and the risk of non-recovery under insurance policies is generally a Developer risk on the basis that the Developer is responsible for managing its insurance program.
- 2) The non-availability of insurance with respect to a risk should not, of itself, be sufficient justification for a particular risk being treated as a Force Majeure Event.

4.3 Categorization of Supervening Events

4.3.1 Compensation Events

Compensation Events consist of those events that are under the control of the Department, that are most efficiently managed by the Department or the risk of which represents value for money when assumed by the Department³. Such events are generally dealt with by compensation methods, rather than by being treated as defaults of the Concession Agreement by the Department, on the basis that termination should, at all times, be a last resort (although the Department may always elect to terminate the Concession Agreement at its convenience if it believes that the continuance of a Compensation Event renders the relationship between the parties untenable). The occurrence and/or continuance of a Compensation Event may cause the Developer to incur (a) a delay in the performance of its obligations under the Concession Agreement, (b) a loss of revenue, (c) an increase in its costs, or (d) buildup of third-party liabilities. Any compensation mechanism would generally allow the Developer to make a claim against the Department with respect to each of these exposures.

An example definition of Compensation Event is set forth below.

Compensation Event means the occurrence of any one or more of the following events or conditions:	
(a)	a breach of the [Concession Agreement] by the [Department] ⁴ ;
(b)	the construction or expansion of a [Competing Facility];
(c)	the development or implementation of any change in the [Work] or technical requirements applicable to the [Work] that the [Department] has directed the [Developer] to perform pursuant to a [Change Order] or a directive letter pursuant to the [Concession Agreement];
(d)	any [Discriminatory Change in Law];
(e)	one or more injunctions or other legal proceedings enjoining or estopping the [Developer] from the performance of its obligations pursuant to the [Concession Agreement], in any case for more than [X] days in the aggregate;
(f)	the imposition of (i) any State or local property tax or similar ad valorem tax or charge (including property taxes) or

³ Please see Section 4.3.4 below for a discussion of those risks that the Developer may encounter during construction that it may, on project specific grounds, represent value for money for the Department to take the financial risk of.

⁴ Amongst other things, this Compensation Event is intended to include any failure by the Department to (a) deliver certificates or approvals within time periods required under the Concession Agreement, (b) comply with its obligations in respect of Right of Way for the Project (in terms of either acquisition responsibilities or ongoing access), (c) ensure that the Developer has the ongoing ability to toll and collect tolls in respect of the Project

recordation tax on a deed, release or other document recorded in connection with the [Concession Agreement], unless recorded by or at the behest of the [Developer]; and (ii) any license fee or sales, use, receipts or similar tax on or measured by receipts or revenues levied, rated, charged, imposed or assessed by the State or any county, city or town of the State with respect to [Toll Revenues] paid to or collected by the [Developer] for travel on the [Project]; but excluding (x) any taxes of general application on overall net income or (y) any taxes levied, rated, charged, imposed or assessed in connection with any transfer during the [Term] of all or any portion of the [Developer]'s interest in the [Concession Agreement] or of any interest in the [Developer];

(g) (i) the enactment of any law after the [Proposal Due Date], or (ii) any change, amendment to, repeal or revocation of any law or in the interpretation or application thereof by any [Governmental Authority] after the [Proposal Due Date] that expands the vehicles exempted from the obligation to pay tolls on the [Project]; excluding, however, any such change in or new law enacted but not yet effective as of the [Proposal Due Date];

(h) [discovery of archeological, paleontological or cultural resources on the [Project Right of Way], excluding any such resources known to the [Developer] on the [Proposal Due Date]];

(k) any release of [Hazardous Substances] into the [Project Right of Way] by the [Department] or any [Department Related Party]; and

(l) an exercise by the [Department] within the [Project Right of Way] of its right to develop and pursue, anywhere in the world, entrepreneurial, commercial and business activities that are ancillary or collateral to the use, enjoyment and operation of the [Project] and [Project Right of Way] and the collection, use and enjoyment of [Toll Revenues] as provided in the [Concession Agreement],

provided, however, that each of the above events does not arise by reason of:

- (1) the negligence or misconduct of the [Developer] or its [Subcontractors]; or
- (2) any act or omission by the [Developer] or its [Subcontractors] in breach of the provisions of the [Concession Agreement].

4.3.2 Competing Facilities

Competing Facilities broadly consist of transportation facilities managed by or on behalf of the Department during the Term that are likely to reduce traffic (and therefore revenue) on the Project. The implementation of a Competing Facility will not generally result in any delay in performance by the Developer of its obligations, but there is a risk that it could lead to lower revenues for Developers. Because Developers (and their Lenders) invest substantial amounts of money in projects on the basis of certain traffic and revenue assumptions, they may be concerned about any potential development undertaken by the Department that is likely to reduce traffic. Departments, on the other hand, may be concerned about any contractual restriction that would constrain their ability to undertake necessary improvements to improve the transportation network in their jurisdictions.

The generally accepted approach is not to restrict the Department's ability to proceed with the development of any transportation facility, but rather to define a set of potential facility developments or improvements that would constitute a Competing Facility and to permit the Developer to claim a Compensation Event to the extent a facility undertaken by or on behalf of the Department falls within the agreed definition. The definition will often be limited in geography to the areas expected to be served by the Project and will generally exclude any transportation projects that are already under construction or planned at the time when bids for the Project are submitted (generally by reference to a medium-term transportation program or similar planning projection of the Department then in effect for the jurisdiction). The commercial characteristics of a Project may also be a factor in defining the scope of potential Competing Facilities, including non-road facilities. For example, the Developer of a Project that is expected to serve commuter traffic may not require protection against the development of a freight rail line immediately adjacent to it, but if the Project is expected to serve long-haul tractor trailer traffic, then the Developer may require protection.

Notwithstanding the foregoing, the location of the Project may also cause the Department to be concerned that future enhancements to neighboring facilities could enhance the Developer’s projected future revenues (e.g., through the introduction of additional interchanges or feeder roads). In such circumstances, the Department may seek to include a mechanism in the Concession Agreement that allows such additional revenue to be offset against any decrease in revenue attributable to the introduction of a Competing Facility.

Although each Project will be particularly unique in this regard, an example definition of Competing Facility is set forth below.

Competing Facility means any newly constructed or materially expanded transportation facility that is built and opened to traffic during the [Term] by (x) the [Department] or a private entity pursuant to a contract with the [Department] or (y) by any other [Governmental Authority] or a private entity pursuant to a contract with the [Governmental Authority], but only where the [Department] has discretionary authority to effectively prevent its construction or opening to traffic or to control its location; in each case, however, excluding the following:

- (a) all those highway projects excluded by statutes in effect on the [Proposal Due Date];
- (b) all highway projects included in any of the long range transportation plans and programs set forth in [Exhibit [X]] to this [Concession Agreement];
- (c) all highway projects located outside the competing facilities boundaries set forth in Exhibit [X] to this [Concession Agreement], and all projects located inside the competing facilities boundaries that are specifically listed as exclusions in such [Exhibit [X]];
- (d) all transportation projects and facilities that are not highway projects, including passenger and freight rail facilities;
- (e) any and all frontage roads, except as otherwise set forth in [Exhibit [X]] to this [Concession Agreement];
- (f) all work and improvements on highway projects necessary for improved safety, maintenance, or operational purposes;
- (g) all [High-Occupancy Vehicle] exclusive lane additions, or other work, on any highway project required by environmental regulatory agencies;
- (h) any work and improvements undertaken to increase traffic capacity by modifying already-constituted highway projects through the installation of traffic sensors, metering devices, intelligent vehicle highway system equipment or other intelligent transportation systems, through intersection grade separation, or localized operational improvements through the restriping of traffic lanes, medians, and shoulders, including restriping that adds lanes; and
- (i) changes to the [Project] directed by the [Department], unless such changes are operated by the [Department] or a person other than the [Developer] after completion.

4.3.3 Delay Events

Delay Events are events typically outside of the Developer's control, the risk of which the Developer is (relative to the Department) best placed to manage. Although the Developer typically takes any financial risk associated with the occurrence of Delay Events, the Concession Agreement would typically provide relief to the Developer in respect of any failure to comply with its obligations under the Concession Agreement that arises as direct result of the relevant Delay Event and (where necessary) provide a reasonable extension to any deadlines that the Developer is required to meet under the Concession Agreement and is delayed in achieving as a direct result of the relevant Delay Event.

An example definition of Delay Event is set forth below.

Delay Event means the occurrence of any one or more of the following events or conditions:

- (a) a [Force Majeure Event];
- (b) *[the discovery of an [Unknown Geotechnical Condition] during the carrying out of the [Construction Work]];

(c)	<i>*[the discovery of any [Unknown Endangered Species] during the carrying out of the [Construction Work]];</i>
(d)	<i>*[the discovery of any [Unknown Pre-Existing Hazardous Substances] during the carrying out of the [Construction Work]];</i>
(e)	<i>*[the discovery of any [Unknown Utility] during the carrying out of the [Construction Work]];</i>
(f)	<i>*a failure to obtain, or an unreasonable and unjustifiable delay in obtaining, a [Governmental Approval] by the deadlines specified in the [Concession Agreement];</i>
(g)	<i>any [Nondiscriminatory Change in Law];</i>
(h)	<i>a failure to relocate, or delay in relocating, by the deadlines specified in this [Concession Agreement] utilities by a utility with which the [Developer] has been unable to enter into an agreement providing for such relocation; or</i>
(i)	<i>a spill or other introduction of [Hazardous Substances] on the [Project Right of Way] after the [Proposal Due Date] other than by the [Developer] or its [Subcontractors],</i>
<i>except, in each case, to the extent attributable to any breach of this [Concession Agreement] by, or any negligent act, or negligent omission of, the [Developer] or any of its [Subcontractors].</i>	
<i>* see Section 4.3.4 (Differing Site Conditions) for a discussion of the circumstances in which the Developer may be granted Compensation Event relief in respect of these matters.</i>	

4.3.4 Unanticipated Circumstances during Construction

One of the key benefits of a greenfield project being undertaken as a P3 transaction is the transfer of certain risks associated with the Site to the Developer. The transfer of these risks is not wholly unique to a P3 transaction, but it is often more comprehensive than other procurement methods. Given that the level of Site related risks that the Project may be exposed to is, in part, a function of the Developer’s design, Departments are typically reluctant to retain any Site related risks (including permitting) in relation to the Project.

Notwithstanding the typical reluctance of Departments to retain Site related risks in respect of the Project, international experience (including in the United States) has demonstrated that the value for money impact of transferring Site related risks (including permitting) to the Developer needs to be carefully considered. In practice, the value for money of transferring these risks to the Developer is directly linked to (as relevant):

- a) the quality (and timing of provision) of relevant information made available to Proposers during the procurement process; and/or
- b) the extent to which Proposers are permitted to undertake their own Site investigations during the procurement process; and/or
- c) the extent to which Proposers are permitted to interact with (particularly in respect of permitting and utility related matters) the relevant governmental agencies and/or utility providers; and/or
- d) the location and/or nature of the Project.

It is extremely difficult to generalize about the extent to which unforeseen geotechnical risk, hazardous substance risk, utility risk and/or unanticipated discovery of endangered species should be treated as Compensation Events or Delay Events in Concession Agreements. By way of example, the Developer is likely to be much more sensitive to unanticipated risks relating to utilities on a downtown project than on a rural. Similarly, risks associated with delays are far more readily capable of being mitigated on projects where the construction work does not have to be undertaken sequentially, than on projects where it does.

Given that the approach to risk allocation in relation to these matters can vary significantly from project to project the example definition of “Compensation Event” does not include events relating to such risks, but

that is not to say that it is unusual for events relating to such risks to be included as Compensation Events. As previously mentioned, the circumstances surrounding any particular project may mean that it represents value for money for a particular risk to be accepted by the Department and included as a Compensation Event.

4.3.5 Force Majeure Events

The purpose of force majeure protection is to give the party affected by the relevant Force Majeure Event relief from liability and, if the event continues for an extended period, an opportunity to terminate the Concession Agreement. The definition of Force Majeure Event will generally be limited to those events that will likely have a catastrophic effect on either party's (although generally the Developer's) ability to fulfill its obligations under the Concession Agreement.

An example definition of Force Majeure Event is set forth below.

Force Majeure Event means the occurrence after the date of this [Concession Agreement] of:

- (a) *war, civil war, invasion, violent act of foreign enemy or armed conflict;*
- (b) *any act of terrorism or sabotage;*
- (c) *nuclear, chemical or biological contamination unless the source or cause of the contamination is brought to or near the [Site] by [Developer] or its [Key Contractors] or is as a result of any breach by [Developer] of the terms of this [Concession Agreement]; or*
- (d) *riot or civil commotion on or in the immediate vicinity of the [Project].*

In recognition of the general inability of the Developer to protect itself financially against the occurrence of Force Majeure Events through insurance, as well as the potential for Force Majeure Events to cause substantial damage to the Project and its long-term economic viability, the Concession Agreement will generally include an additional right of either party to terminate the Concession Agreement if a Force Majeure Event continues for an extended period of time. The other party will generally have a right to veto the election to terminate under these circumstances, provided that the vetoing party will be required to pay the cost of restoring the Project and continuing the Concession Agreement. In the event of a termination following an extended Force Majeure Event, the Concession Agreement generally requires the Department to pay termination compensation to the Developer as more fully described in Section 7.4 below.

Some transactions in the United States have also provided for a similar termination right if a Compensation Event or Delay Event continues for an extended period (often lasting several consecutive months). A Department may wish to consider the following points before agreeing to the inclusion of such a provision in a Concession Agreement:

- a) many Delay Events are insurable and provided the Developer places sufficient loss of revenue insurance to mitigate against the lost income suffered as result of the occurrence of an insurable event, there should be no need for either party to have a right to terminate;
- b) in the event of a substantial loss of the Project, reinstatement of the asset could take a significant period of time, perhaps in excess of the extended period of time that would otherwise give rise for either party to have the right to terminate the Concession Agreement;
- c) in the international P3 market, the inclusion of such a termination right is the exception, rather than the norm, principally because in the event of a termination, the Department will be required to pay a significant level of termination compensation to the Developer and nevertheless have a need to complete the construction and/or reinstatement of the Project; and

- d) the benefits of considering the inclusion of such a termination right on a risk by risk basis, rather than generically in respect of all Compensation Events and/or Delay Events.

An example provision permitting termination for an extended Force Majeure Event is set forth below.

If one or more [Force Majeure Events] occurring after the [Financial Close Date] results in the [Project] being substantially unavailable for public use or the suspension or substantial reduction of toll collections for a period in excess of (i) [X] consecutive days or (ii) [Y] days in the aggregate within any [Z]-day period, then:

(x) *the [Developer] may elect to terminate this [Concession Agreement] unless the [Department] elects, within [X] days following receipt of the [Developer]'s written notice of election to terminate, to treat such [Force Majeure Event] as a [Compensation Event]; and*

(y) *the [Department] may elect to terminate this [Concession Agreement] unless the [Developer] elects, within [X] days following such [Force Majeure Event], to restore any resulting damage or destruction at the [Developer]'s sole cost and expense and furnishes a restoration plan acceptable to the [Department] with respect to such damage or destruction, provided, however, in each case, that if this [Concession Agreement] is terminated, the [Department] will pay to the [Developer] the [Force Majeure Termination Sum].*

4.4 Types of Contractual Relief Generally Granted

4.4.1 Notice of occurrence of supervening event

The mere occurrence of a supervening event generally will not automatically entitle the Developer to relief. The Concession Agreement will often require the Developer to give notice of the occurrence of the supervening event within a specified period of time and to provide evidence to support the extent of the relief that is claimed. The burden of proof for any claim will be on the Developer, and the Department will generally be permitted to deny the requested relief if it is not sufficiently supported, subject to the right of the parties to submit any dispute relating to a claim (or denial thereof) to the dispute resolution procedures set out in the Concession Agreement.

An example provision providing for this notice and the provision of associated supporting information, using a Compensation Event as an example, is set forth below.

(a) *If at any time the [Developer] determines that a [Compensation Event] has occurred or is imminent, the [Developer] shall submit a written notice to the [Department]. The [Developer] shall identify the [Compensation Event] in reasonable detail, describe the [Developer]'s current estimate of the anticipated effects of the [Compensation Event], and include a written analysis of the calculation of the [Developer]'s current estimate of the [Net Cost Impact] and [Net Revenue Impact] resulting from the occurrence of the [Compensation Event].*

(b) *If the [Developer] fails to deliver such written notice within [X] days after the date on which the [Developer] first became aware (or should have been aware, using all reasonable due diligence) of the occurrence of the [Compensation Event], the [Developer] shall be deemed to have irrevocably and forever waived and released the portion of any claim or right to compensation for adverse effect on [Toll Revenues] and costs attributable to such [Compensation Event].*

(c) *Within [X] days after receiving the notice of a [Compensation Event] and the supporting documentation described in paragraph (a) above, the [Department] and the [Developer] will commence good faith negotiations to determine the amount of compensation, if any, to which the [Developer] is entitled.*

(d) *If, following issuance of any notice of a [Compensation Event] and during the period of analysis and negotiation described in paragraph (c) above, the [Developer] receives or becomes aware of any further information relating to the [Compensation Event] and/or actual or anticipated adverse or beneficial effects thereof, it shall submit such further information to the [Department] as soon as possible. The [Department] may request from the [Developer] any further information that the [Department] may reasonably require, and the [Developer] shall supply the same within a reasonable period after such request.*

(e) *The [Developer] shall conduct all discussions and negotiations to determine any compensation, and shall share with the*

[Department] all data, documents and information relating thereto, on an open book basis.

(f) *Following a determination of the [Compensation Amount] by mutual agreement or the dispute resolution procedures, the [Department] shall pay such amount to the [Developer] (a) through quarterly or other periodic payments, (b) in a lump sum, payable as determined by mutual agreement, or (c) by any other means mutually agreed by the parties; provided, however, in each case, that no method may be chosen if it will not yield an amount necessary to restore the [Developer] to the same economic position it would have been in had the [Compensation Event] not occurred.*

4.4.2 Relief for Nonperformance and Extension of Time to Key Dates

During the occurrence of a Compensation Event or Delay Event, the Developer will generally be excused from the performance of its obligations to the extent performance is prevented or delayed by the relevant Compensation Event or Delay Event. The Developer will often be required to continue performing those obligations not affected by the relevant Compensation Event or Delay Event and to mitigate the effects of the Compensation Event or Delay Event. Generally, the Developer’s obligation to pay money and its obligation to comply with applicable law and the Project’s technical requirements (except to the extent of a temporary inability to comply as a direct result of the relevant Compensation Event or Delay Event) will not be suspended.

The Developer’s obligation to meet construction milestones or other deadlines will often be suspended and such milestones and deadlines will generally be extended as part of the relief the Department provides. However, the length of the extension may not necessarily be day-for-day with the duration of the relevant Compensation Event or Delay Event. Concession Agreements will generally provide for an analysis of the critical path items actually impacted by the relevant Compensation Event or Delay Event, and may require that available float (or some portion thereof) in the then-current schedule be exhausted before an extension is granted. In addition, relief will not generally be granted where there are concurrent delays in the Work that are unrelated to the relevant Compensation Event or Delay Event (for example, where the Developer’s Design-Build Contractor is merely late in completing the Work). In addition, the Developer generally will not incur noncompliance/performance points under the Concession Agreement to the extent its performance failures are the result of a Compensation Event or a Delay Event.

An example provision providing for the calculation of time relief is set forth below.

(a) *During the performance of the [Construction Work], extensions of key milestones and/or activities identified in the most recent [Project Schedule] for [Compensation Events or Delay Events] affecting the [Work] will be made based on [Time Impact Analysis], and will extend each of the construction deadlines affected thereby.*

(b) *A [Compensation Event or Delay Event] will excuse the [Developer] from performance of its operations and maintenance obligations only to the extent such [Compensation Event or Delay Event] directly affects such obligations.*

(c) *For purposes of paragraph (a) above, **Time Impact Analysis** means a time impact analysis, (i) establishing the influence of an event on the most recent [Project Schedule], and will include a fragmentary network,⁵ and for events that have not yet occurred, the fragmentary network will demonstrate how the [Developer] proposes to incorporate such event in the most recent [Project Schedule], and (ii) demonstrating: (A) the time impact based on the date the event occurred or notice of a proposed change is given to the [Developer], (B) the status of the [Work] at such point of time; and (C) the time computation of all affected activities.*

⁵ A fragmentary network is generally a breakdown of the schedule into its component parts and (and their sub-parts) which substantiates the build-up of time needed to complete an activity

4.4.3 When Is Compensation Appropriate?

4.4.3.1 Calculating Compensation

In calculating the monetary relief payable to the Developer following a Compensation Event, the Concession Agreement will generally apply the principle that the Developer should be left in a no better or no worse position than it was in immediately prior to the Compensation Event. The net impacts to both costs and revenues will generally be considered, including by reference to estimates prepared by independent engineering firms and traffic and revenues consultants, respectively.

Once determined, monetary relief can generally be paid as a lump sum cash payment upfront, as a periodic fixed payment during the Term, as an adjustment to any revenue or Refinancing Gain-sharing mechanism contained in the Concession Agreement, or through such other means as the parties may agree. Some Concession Agreements may require the Developer to use commercially reasonable efforts to obtain financing to fund the Compensation Amount albeit on the understanding that the underlying commercial terms of the Concession Agreement may need to be amended in order to substantiate the Developer incurring such additional debt. This approach helps to alleviate the potential burden of a large lump sum payment on the Department; however, the failure of the Developer to actually raise financing will not prejudice its right to receive the amounts due.

An example provision providing for the calculation and payment of compensation is set forth below.

<p>(a)</p>	<p><i>The amount of any compensation payable with respect to any [Compensation Event] (such amount, the Compensation Amount) will be calculated based on the sum of (A) any adverse [Net Cost Impact] and (B) any adverse [Net Revenue Impact] for each year that there is an impact attributable to such [Compensation Event]; provided, however, that, subject to paragraph (c) below, any [Net Cost Savings] and positive [Net Revenue Impact] attributable to such [Compensation Event] will be used to decrease the [Compensation Amount]. The calculation of the [Compensation Amount] will be based on the difference in the projected cost and revenue related to the [Project] immediately prior to the occurrence of the [Compensation Event] and the projected cost and revenue related to the [Project] after taking into account the impact of the [Compensation Event].</i></p>
<p>(b)</p>	<p><i>For purposes of this [Concession Agreement]:</i></p> <p>(i) Net Cost Impact means the aggregate value of any net increase in the [Developer]'s costs reflected on an annual basis directly attributable to a [Compensation Event], as compared with what the [Developer]'s costs would have been absent the occurrence of the [Compensation Event], less the increased costs that can reasonably be mitigated by the [Developer].</p> <p>(ii) Net Cost Savings means the aggregate value of any decrease in the [Developer]'s costs reflected on an annual basis directly attributable to a [Compensation Event] as compared with what the costs would have been absent occurrence of a [Compensation Event], but excluding any savings in costs taken into account to reduce the [Net Cost Impact] attributable to such [Compensation Event].</p> <p>(iii) Net Revenue Impact means the aggregate value of any net increase or decrease in [Gross Revenues] reflected on an annual basis directly attributable to a [Compensation Event], less any lost [Gross Revenues] that can reasonably be mitigated by the [Developer] (excluding any mitigation of costs subtracted from [Net Cost Impact] for the same [Compensation Event]).</p>
<p>(c)</p>	<p><i>Following a determination of the [Compensation Amount] pursuant to paragraph (a) above, the [Department] will compensate the [Developer] for such [Compensation Amount] in such manner as agreed upon by the parties in writing or as may be determined through the dispute resolution procedures; provided, however, that:</i></p> <p>(i) <i>in the case of any lump sum payment of the [Compensation Amount] or any other payment schedule that differs from the projected timing of the [Compensation Amount], the present value of the [Compensation Amount] will be determined using the then appropriate risk adjusted discount rate(s), as agreed between the [Department] and the [Developer]; and</i></p> <p>(ii) <i>the amount and timing of payment of the [Compensation Amount] related to a [Compensation Event] will</i></p>

take into account the ability of the [Developer] to obtain funding in relation to such [Compensation Amount] in accordance with paragraph (d) below and will take into account the ability of the [Developer] to have available funds at such times as the [Developer] is required to make payments to third parties in respect of any [Compensation Amount].

- (d) *If requested by the [Department], the [Developer] will use commercially reasonable efforts to obtain funding for the [Compensation Amount]; provided, however, that the [Developer] will not be obligated to obtain such funding if the [Developer], in its reasonable discretion, determines that obtaining such funding will diminish the [Project Value]. If the [Developer] is able to obtain funding for all or part of the [Compensation Amount], the [Developer] will submit a funding proposal for the [Department]'s review and approval. Such funding proposal will identify the terms and conditions required to secure funding for such [Compensation Amount], including any proposed adjustments to the toll rate schedule, proposed extensions of the [Term] and/or proposed payments by the [Department]. The [Department] will reject or accept the funding proposal within [X] days of receipt of the funding proposal. If the funding proposal is accepted by the [Department], the [Department] will issue a [Change Order] to implement the funding proposal and, to the extent such funding proposal secures financing for less than 100% of the [Compensation Amount], the [Change Order] will provide funding for the remainder thereof on terms and conditions mutually agreed by the parties.*

4.4.3.2 Deductibles – Factors to Consider

Some Concession Agreements include so called “deductibles” in respect of certain Compensation Event claims that require the Developer to absorb the financial impact of specific risks before the Department is required to pay compensation. A deductible might be applied on a per claim basis or on an aggregate basis across all claims for a particular risk or basket of risks.

The merits of utilizing deductible arrangements in the context of Compensation Event claims is debatable and requires complex analysis by Departments. On the one hand, the use of deductibles can be an attractive proposition to the Department as it reduces the likelihood of the Developer making claims against the Department during the Term, and any contingency that the Developer includes in its pricing is passed on to users of the Project as it will be reflected in the toll pricing. On the other hand, the inclusion of contingency by the Developer in its construction pricing does, by definition, bring with it the risk that the users of the Project may ultimately pay for something that they do not receive (i.e., if the risk does not materialize), which can be unattractive on public policy/value for money grounds.

Accordingly, to the extent that the Department proposes to apply deductibles to certain Compensation Event claims, it will be important for the Department to be confident that such an arrangement represents better value than fully compensating the Developer in respect of the financial impact of the relevant Compensation Event.

4.4.3.3 Extensions to the Term

The Department may wish to reserve the right to extend the Term to compensate the Developer for a Compensation Event. Doing so will provide the Developer with additional years of revenue that may be used to offset its Losses and will permit the Department to avoid having to pay a large sum of money out of its then current operating budget (or reserves).

However, this remedy may not be wholly satisfactory to the Developer in circumstances where the Compensation Event has caused the Developer to incur substantial out-of-pocket costs or loss of revenue in a short period of time because the promise of revenue several years or even decades in the future will not resolve an immediate funding gap and the Developer may nevertheless have to seek additional financing to cover the gap. However, a Term extension may be a more welcome remedy where the impact of the Compensation Event is less acute and its primary effect is to reduce the Developer’s Equity IRR over the original Term (without impacting the Developer’s ability to service its ongoing debt obligations). Under those circumstances, the Developer may be less concerned about immediate funding needs and may take

more comfort from the promise of additional years of revenue to restore its Equity IRR. Because the utility of the remedy is uncertain, however, Developers may seek a right in the Concession Agreement to determine how and when this remedy is exercised.

In some jurisdictions, authorizing statutes limit the permissible length of a Concession Agreement. If the initial Term is equal, or nearly equal, to this upper limit, then this remedy may be unavailable or of only limited value.

5 Changes in Equity Interests

5.1 Introduction

In the early stages of the procurement process for any P3 transaction, the Department will generally solicit requests for qualification from prospective bidder teams in the market. The Department will generally evaluate each respondent in a number of predetermined areas, concluding with the shortlisting of several bidders who are then invited to submit detailed proposals.

As part of the aforementioned evaluation, an assessment is generally undertaken of the respondent team's Equity Investors' credentials, principally in the following areas:

- ▶ Availability of capital that can be committed to invest in the Project.
- ▶ Experience investing in similar projects.
- ▶ Demonstrated ability to manage effectively all aspects of future work on the Project.
- ▶ To the extent relevant, experience of managing the self-performance of operations and/or maintenance by special-purpose Developers that choose not to subcontract out those responsibilities on a long-term basis.

During the competitive bidding process, the Department will generally reserve for itself approval rights with respect to changes to certain key members of a bidder's team. The reservation of such rights affords the Department the opportunity to ensure that the qualifications of each bidder team (which led to those teams being shortlisted) cannot be eroded through changes being made to key members of the teams. As a general rule, if a bidder team requests approval of a change to a key member of its bidding team, the Department should only approve any such request if it can be confident that the proposed change does not have an adverse impact on the Department's original evaluation of the bidder team's credentials.

The Department's concerns with respect to changes to members of the bidding team during the competitive bidding process apply equally during the Term. Accordingly, the Concession Agreement will generally include provisions that require the Department's approval to certain changes in the identity of the Developer's investors or supply chain members.

For the purposes of this guide, discussion is limited to the extent to which the Department should have approval rights with respect to any Change in Ownership of the Developer (i.e., changes in the ultimate ownership, either directly or indirectly, of the equity interest in the Project).

5.2 When Does a Change in Ownership Occur?

Broadly, a Change in Ownership can arise in one of two ways:

- 1) **Directly** – i.e., through a change in the ownership of shares or membership interests in the Developer.
- 2) **Indirectly** – i.e., as a result of a change in the ownership of shares or membership interests in any entity that is a direct or indirect holding company of shares or membership in the Developer.

Although the Concession Agreement will generally include provisions relating to direct changes in the ownership of shares or membership interests in the Developer, the Department will also generally seek to ensure that the provisions of the Concession Agreement capture a change in the ownership of any shares or

membership of any entity in the vertical ownership chain between the Developer and the relevant investors that were first evaluated by the Department in putting together the shortlist of bidders for the Project.⁶

The Department will want to ensure that any Change in Ownership restrictions cannot be circumvented through sophisticated legal structuring of equity transfers and accordingly, any such restrictions would generally capture transfers of any interest (legal, beneficial, or equitable) in shares or membership interests, together with transfers of economic interest in the same (e.g., voting or dividend rights).

An example definition of Change in Ownership is set forth below.

Change in Ownership means:	
(a)	any sale, transfer or disposal of any legal, beneficial or equitable interest in any or all of the shares or membership interests in the [Developer] and/or any [Related Entity];
(b)	in respect of any of the shares or membership interests referred to in (a) above, any change in the direct or indirect control over:
(i)	any voting rights conferred on those shares or membership interests; or
(ii)	any right to appoint or remove directors; or
(iii)	any right to receive dividends or distributions); and
(c)	any other arrangements that have or may have or which result in the same effect as paragraph (a) or (b) above,
Related Entity means [Names of each entity to be incorporated from the Successful Proposer's Proposal] [Note to Proposers: Each Related Entity shall be those entities that were evaluated for the purposes of the RFQ short-listing process, or as otherwise approved by the Department pursuant to the RFP]. ⁷	

5.3 Common Equity Investor Concerns

In contrast to the concerns of the Department, the Equity Investors in the Project will want maximum flexibility to transfer their interests in the Developer throughout the Term. Although such a level of free transferability is unlikely, Departments do generally recognize that permitting transfers of equity interests in projects allows Equity Investors to free up capital for other projects and generally makes the market more liquid, which in turn can help improve pricing on the Project. Additionally, Equity Investors in the Project, particularly investment or pension funds, may be required to diversify their interest in certain sectors over time, and restricting transfer, particularly in relation to a long-term concession, may have the effect of deterring potential investors in the Project.

5.4 Permitted and Prohibited Changes in Ownership

To the extent that the Developer's ability to perform its obligations under the Concession Agreement will not be prejudiced by a direct or indirect change in ownership, the Developer and its investors will generally maintain that the Department should not have an approval right over such Change in Ownership. However,

⁶ The change in ownership provisions are in contrast to general restrictions on assignment and transfer, which cover a direct transfer or sale of the Project from one Developer to another Developer.

⁷ Depending on the Department's requirements with respect to indirect changes in ownership. This definition would generally include each entity in the ultimate ownership structure between the Developer and either (a) each relevant investment entity that was evaluated for the purposes of determining the shortlisted bidders in the Project and/or (b) any parent of such investment entity not evaluated for purposes of determining the shortlisted bidders in the Project but that the Department considers important to the success of the Project.

best practice in the United States and internationally has tended to adopt the following principles in connection with permitted and prohibited Changes in Ownership:

- 1) At all times during the Term, any Change in Ownership arising from a transfer of shares or membership interests to a Prohibited Person is prohibited.
- 2) Subject to paragraph (3) below, Changes in Ownership are prohibited until the end of the Defects Liability Period (generally two to five years following Substantial Completion). Generally speaking, the Department will take comfort from the ongoing involvement of the original Equity Investors in the Project until construction has been completed. Amongst other things, the concern for the Department will be that the incoming investor may disrupt momentum in the delivery of the construction and introduce new relationships into the Project at a critical time.
- 3) Changes in Ownership that result from a transfer of shares or membership interests between affiliated entities are generally permitted.⁸
- 4) Once the Defects Liability Period has expired, Changes in Ownership are generally only prohibited to the extent that it would reasonably be likely to prejudice the Developer’s ability to perform its obligations under the Concession Agreement. By way of example, if the Developer self-performed its operation and maintenance responsibilities (and its ability to do so was principally a function of the outgoing investor’s experience in managing operation and maintenance), the Department may wish to consider the incoming investor’s experience of managing the operation and maintenance of similar projects.

5.5 Example Provisions

An example Change in Ownership provision is set forth below.

(a)	<i>A Restricted Change in Ownership shall arise if:</i>
(i)	<i>at any time on or before the last day of the [Defects Liability Period], any [Qualified Investor] ceases to own (directly or indirectly) the same percentage of the issued share capital or membership interests in the [Developer] that it owned (directly or indirectly) at the date of this [Concession Agreement];</i>
(ii)	<i>a [Change in Ownership] occurs which involves the transfer of any shares or membership interests to a [Prohibited Person]; or</i>
(iii)	<i>a [Change in Ownership] occurs which would be reasonably likely to have a material adverse effect on the [Developer]’s ability to perform its obligations under the [Transaction Documents], taking into account the financial strength and integrity of the transferee, compared to that of the transferor.</i>
(b)	<i>Any [Restricted Change in Ownership] will constitute a [Developer Default] for the purposes of [Section [X] (Termination for Developer Default)].</i>
(c)	<i>A [Restricted Change in Ownership] shall not arise pursuant to paragraph (a) above as a direct result of:</i>
(i)	<i>the grant or enforcement of security in favor of the [Lenders] over or in relation to any shares or membership interest in the [Developer] under the [Financing Documents];</i>
(ii)	<i>a change in legal or beneficial ownership of any shares that are listed on a recognized stock exchange, including without limitation such transactions involving any public offering; or</i>
(iii)	<i>a transfer of interests between managed funds that are under common ownership or control or between the general partner, manager or the parent company of such general partner or manager and any managed funds</i>

⁸ With respect to transfers between affiliated funds, the Department may wish to ensure that a transfer of interests between two funds managed by the same fund manager represents a transfer between similar funds and that the fund manager is not simply “fronting” for a single investor.

under common ownership or control with such general partner or manager (or parent company of such general partner or manager), provided that the relevant funds and the general partner or manager of such funds (or the parent company of such general partner or manager) have been approved by the [Department] in writing prior to the date of this [Concession Agreement].

- (d) *For the purposes of paragraphs (a) through (c) above, a person will only be deemed to own shares or membership interests in another person if such person owns the legal, beneficial and equitable interest in the relevant shares or membership interests of that other person.*
- (e) *Except in respect of any change in legal or beneficial ownership of any shares that are listed on a recognized investment exchange, the [Developer] shall provide the [Department] with at least [X] days prior written notice of any [Change in Ownership].*
- (f) *The [Developer] agrees to reimburse the [Department] for all reasonable out-of-pocket expenses (including, without limitation, reasonable and proper fees of consultants and legal counsel) incurred by the [Department] in connection with its review of any [Change in Ownership] that it receives notice of pursuant to (e) above.*

6 Change in Law

6.1 Understanding the Concerns of All Parties

A core requirement of the Concession Agreement should be for the Developer to comply, and cause all of its Subcontractors to comply, with all applicable law in the development and operation of the Project. A failure to comply with this requirement may ultimately result in termination for Developer Default (see Chapter 7 (Defaults, Early Termination, and Compensation)). Accordingly, to the extent that a Change in Law arises during the Term, the Developer may need to incur additional costs to comply with the requirements of the Change in Law.

Broadly speaking, there are two questions that are generally discussed when determining whether the Developer should be protected against the financial impact of a Change in Law:

- 1) Was the Change in Law foreseeable (e.g., based on publicly available information such as draft legislation) at the time the Developer submitted its final bid?
- 2) In the absence of being contractually protected against any negative impact of a Change in Law on the Developer's business, is the Developer in any other way able to mitigate such negative impact without negatively impacting its own financial position?

Except in unique circumstances, costs and timing impacts of complying with current or foreseeable laws are generally for the account of the Developer and are therefore required to be priced into the Developer's bid. Thus, the question then becomes to what extent the Developer should be contractually protected when unforeseeable Changes in Law arise during the Term.

6.2 Unforeseeable Changes in Law – Relevant Considerations

Developers generally express the view that Change in Law is a risk that they cannot control and that the Department is better placed to manage. In practice, however, Departments only have influence over certain categories of legislation. Accordingly, some level of risk sharing is generally seen as being appropriate in respect of Changes in Law.

Consequently, most Departments have (consistent with international best practice) focused on the following three issues when considering the extent to which the Developer should be protected against unforeseeable Changes in Law:

- 1) Should the Developer be protected with respect to the negative financial impact of all categories of unforeseeable Changes in Law?
- 2) Should the Department bear the risk of the negative impact on the Developer of Changes in Law introduced at all levels of government?
- 3) Should the Developer be protected with respect to any increases in taxes or the introduction of new taxes that, in each case, either increase the Developer's costs or have a negative impact on the after-tax return of investors in the Developer?

Any consideration of the above issues is generally undertaken in conjunction with an assessment of the circumstances under which the Developer can increase toll rates and the toll rate setting policy generally. This relationship is particularly relevant when considering the extent to which the Developer should be protected with respect to a Change in Law that results in an increase in the Developer's operating costs.

That is not to suggest that the Developer is generally permitted to apply one-off increases in toll rates in the event of a Change in Law, but rather that the toll rate setting policies will often permit annual increases in line with indexation and, by definition, indexation of the tolls may, over time, provide a suitable hedge against certain categories of Change in Law (e.g., a general increase in corporation tax).

6.3 Trends in the United States P3 Market

Consideration by Departments of the issues highlighted in Section 6.2 above have broadly resulted in the emergence of three relatively consistent themes:

- 1) The Developer generally bears any negative financial impact associated with any unforeseen change in Federal law on the basis that (unlike with respect to other transportation sectors (e.g., aviation) regulation of highways is largely devolved down to State government, the private business community is as well (if not better) placed as any Department to address any pending Change in Law, and (subject to the terms of the toll rate schedule) an increase in toll rates may afford some level of “hedge” against any negative impact of such a Change in Law.
- 2) With respect to any unforeseen change in a non-Federal law, the Department only bears any negative financial impact associated with such Change in Law to the extent that it is a “Discriminatory Change in Law” (see Section 6.5 below for a discussion of the definition of Discriminatory Change in Law).
- 3) The negative financial impact associated with any “Nondiscriminatory Change in Law” are generally borne by the Developer, except that with respect to changes in sales tax rates or exemptions (whether of general application to suppliers or not), protection is often afforded to the Developer (see Section 6.6 below).

6.4 Compensation, Relief from Delay, and Mitigation

Discriminatory Changes in Law (for which the Department bears all of the risk) are generally Compensation Events, meaning that the Developer is entitled to claim compensation and performance relief (e.g., an extension of time), so as to ensure that the Developer is left in a no better and no worse position than it would have been in had such Discriminatory Change in Law not arisen. With respect to any other unforeseeable Change in Law, these are generally treated as Delay Events, meaning that the Developer is only afforded performance relief with respect to such Change in Law. Chapter 4 (Supervening Events) sets forth the process that applies to any Compensation Event or Delay Event claim that the Developer proposes to make during the Term.

As with any other Compensation Event, a key concern for the Department will be to ensure that the Developer mitigates the negative impact associated with any Discriminatory Change in Law. Given that any Discriminatory Change in Law will most likely apply beyond the limits of the Project, this duty to mitigate should be capable of being measured, in part, by reference to the extent to which price increases in comparable sectors are experienced. It will also require the Developer to foresee and anticipate the effect of Changes in Law, particularly in relation to expenditures which it has already planned to incur in the performance of its obligations under the Concession Agreement. For example, the Developer cannot on one day replace the overhead lighting on the Project under its normal maintenance program and then argue that it immediately has to replace it due to a subsequent Change in Law which the Developer should have anticipated at the time of the replacement. For that reason, any compensation should reflect any anticipated future savings of maintenance costs.

6.5 Discriminatory Changes in Law

Generally, a Discriminatory Change in Law will arise if the relevant Change in Law is not applicable across all modes of business. For example, an increase in corporation tax or capital gains tax of broad application will not constitute a Discriminatory Change in Law. Similarly, a Change in Law that relates to the operating standards of all highways in the United States would not be considered to be a Discriminatory Change in Law, whereas a Change in Law that is purely targeted at private operators of toll roads would. In broad terms, the concept of equivalence can be said to determine whether a Change in Law can be categorized as a Discriminatory Change in Law—if the change is targeted at one business community or asset class that competes against another business community or asset class that is not impacted by such change, the relevant change will generally be considered to be a Discriminatory Change in Law.

6.6 Tax-Related Issues

Discriminatory changes in tax law should come within the definition of Discriminatory Change in Law provided above.

Changes in tax law of general application would not generally afford the Developer any right to receive compensation under the Concession Agreement, except with respect to the following categories of Nondiscriminatory Changes in Law:

- ▶ With respect to the procurement of goods and materials by the Developer during the Construction Period, any revocation of sales tax exemption (particularly in States where materials procured pursuant to public works contracts are exempt from such taxes).
- ▶ Any introduction or increases in sales tax on tolls paid by users of the Project.

6.7 Example Provisions

An example compliance with laws provision and associated definitions are set forth below.

<p>(a) <i>The [Developer], in addition to performing all other requirements of the [Transaction Documents], shall comply with, and require that all its [Subcontractors] comply with, all requirements of all applicable laws.</i></p> <p>(b) <i>To the extent that any [Discriminatory Change in Law] arises during the [Term], the [Developer] may exercise its rights pursuant to [Section [X]] (Compensation Events).</i></p> <p>(c) <i>To the extent that any [Nondiscriminatory Change in Law] arises during the [Term], the [Developer] may exercise its rights pursuant to [Section [X]] (Delay Events).</i></p> <p>Change in Law means:</p> <p>(a) <i>the enactment of any [Law];</i></p> <p>(b) <i>any change, amendment to, repeal or revocation of any [Law] or in the interpretation or application thereof by any [Governmental Authority], excluding, however, any change in or new [Law] which was foreseeable as of the [Setting Date].</i></p> <p>Discriminatory Change in Law means:</p> <p>(a) <i>any [Change in Law] [with respect to [Laws] of the State and any county, city or town of the State] that has the effect of discriminating solely against the [Project], the [Developer], or private operators of [tolled transportation assets] in the State, except where such [Change in Law] is (a) in response, in whole or in part, to any (i) failure to perform or breach of the [Concession Agreement], (ii) violation of [Law] or [Governmental Approval], or (iii) culpable act, omission or negligence on the part of any [Related Entity], or (b) otherwise permitted under the [Concession Agreement]; or</i></p> <p>(b) <i>a [Relevant Tax Event].</i></p> <p>Law means all laws, treaties, ordinances, judgments, Federal requirements, decrees, injunctions, writs and orders of any [Governmental Authority], and all rules, regulations, orders, formal interpretations of any [Governmental Authority] that are</p>

applicable to the Developer, the Project or the Work., in each case as the same may be amended from time to time.

Nondiscriminatory Change in Law means a [Change in Law] which is not a [Discriminatory Change in Law].

Relevant Tax Event means:

- [(i) any State or local property tax or similar ad valorem tax or charge or recordation tax on a deed, release or other document recorded in connection with the [Concession Agreement], unless recorded or at the behest of the [Developer]]; and*
- [(ii) any license fee or sales, use, receipts or similar tax on or measured by receipts or revenues levied, rated, charged, imposed or assessed by the State or any county, city or town of the State with respect to [Toll Revenues] paid to or collected by the [Developer] for travel on the [Project];*

but excluding (a) any taxes of general application on overall net income or (b) any taxes levied, rated, charged, imposed or assessed in connection with any [Transfer] during the [Term] of all or any portion of the [Developer]'s interest in the [Project] or of any interest in the [Developer].

Setting Date means [the date falling [45] days prior to the [Proposal Due Date]].

7 Defaults, Early Termination, and Compensation

7.1 Introduction

The intention of the parties to any Concession Agreement should be that it will run its full course and terminate on the last day of its Term. However, situations may arise during the Term that take either party beyond its point of indifference, to the point where the ability to call a default is necessary, along with the ability to (in the absence of cure of the relevant default) terminate the Concession Agreement. Accordingly, the Concession Agreement will generally:

- ▶ Define the circumstances under which the Concession Agreement may be terminated early.
- ▶ Define the circumstances under which either party will be in default under the Concession Agreement.
- ▶ Where appropriate, provide the defaulting party with the ability to cure the relevant default.
- ▶ Set out the process that the non-defaulting party must follow if it elects to terminate the Concession Agreement.
- ▶ Specify precisely what compensation (if any) is payable by the Department to the Developer if the Concession Agreement is terminated early.

Early termination can generally be caused by Department Default, Developer Default, or a Force Majeure Event. It can also generally be caused by the Department exercising a right to terminate the Concession Agreement voluntarily, for its own convenience. This guide looks at each of these early termination scenarios and discusses the issues generally of concern to each party in the relevant scenario.

In addition to the termination scenarios described more fully below, Concession Agreements will also typically be terminable by the Department if the Developer fails to achieve the Financial Close Date by a specified deadline. Where the failure to achieve financial close is outside the control of the Developer, the Department will, if permitted by applicable law, typically pay the Developer a fee to reimburse a portion of the Developer's costs associated with attempting to reach financial close.

Concession Agreements may also include a right of the Developer to receive termination compensation (typically equal to the amount that would be payable following a termination for extended Force Majeure Events, as described in Section 7.4 below) if a ruling is issued by a court of competent jurisdiction that declares the Concession Agreement void or unenforceable, or that renders performance substantially impossible. The inclusion of such a termination right may or may not be appropriate in the context of a particular Project, and Departments should consult their legal advisors to determine the scope of such a provision, if appropriate.

7.2 Termination for Department Default

7.2.1 *Events Giving Rise to Department Default*

The Developer is generally allowed to terminate the Concession Agreement in circumstances where the Department acts in a way which either (a) renders the parties' contractual relationship untenable or, (b) completely frustrates the Developer's ability to perform the services that are the subject of the Concession Agreement. A minor breach of the Concession Agreement would not generally fall into this category and even a material breach is likely to be insufficient if the Department's actions do not have either of the aforementioned effects. Termination by the Developer should be a last resort. It is important to ensure that

there are no “hair trigger” defaults that could put the Department at risk of termination before it has had an opportunity to cure its default.

Accordingly, the Department needs to have a thorough understanding of both the scope of its obligations under the Concession Agreement and the likelihood of it breaching those obligations when determining both the scope of the definition of Department Default and the extent to which cure periods should be required in respect of Department Defaults. As a general point, however, when assessing the likelihood of a Department Default occurring under the Concession Agreement, Departments generally take comfort from the fact that their obligations under the Concession Agreement are far less substantive than those of the Developer.

Although the scope of a common definition of Department Default is, in contrast to the definition of Developer Default, very limited, Developers generally are comfortable with this approach because a failure by the Department to comply with its obligations under the Concession Agreement can in most cases be adequately dealt with by way of a Compensation Event (see Chapter 4 (Supervening Events)), and any failure by the Department to make a payment when due generally gives rise to interest on late payment being payable.

An example definition of Department Default is set forth below.

Department Default means the occurrence of any one or more of the following events or conditions:

- (a) any representation or warranty made by the [Department] in this [Concession Agreement] is false or misleading or inaccurate when made or omits information when made, the effect of which is to have a material adverse effect on the [Project Value] or the [Developer]’s ability to perform its obligations or exercise its rights under the [Concession Agreement];
- (b) the Department fails to comply with any of its material obligations under this [Concession Agreement] and such failure has a material adverse effect on the [Project Value] or the [Developer]’s ability to perform its obligations or exercise its rights under the [Concession Agreement]; or
- (c) any confiscation, sequestration, condemnation or appropriation of a material part of the [Project], the equity interests in the [Developer] or the [Developer]’s rights under the [Concession Agreement], in each case except to the extent permitted under the terms of this [Concession Agreement].

7.2.2 Department Default Cure Periods

To the extent that a Department Default arises, the Department would, except in limited circumstances, generally have the benefit of a cure period. The purpose of a cure period is to allow the defaulting party an opportunity to cure the relevant default and avoid the early termination of the Concession Agreement for its default. The appropriateness of a Department Default having a cure period is generally a function of the nature of the Department Default: a Department Default that is unlikely to be curable or that arises as a result of an affirmative action being taken by the Department would not generally benefit from a cure period.

The length of any cure period will be an issue of concern to both parties to the Concession Agreement. In particular, Developers are generally uncomfortable with long cure periods if they have no ability to terminate the Concession Agreement in the event that the Department is not taking positive action to cure the relevant Department Default during the cure period. Accordingly, cure periods for covenant defaults of the Department are often set at relatively short periods (e.g., 30 days), but may then be extended (provided that the Department is diligently attempting to cure the default and subject to a maximum extension period) if the initial period is an unreasonable period of time for the Department to cure the relevant Department Default. Payment defaults of the Department, however, typically have a relatively longer cure period (e.g., 45-60 days), but will not be subject to any extension.

With reference to the example definition of Department Default shown in Section 7.2.1 above, an example provision relating to the cure period for a Department Default is set forth below.

- (a) *The Developer shall provide written notice to the [Department] of the occurrence of a [Department Default]. Upon receipt of the [Developer]’s notice, the [Department] shall have the following cure periods with respect to the following [Department Defaults]:*
- (i) *for a [Department Default] referred to in paragraph (a) of that definition, a period of [X] days after the [Developer] delivers to the [Department] the written notice of such a [Department Default] or, to the extent that the [Department Default] is capable of cure and the [Department] has, despite using its best efforts, failed to cure such [Department Default] within the [X] day period, such cure period may be extended by such additional period as may be reasonably necessary to cure such [Department Default], subject to a maximum extension of [X] days;*
 - (ii) *for a [Department Default] referred to in paragraph (b) of that definition, a period of [X] days after the [Developer] delivers to the [Department] the written notice of such a [Department Default] or, to the extent that the [Department Default] is capable of cure and the [Department] has, despite using its best efforts, failed to cure such [Department Default] within the [X] day period, such cure period may be extended by such additional period as may be reasonably necessary to cure such [Department Default], subject to a maximum extension of [X] days; and*
 - (iii) *for any other [Department Default] not referred to in paragraph (a) or (b) above, there is no cure period.*
- (b) *Any extension of a cure period in accordance with sub-paragraph (a)(i) or (a)(ii) above is subject to the [Department] continuing to use its best efforts to cure or cause to be cured such [Department Default] during the period of such extension.*
- (c) *In the event that a [Department Default] occurs and it has either not been cured within any relevant cure period or (in the case of an extended cure period) the [Department] ceases to use its best efforts to cure the [Department Default], the [Developer] may terminate this [Concession Agreement] in accordance with [Section X] (Developer’s Rights to Terminate for Department Default)].*

7.2.3 Developer’s Rights to Terminate for Department Default and Procedure

An example provision permitting the Developer to terminate the Concession Agreement for Department Default is set forth below.

- (a) *If a [Department Default] occurs and it has not been cured within any relevant cure period set out in [Section X], the [Developer] may serve a termination notice on the [Department] at any time during the ongoing continuance of that [Department Default].*
- (b) *A termination notice issued pursuant to paragraph (a) above must specify the [Department Default] that has occurred and has entitled the [Developer] to issue the termination notice.*
- (c) *This [Concession Agreement] will terminate on the date falling [X] days after the date the [Department] receives the termination notice.*
- (d) *If this [Concession Agreement] is terminated for [Department Default] in accordance with paragraphs (a) - (c) above, the [Department] shall pay the [Department Default Termination Sum] to the [Developer] in accordance with [Section X] of this [Concession Agreement].*

Many Concession Agreements will limit the ability of the Developer to terminate for a Department Default to circumstances where the Department Default arises from an uncured failure of the Department to pay a material sum due to the Developer. In some cases, it may be appropriate to expand this limitation to include performance-related Department Defaults where such Department Defaults have a direct impact on the Project's ability to generate profits and thus negatively impact the Developer's return on equity (e.g., the Department initiates an unpermitted condemnation or other confiscation of the Project).

7.2.4 *Compensation on Termination for Department Default*

Basis of Calculation

In the event of an early termination caused by a Department Default, the broadly accepted principle is that the Department should pay the Developer sufficient compensation to ensure that the Developer is left in a no better or no worse economic position than it would have been had the early termination not occurred and the Concession Agreement has continued until the last day of its Term. In practical terms, this broadly means that there will be three components to the amount of compensation that will be paid to the Developer by the Department as a result of an early termination of the Concession Agreement for Department Default:

- i) The value of the invested and committed equity (whether in the form of capital contributions or Shareholder Loans) in the Developer at the time of the termination.
- ii) An amount sufficient to allow the Developer to repay all Project Debt, including amounts due as a result of the early termination of the Concession Agreement, such as breakage costs.
- iii) Reasonable costs and liabilities that the Developer incurs as a result of having to terminate Subcontracts as a direct result of the early termination of the Concession Agreement.

Valuing the Equity in the Developer

Determining the market value of the equity in the Developer in the event of an early termination of the Concession Agreement has been an issue encountered in most P3 transactions that have closed in the United States to date. The basic philosophy underlying the valuation methodology should be to ensure that the Equity Investors are put in the same financial position that they would have been in had it not been for the early termination. In other words, the Department should pay compensation that equates to the true market value of the equity in the Developer.

The sensitivity for both parties will generally be that any determination of the value of the equity in the Developer requires relatively subjective projections of future revenues and costs which, by definition, involves the projection of future traffic levels using the Project. To address this concern and the scope for dispute between the parties, the Concession Agreement will typically provide for the parties to either jointly appoint an independent expert who undertakes the evaluation, with such evaluation being final and binding on both parties, or submit evidence in the event of dispute for ultimate determination by a court or other dispute resolution forum. As an alternative, the Department and Developer could agree at the time of closing on a minimum base case traffic projection for the life of the Project, and value the equity according to such minimum base case rather than performing a projection based on then-current (and then-expected) conditions at the time of termination. This approach would eliminate the need for a forecast of future revenues, and would limit the compensation payable for equity in the event that traffic turned out to be higher than expected. Departments considering whether to adopt this alternative approach should consult with their legal and financial advisors based on the particular circumstances of a particular Project.

In the context of projects that anticipate a "ramp-up" period before traffic volumes reach steady state, the Developer may be concerned about how any independent expert would value the equity interest in the Developer in the event that an early termination for Department Default occurred during construction or

the ramp-up period. To address this concern, some Concession Agreements have adopted an alternative approach in the early years of the Project to determining the valuation of the equity in the Developer, with such valuation being based on the revenue and cost projections included in the Base Case Financial Model.

Calculating the Developer's Liabilities under its Financing Arrangements

To the extent the Termination Sum includes amounts that are calculated by reference to the amount of outstanding Project Debt, the Developer and the Lenders will seek to ensure that the provisions which calculate such amounts are sufficiently broad so as to accommodate all potential financing structures that the Developer may seek to use during the Term. The Department, by comparison, will need to ensure that amounts which are not genuine third party debt are not required to be paid and that the provisions do not permit legitimate amounts to be inflated or revised unexpectedly. Concession Agreements will generally include a defined term to encapsulate these amounts and related issues, the overall purpose of which is to properly describe only those debt obligations that the Department is willing to pay in the event of a termination of the Concession Agreement (whether in whole or in part, depending on the other provisions of the Concession Agreement).

When addressing the scope of obligations that may be included, Developers will seek to ensure that all potential debt financing solutions for the Project, including bank loans, bonds (including PABs), TIFIA loans, guarantee obligations, letter of credit obligations, and others, as well as related costs and expenses, such as interest, fees, hedging arrangements, and others are included. Departments should seek the advice of their legal and financial advisors when deciding whether to include or exclude particular items, as the market for financing opportunities is constantly changing. Departments should, however, be cautious wherever Developers seek to include any type of subordinated indebtedness within this definition because Developers may structure their equity investments as Shareholder Loans extended by Equity Investors to the Developer to take advantage of tax benefits associated with the payment of interest. Shareholder Loans of this type will be subordinated to the debts owed to third-party Lenders, so it will be important to distinguish these Shareholder Loans from other debt that third-party Lenders provide that may also be subordinate to the debt the Developer's senior Lenders provide. For example, TIFIA loans are generally included within the scope of Project Debt compensated on termination, even though they are subordinate in payment to other sources of debt in the ordinary course. The Department may (or may not) wish to provide protection to other bona fide subordinated third-party Lenders and should consult with their financial advisors regarding the costs and benefits of doing so in the context of each individual Project.

Subcontract Breakage Costs

The Developer may incur costs or liabilities (e.g., breakage costs in respect of cancellation of orders for materials and goods) as a direct result of the early termination of the Concession Agreement for Department Default. To the extent that the Developer will incur such costs, it would generally be included in the compensation payable by the Department on early termination. One point that Departments generally want to ensure in relation to the costs of breaking Subcontracts is that they are not required to pay any compensation with respect to future loss of profits or other consequential Losses.

An example definition of Subcontract Breakage Costs is set forth below.

Subcontract Breakage Costs means [Losses] that have been or will be reasonably and properly incurred by the [Developer] under a [Subcontract] as a direct result of the early termination of this [Concession Agreement] (and which shall not include lost profit or lost opportunity), but only to the extent that:

(a) *the [Losses] are incurred in connection with the [Project] and in respect of the works required to be provided or carried out, including:*

(i) *any materials or goods ordered or [Subcontracts] placed that cannot be cancelled*

- without such [Losses] being incurred;*
- (ii) any expenditure incurred in anticipation of the provision of services or the completion of works in the future; and*
 - (iii) the cost of demobilization including the cost of any relocation of equipment used in connection with the [Project];*
- (b) the [Losses] are incurred under arrangements and/or agreements that are consistent with terms that have been entered into in the ordinary course of business and on an arm's length basis; and*
- (c) the [Developer] and the relevant [Subcontractor] have each used their reasonable efforts to mitigate such [Losses].*

7.3 Termination for Developer Default

7.3.1 Events Giving Rise to Developer Default

The Concession Agreement will generally provide for a series of events or circumstances that constitute Developer Defaults. Broadly speaking, such events occur when the Developer fails to perform its obligations, or otherwise takes, or permits to be taken, some action that calls into question its fitness to continue performing under the agreement. A number of remedies are typically available to the Department following a Developer Default, such as stepping in and performing the Developer's obligations or drawing on any performance security which may have been provided by the Developer. The occurrence of a Developer Default will also generally permit the Department to terminate the Concession Agreement subject to additional procedures and conditions, though some Concession Agreements may permit the Department to terminate the Concession Agreement only in the case of a limited set of Developer Defaults which are designated as material.

The list of Developer Defaults contained in a Concession Agreement often range from a generic failure of the Developer to perform its material obligations under the Concession Agreement to more specific events, such as the bankruptcy of the Developer or violation of a State's anticorruption laws in connection with the award of the Concession Agreement. The precise set of Developer Defaults varies from Project to Project, but the goal is to clearly establish the Department's threshold for taking action relating to various acts or omissions of the Developer under the Concession Agreement without creating a risk of a "hair trigger" that could discourage investors or Lenders from investing in the Project. Because the consequences of a termination for Developer Default are so severe, including the loss of potentially substantial amounts of money invested by both Equity Investors and the Lenders, the list of Developer Defaults may be the subject of significant negotiation.

An example definition of Developer Default is set forth below.

- Developer Default*** means the occurrence of any one or more of the following events or conditions:
- (a) the [Developer] fails to comply with, perform or observe any material obligation, covenant, agreement, term or condition in this [Concession Agreement] or any other [Project Document], which failure materially adversely affects the [Department]'s rights or obligations hereunder;*
 - (b) any representation or warranty made by the [Developer] under this [Concession Agreement] is false or misleading in any material respect on the date made;*
 - (c) the [Developer] fails (i) to pay to the [Department] when due any undisputed sum payable to the [Department] pursuant to this [Concession Agreement], or (ii) to deposit funds to any reserve or account, in either case in the amount and within the time period required by this [Concession Agreement];*

- (d) *the [Developer] fails to commence the [Construction Work] within [X] days of the issuance of the notice to proceed;*
- (e) *the [Developer] fails to achieve [Substantial Completion] of all of the [Project] by the [Long Stop Date], as such date may be extended pursuant to this [Concession Agreement];*
- (f) *this [Concession Agreement] or all or any portion of the [Developer's Interest] is transferred, or there occurs a [Change in Ownership], in either case in contravention of this [Concession Agreement];*
- (g) *a voluntary or involuntary insolvency event, including the commencement by any third party of liquidation, dissolution, reorganization or similar proceedings, arises with respect to (i) the [Developer], (ii) any investor in the [Developer], or (iii) the [Developer]'s [Design-Build Contractor] (but only during the [Construction Period]) or [Operations and Maintenance Contractor], in each case unless such [Subcontractor] is replaced by the [Developer] with a reputable counterparty reasonably acceptable to the [Department];*
- (h) *the Developer abandons or otherwise ceases work on the [Project], or following a permitted suspension of the work ceases to resume the work, for more than [X] days, except as otherwise permitted under this [Concession Agreement];*
- (i) *the [Developer] fails to comply with any permits or applicable laws in any material respect;*
- (j) *the [Developer] fails to obtain, provide and maintain the insurance policies in accordance with the [Concession Agreement];*
- (k) *the [Developer] fails to comply with any written suspension of work order issued by the [Department];*
- (l) *the [Design-Build Contract] or the [Operations and Maintenance Contract] is terminated (other than non-default termination on its scheduled termination date) and the [Developer] has not entered into a replacement of such contract with a reputable counterparty reasonably acceptable to the [Department]; or*
- (m) *the [Developer], any investor in the [Developer], any [Key Contractor] whose work is not completed, or any affiliate of [Developer] for whom transfer of ownership would be permitted without the [Department]'s consent, or any of their respective officers, directors, employees or agents, is suspended or debarred, following exhaustion of all rights of appeal, or there goes into effect an agreement for voluntary exclusion, from bidding, proposing or contracting with any Federal or State department or agency.*

7.3.2 Cure Periods for Developer Default

Following the occurrence of a Developer Default and before the Department has the right to terminate the Concession Agreement, the Developer will generally have a period of time during which it may take corrective action to cure the Developer Default. If the Developer Default is corrected during the cure period, the Department will not be permitted to terminate the Concession Agreement (although the Developer may remain liable for Department losses attributable to the Developer Default).

The standard cure period for most Developer Defaults is often 30 days, running from the date on which the Department notifies the Developer in writing of the occurrence of the Developer Default. However, cure periods may vary depending on the nature of the Developer Default. For example, the cure period for a Developer Default consisting of the failure to pay money to the Department is often not more than 3–5 days because the only acceptable cure is actual payment, which under ordinary circumstances should be completed quickly. By comparison, the cure period for a Developer Default consisting of a general failure by the Developer to perform its material obligations may initially be 30 days, but if the circumstances giving rise to the Developer Default cannot be cured within the initial 30 days, but are nevertheless capable of

being cured and the Developer is actually taking steps to do so, then the cure period may be extended up to a maximum of as long as 120 or, in some cases, 180 days.

Certain Developer Defaults, such as a failure to comply with an order to suspend work issued by the Department, may not be capable of cure. For these Developer Defaults, the Concession Agreement will generally not include a cure period or may expressly state that no cure period is afforded to the Developer.

Although the exact cure periods are often the subject of negotiation and will vary from one Project to another, the Concession Agreement should strike a balance between giving the Developer a meaningful opportunity to correct a Developer Default, on the one hand, and on the other, not unduly delaying the right of the Department to terminate the Concession Agreement.

A Concession Agreement may be drafted in one of two ways with respect to the description of the cure periods. First, the cure periods may be included in the description of the Developer Default, in which case the Developer Default and its consequences do not arise until the expiration of the relevant cure period.

An example provision drafted in this style is set forth below.

The [Developer] fails to comply with, perform, or observe any material obligation, covenant, agreement, term or condition in this [Concession Agreement] and such failure continues without cure for a period of [X] days following the date the [Department] delivers written notice thereof to the [Developer], or for such longer period as may be reasonably necessary to cure such failure up to a maximum cure period of [X] days; provided, however, that in the latter case, (i) the [Developer] is proceeding with all due diligence to cure or cause to be cured such failure, (ii) such failure is capable of being cured within a reasonable period of time, and (iii) such failure is in fact cured within such period of time.

Second, the cure periods may be described in a separate provision of the Concession Agreement, such that the Developer Default arises immediately but the consequences are delayed until after the expiration of the relevant cure period.

An example provision drafted in this style is set forth below.

The [Department] shall provide written notice to the [Developer] of the occurrence of a [Developer Default]. Upon receipt of the [Department]'s notice, the [Developer] shall have the following cure periods:

- (a) for a [Developer Default] under [Section [X] of this [Concession Agreement], a period of [X] days after the [Developer] receives written notice from the [Department] of such [Developer Default];*
- (b) for a [Developer Default] under [Section [X] of this [Concession Agreement]], a period of [45] days after the [Developer] receives written notice from the [Department] of such [Developer Default]; provided, however, that if such [Developer Default] cannot be cured within such time period, despite the [Developer]'s commencement of meaningful steps to cure immediately after receiving the default notice, the [Developer] shall have such additional period of time, up to a maximum cure period of [X] days, as is reasonably necessary to diligently effect cure; and*
- (c) for any other [Developer Default] not referred to in paragraphs (a) or (b), there is no cure period.*

Either approach is generally accepted, although in cases where the cure periods are drafted into the description of the Developer Defaults, the Concession Agreement should not also contain a provision that grants the Developer an additional cure period following receipt of a notice of default, and vice versa.

7.3.3 Department's Right to Terminate for Developer Default and Procedure

The Department is generally permitted to terminate the Concession Agreement following the occurrence of a Developer Default and the expiration of any cure period associated with it. However, the Department's right to terminate the Concession Agreement is subject to the right of the Collateral Agent (acting on the instructions of designated senior Lenders, the composition of which may differ depending on the nature of the Project) to an additional cure period after the expiration of the Developer's cure period, during which time they will be permitted to cure any Developer Default on behalf of the Developer. The right of the Collateral Agent to cure a Developer Default will generally be set forth in a stand-alone Direct Agreement among the Collateral Agent, the Developer and the Department. If the Developer Default is cured before the Department exercises the right to terminate the Concession Agreement, then the termination right will cease.

If the Department chooses to terminate the Concession Agreement, it will be required to deliver written notice of its decision to the Developer. The Concession Agreement may terminate immediately upon the Department's delivery of a termination notice to the Developer, or it may terminate automatically after the passage of a short period of time after delivery of the termination notice (generally not more than 60 days thereafter).

An example provision describing the Department's right to terminate the Concession Agreement is set forth below.

- (a) *Upon the occurrence of a [Developer Default] that has not been cured within the relevant cure period, the [Department] may, subject to the rights of the [Collateral Agent] under the [Direct Agreement], terminate this [Concession Agreement] by issuing a written notice of termination to the [Developer] specifying the [Developer Default] giving rise to the right of the [Department] to terminate this [Concession Agreement].*
- (b) *This [Concession Agreement] will terminate [immediately] [on the date specified in the termination notice referred to in paragraph (a) above, which must be a minimum of [X] days after the date of receipt of the notice by the [Developer]].*
- (c) *If this [Concession Agreement] is terminated for [Developer Default] in accordance with paragraph (a) and (b) above, the [Department] shall pay the [Developer Default Termination Sum] to the [Developer] in accordance with [Section[X]] of this [Concession Agreement].*

7.3.4 Compensation on Termination for Developer Default

Following a termination of the Concession Agreement for a Developer Default, the Department will still generally be required to pay compensation to the Developer. Departments may find this unusual given that the termination will likely be caused by the act or omission of the Developer, whereas in many service contracts entered into by Departments, it is often the case that the contractor, not the Department, makes a payment on termination. In the context of a greenfield project, however, compensation is paid because upon termination the Department will receive an asset of potentially considerable value that it did not have before the Concession Agreement was entered into, and if compensation is not paid, then the Department will be unjustly enriched as a result. This principle is often considered alongside the need to impose a financial consequence on Developers (and their Lenders) to discourage them from walking away when the possibility of termination arises, while not imposing such drastic consequences that the risks are too high to justify investment in the Project. The amount of termination compensation payable will generally be adjusted to reflect other pools of cash available to the parties, such as Account Balances held by the Developer and Insurance Proceeds received by the Developer (or that would have been received had the Developer entered into the required insurance policies).

The amount of termination compensation payable following a Developer Default will depend on whether the construction of the Project is completed at the time of termination. If the construction of the Project is not complete, then the termination compensation will generally be calculated by reference to the value of the Work performed to date (taking into account the anticipated cost to the Department of completing the remaining Work) or the amount owed to the Developer's Lenders. This calculation provides the Developer's Lenders with some comfort that they will receive compensation in the event of a termination, but also provides the Department with the opportunity to ensure that it does not pay any more than is necessary to receive the Project it originally contracted for.

An example provision describing the calculation of termination compensation payable prior to completion of the Project is set forth below.

On termination of the [Concession Agreement] following a [Developer Default] prior to the [Substantial Completion Date], the [Department] shall pay to the [Developer] an amount equal to the lower of:

- (a) the [Work Value], being equal to:*
 - (i) the stated value of the [Design-Build Contract] for the [Project], less*
 - (ii) the [Cost to Complete], being equal to (A) those costs (internal and external) that the [Department] reasonably and properly projects that it will incur in carrying out any process to request tenders from any parties interested in entering into a contract with the [Department] to achieve [Substantial Completion], including all costs related to the preparation of tender documentation, evaluation of tenders and negotiation and execution of relevant contracts; plus (B) the costs that the [Department] reasonably and properly projects that it will incur in achieving [Substantial Completion]; plus (C) any other [Losses] that the [Department] would, but for the termination of this [Concession Agreement], not have incurred prior to [Substantial Completion]; minus (D) any insurance proceeds available to the [Department] for the purposes of achieving [Substantial Completion] (Insurance Proceeds); and*
- (b) the [Net Project Debt], being equal to:*
 - (i) the [Project Debt], minus*
 - (ii) all amounts standing to the credit of any bank account held by or on behalf of [Developer] (excluding the [Handback Reserve Account]), or the value of any letter of credit issued in substitution for any bank account previously held by [Developer] (excluding the [Handback Reserve Account]), at the [Early Termination Date] (Account Balances); minus [Insurance Proceeds].*

If the construction of the Project is complete, then the termination compensation will generally be calculated by reference to the amount owed to the Developer's Lenders. During this period, the Department will generally be concerned about the cost to correct any outstanding maintenance issues rather than the Cost to Complete the Project. In addition, the Department will generally look to impose some financial consequences on the Developer's Lenders and its Equity Investors, because they have chosen not to cure the outstanding Developer Default that leads to termination.

An example provision describing the calculation of termination compensation payable after completion of the Project is set forth below.

On termination of the [Concession Agreement] following a [Developer Default] on or after the [Substantial Completion Date], the [Department] shall pay to the [Developer] the amount calculated at the date of such termination (without double-counting) as follows:

- (a) [Project Debt] [[X%] of Project Debt]; minus*

- (b) *[Insurance Proceeds]; minus*
- (c) *[Account Balances]; minus*
- (d) *all [Losses][that the [Department] determines it is reasonably likely to incur as a direct result of the termination of this [Concession Agreement], including the following:*
 - (i) *those costs (internal and external) that the [Department] is reasonably likely to incur as a direct result of carrying out any process to request tenders from any parties interested in entering into a contract with the [Department] to carry out [Maintenance Work], including all costs related to the preparation of tender documentation, evaluation of tenders and negotiation and execution of relevant contracts; and*
 - (ii) *those costs reasonably projected to be incurred by the [Department] in relation to: (A) remediation or, if remediation is not possible or would cost more than renewal, renewal of any defective [Work]; (B) rectification or cure of any breach of this [Concession Agreement] by the [Developer]; and (C) carrying out of all other matters necessary in order to ensure that within a reasonable period after the [Early Termination Date], the [Project] complies with the requirements of the [Project Documents] and has a reasonable prospect of continuing to perform to the same standard and cost that it would have continued to perform at had this [Concession Agreement] not been terminated and the [Project] been in compliance with all of the requirements of the [Project Documents]; minus*
- (e) *any amount of unfunded equity that has been committed to the [Developer] and is shown to be available for use in the [Base Case Financial Model] prior to the [Substantial Completion Date], but only to the extent that the commitment to provide such amount is supported by an irrevocable on-demand letter of credit issued by or for the account of an [Equity Investors] naming the [Developer] and/or the [Collateral Agent] as beneficiary and guaranteeing the provision of the committed amount by a date that is not later than the [Substantial Completion Date]; plus*
- (f) *the balance standing to the credit of the [Handback Reserve Account] on the [Early Termination Date].*

7.4 Termination for Extended Force Majeure Events

7.4.1 Rights of Either Party in the Event of Extended Force Majeure Events and Procedure

As described in Chapter 4 (Supervening Events), the Concession Agreement generally defines the Force Majeure Events that can lead to termination and provides for the rights of the parties if this occurs. If a Force Majeure Event occurs and the parties cannot agree on a solution within a specified period of time, either party is generally entitled to terminate the Concession Agreement with compensation payable to the Developer as summarized in Section 7.4.2 below. However, it should be noted that in the event that the Developer elects to terminate the Concession Agreement due to the continuance of an extended Force Majeure Event, the Concession Agreement will often give the Department the right to prevent termination by allowing the Department to pay the Developer compensation as if the Project was continuing to perform at the same level as it was prior to the occurrence of the relevant Force Majeure Event. As discussed in Section 4.3.5 above, the Department may also expand this termination right to include any Compensation Event or Delay Event for which a solution is not agreed within a specified period of time, rather than just Force Majeure Events. For the sake of clarity, the following discussion refers only to Force Majeure Events, but would apply, subject to the considerations discussed in Section 4.3.5, to the extent the termination right is extended to these additional events.

7.4.2 Compensation on Termination for Extended Force Majeure Events

To the extent that the Concession Agreement is terminated due to the continuance of an extended Force Majeure Event, the Department will generally pay compensation to the Developer on the basis that the financial consequences of the early termination of the Concession Agreement should to some extent be shared. The justification for this approach is that the early termination is not the fault of either party.

In determining the extent to which the financial consequences of the early termination should be shared between the parties, a common approach is generally taken across all jurisdictions, which can be summarized as follows:

- ▶ Lenders do not take on the risk of Force Majeure Events and, accordingly, are compensated for all amounts owed to them by the Developer as a direct result of the early termination of the Concession Agreement.
- ▶ The Developer will generally be compensated for any Subcontractor Breakage Costs (see Section 7.2.4.4).
- ▶ The Equity Investors will generally be compensated an amount equal to the amount of any unrecovered equity invested in the Developer (i.e., capital contributions and Shareholder Loans).

In other words, the extent of the sharing of the financial consequences of early termination relates to the Developer indirectly foregoing all equity return that it has previously received prior to the early termination, together with any future equity return that it would have received had the Concession Agreement continued through to the last day of its Term.

Although the Department may be required to fund a material amount of compensation in the event of an early termination of the Concession Agreement due to an extended Force Majeure Event, it should be noted that the early termination may result in the Project effectively being acquired from the Developer by the Department at an undervalue. Additionally, the scope of the definition of Force Majeure Event is generally drafted very narrowly and with reference to extreme events, thereby reducing the likelihood of the Concession Agreement being terminated early due to the extended continuance of a Force Majeure Event.

An example provision calculating the Termination Sum due in the event of an extended Force Majeure Event is set forth below.

If the [Concession Agreement] is terminated following an extended [Force Majeure Event], the [Department] will pay to the [Developer] the [Force Majeure Termination Sum].

Force Majeure Termination Sum means the aggregate of (i) the [Project Debt], [(ii) all amounts at par paid by the [Equity Investors] in the form of capital contributions or [Shareholder Loans] up until the termination date, less any amounts actually received by the [Equity Investors] from the [Developer] as distributions or payment of principal and interest for such [Shareholder Loans], and (iii) all [Subcontractor Breakage Costs]; (iv) less [Account Balances]; and (v) less [Insurance Proceeds].

7.5 Termination for Convenience by Department

7.5.1 Termination for Convenience and Procedure

The intention of the parties to any Concession Agreement should be that it will run its full course. Concession Agreements are, however, long-term agreements and circumstances may arise that cause the Department to no longer be able to continue the relationship it has with the Developer under the Concession Agreement. For example, the Department may wish to grant a concession with respect to the facilities that are the subject of the Concession Agreement as part of a broader concession arrangement,

perhaps as a result of a policy decision on the part of the Department to place operations and maintenance of all Projects in a region (including those that are the subject of the Concession Agreement) under common management. Additionally, notwithstanding the ability of many Departments (particularly those that are beneficiaries of P3-enabling legislation in their relevant jurisdiction) to enter into long-term Concession Agreements, most jurisdictions require (as a matter of public and administrative law) that the relevant government’s ability to exercise its statutory powers should not be fettered by the terms of contracts that it enters into. Accordingly, it is generally considered a matter of best practice and common for Concession Agreements to include provisions that allow the Department to terminate the Concession Agreement at its convenience, whereupon compensation generally becomes payable by the Department to the Developer (see Section 7.5.2 below).

An example provision permitting the Department to terminate the Concession Agreement for convenience is set forth below.

- (a) *The [Department] may terminate this [Concession Agreement] at any time by issuing a termination notice to the [Developer] stating that:*
 - (i) *the [Department] is exercising its right to terminate this [Concession Agreement] in accordance with its terms; and*
 - (ii) *this [Concession Agreement] will terminate on the date specified in such termination notice, such date to be a minimum of [X] days after the date of receipt of the notice by the [Developer].*
- (b) *This [Concession Agreement] will terminate on the date specified in the termination notice referred to in (a) above.*
- (c) *If this [Concession Agreement] is terminated for convenience in accordance with paragraphs (a) and (b) above, the [Department] shall pay the [Termination for Convenience Termination Sum] to the [Developer] in accordance with [Section [X]] of this [Concession Agreement]].*

7.5.2 Compensation on Termination for Convenience

The Termination for Convenience Termination Sum is generally an amount equal to the Department Default Termination Sum (see Section 7.2.0 above). Choosing different approaches to how early termination compensation should be calculated for these two types of termination scenario could lead to the Department being incentivized to default in certain circumstances or, in the anticipation of a forthcoming Department Default, terminate the Concession Agreement for convenience, which is why it is common that the methods used for both Termination for Convenience and Termination for Department Default are the same.

7.6 Other Issues Related to Calculation of Compensation for Early Termination

7.6.1 Increased Termination Liabilities Arising from Changes to Financing Documents

To the extent that the amount of compensation payable by the Department to the Developer on an early termination is calculated in whole or in part by reference to the level of Project Debt that the Developer has outstanding at the time of the termination payment, the Department may be concerned to ensure that the level of Project Debt outstanding at any time is not inflated in a way that will significantly and unexpectedly increase the Department’s liabilities on termination beyond the levels that could otherwise have been anticipated at the time the Concession Agreement was entered into. Examples of how such circumstances could arise include the borrowing of additional debt by the Developer during the Term or a rescheduling of the Developer’s debt during the Term.

The approaches taken to this issue in Concession Agreements in the United States are relatively binary. Either any additional liabilities that arise as a result of the Developer refinancing or rescheduling its debt

during the Term are automatically taken into account when calculating compensation on early termination or they are not. A specific provision is generally only included in the Concession Agreement with respect to this issue to the extent that the Department wishes to exclude any such additional liabilities from the compensation calculation that it has not consented to.

An example provision addressing such concern is set forth below.

No amendment, waiver or exercise of a right under any [Financing Document] shall have the effect of increasing the amount of the [Department]'s liabilities on early termination of this [Concession Agreement], unless the [Developer] has obtained the prior written consent of the [Department] to such increased liability for the purposes of this provision.

Another approach is to specifically exclude such additional amounts from the definition of Project Debt in the Concession Agreement.

To the extent that the Developer takes the risk of a future refinancing in the context of its financial plan for the Project, the Developer is likely to require some level of comfort in the Concession Agreement that any such future refinancing will be covered by the compensation on termination provisions in the Concession Agreement.

7.6.2 Rights of Set-off on Early Termination

The Department is generally entitled to exercise a right of set-off in respect of any outstanding liabilities of the Developer against the amounts it pays in compensation on an early termination of the Concession Agreement.

Notwithstanding the above principle, the Lenders (particularly non-governmental affiliated Lenders) will generally be concerned to ensure that the Department's ability to set-off such liabilities cannot result in the amount of compensation payable on early termination being less than the amount of the Project Debt. This principle is often reflected in Concession Agreements, except in the case of a termination for Developer Default, where the Lenders have the opportunity to avoid the termination by exercising their rights to cure the Developer Default.

An example provision allowing the Department to exercise such right of set-off is set forth below.

The [Department] is not entitled to set-off any amount against the [Department Default Termination Sum], the [Termination for Convenience Termination Sum], or the [Force Majeure Termination Sum] if the effect of exercising such right of set-off would be to reduce the amount payable to the [Developer] to an amount that is less than the amount of the [Project Debt].

7.6.3 Timing of Payment

In the event of an early termination of the Concession Agreement, the Developer (and its Lenders) will be concerned to ensure that within a reasonable period of the amount of the Termination Sum being calculated, the Department will be required to make payment of such Compensation Amount to the Developer.

One issue relating to timing of payment where there is significant divergence in approach in Concession Agreements relates to the period of time that the Department should have to make payment of the Termination Sum. In particular, this issue is frequently of concern to any Department that believes that an appropriation would need to be made at the relevant State level to fund the relevant payment. Experience has shown that, within reason, Developers and Lenders are willing to agree to the Department having a material period of time to pay the Termination Sum, particularly where an appropriation is required.

However, the acceptability of this issue to Developers and Lenders is generally a function of the extent to which (in terms of both time period and interest rate) the Department is willing to pay interest on the Termination Sum between the date that the amount is finally calculated and the date that it is paid to the Developer.

7.6.4 Treatment of Assets on Early Termination

On the early termination of the Concession Agreement, any proprietary interest that the Developer may have in the Project (e.g., a leasehold interest) will automatically terminate (on the basis that the Developer's right to operate the relevant Project and charge tolls to users of that Project has come to an end) as the Department will need to be immediately able to continue to operate the Project and provide continuity of service to the users of the Project. However, the reversion of the Project to the Department may not be sufficient to allow its continued and efficient operation by the Department. By way of example, the Department may not be able to effectively operate the Project without the right to access intellectual property associated with toll collection equipment.

To address the above concerns, the Concession Agreement will generally include a provision that requires the Developer to transfer to the Department (as a condition precedent to the payment of the early termination compensation by the Department) certain Key Assets to the Department, such assets intended to be those that the Department needs access to provide continued and seamless operation of the facilities to its users.

An example provision providing for a transfer of assets is set forth below.

As a condition precedent to the payment of any [Termination Sum], the [Department] may require [Developer] to transfer its rights, title and interest in and to the [Key Assets] to the [Department].

Key Assets means all assets and rights to enable the [Department] or a successor contractor to own, operate and maintain the [Project] in accordance with this [Concession Agreement], including the following:

- (a) any land or buildings;
- (b) any equipment;
- (c) any books, records, drawings, surveys, designs and other design documentation (including operating and maintenance manuals, health and safety manuals and other know how);
- (d) any borings, samples, spare parts, tools and other assets (together with any warranties in respect of assets being transferred);
- (e) any policies of insurance including rights to outstanding claims;
- (f) any contractual rights, including rights under the [Design-Build Contract] or [Operations and Maintenance Contract] or any other design-build agreement or operations and maintenance agreement then in effect; and
- (g) any intellectual property.

7.6.5 Compensation on Termination as an Exclusive Remedy

During the negotiation of the Concession Agreement, significant time is generally spent by both parties assessing the adequacy of the compensation provisions related to early termination of the Concession Agreement. Accordingly, both parties generally expect that on an early termination, their respective liabilities to each other in connection with the early termination will be limited to the following:

- a) In the case of the Department, the Termination Sum payable to the Developer.

- b) In the case of the Developer, the extent of any deductions that are made in the calculation of the Termination Sum.

Accordingly, it is common for both parties to agree that early termination compensation payments represent their exclusive and only remedy against each other with respect to the recovery of Losses incurred as a result of the early termination. As a consequence of this, the Developer and its Lenders (particularly non-governmental affiliated Lenders) will conduct significant due diligence over the scope of the compensation on early termination provisions, so as to ensure that they adequately compensate the Developer for the costs and Losses that it incurs in the context of the relevant termination scenario.

The aforementioned concept of exclusivity of remedy for recovery of Losses that arise in the context of termination should not be confused with each party's ongoing right to pursue the other party for Losses associated with breaches of the Concession Agreement that arose prior to the Early Termination Date. Such rights of claim would generally fall outside of any exclusive remedy arrangements relating to compensation on early termination of the Concession Agreement.

An example exclusive remedy provision is set forth below.

Any [Termination Sum] irrevocably paid by the [Department] to the [Developer] shall be in full and final settlement of each party's rights and claims against the other for breaches and/or termination of this [Concession Agreement] whether under contract, tort, restitution or otherwise, but without prejudice to:

(a) *any antecedent liability of either party to the other that arose prior to the [Early Termination Date] (but not from the termination itself) to the extent such liability has not already been taken into account in the calculation of the [Termination Sum]; and*

(b) *any liabilities arising in respect of any breach by either party after the [Early Termination Date] of any obligation under this [Concession Agreement] that survives the [Early Termination Date], to the extent not taken into account in the calculation of any [Termination Sum].*

8 Handback

8.1 Introduction

The Term of a toll road concession generally ranges from 30 to 50 years, although Projects have run as long as 99 years, and the Term will ultimately depend on the nature of the Project, the authorizing legislation and the needs (and relative bargaining power) of the parties. On termination or expiration of the Term, the Project will generally pass back to the Department. Because the Department will be responsible for operating and maintaining the Project after the end of the Term, it will have a strong interest in ensuring that all of the Project assets it receives are not in a condition that will require immediate and costly life-cycle maintenance. The Developer, by comparison, will naturally seek to minimize its costs and may be unlikely to voluntarily make long-term investments in the Project during the final years of the Term (as it will not receive much of the benefit of those investments). Although the ongoing performance specifications contained in the Concession Agreement would require the Developer to comply with such items as ride quality and cracking of the roadway, there is nevertheless a risk that the Developer could defer necessary renewals and instead choose to incur additional routine maintenance costs, together with the possibility of incurring noncompliance deductions for failure to meet performance requirements. For this reason, special provision should be made in the Concession Agreement to ensure that the Developer does not hand back a Project to the Department requiring extensive major maintenance.

The Concession Agreement should therefore include provisions for dealing with what will happen to the Project (and particular assets) at the end of the Term, including the rights and obligations of the Department and the Developer with respect to the long-term condition of the Project on handback, including any Required Residual Life of the Project assets. These provisions are important to avoid disputes at the end of the Term and also to further incentivize the Developer to make life-cycle investments in the Project at the appropriate time. The extent of the obligations the Department places on the Developer with respect to the handback condition of the Project may be reflected in the pricing of the Developer's bid for the Project and may have an impact on the design, construction, or maintenance strategies considered during the procurement process.

8.2 Handback Requirements

8.2.1 *Defining Handback Requirements*

The Developer will generally be required to transfer the Project back to the Department in accordance with prescribed Handback Requirements. From the Department's perspective, Handback Requirements are particularly important as they play an important role in incentivizing the Developer to renew and replace Elements of the Project at the optimum time (from a life-cycle perspective), rather than performing the minimum maintenance required and, as described above, possibly accepting some payment deductions for breach of its performance requirements. The Developer will seek to economize its long-term life-cycle costs in light of the performance specifications required under the Concession Agreement, so a well-defined set of Handback Requirements will likely impact the Developer's approach to operations and maintenance at all stages of the Project life-cycle. In particular, the Department should give careful consideration to complex assets, such as bridges, tunnels and other major structures, because properly crafted Handback Requirements can encourage the Developer to invest in these assets early and avoid the need for the Department to undertake expensive replacement efforts after the end of the Project.

Handback Requirements are generally contained in a schedule to the Concession Agreement within the technical specifications for the Project and should include the Developer's obligations, including valuation

methodologies and inspection requirements, in relation to maintenance and condition of each Element of the Project during what is known as the Handback Period, generally commencing 5 years prior to the end of the Term.

The Handback Requirements should draw a distinction between long-life Elements and those Elements that naturally wear out during the Term. Although not every Element of the Project needs to be in “as-new” condition at the time of handback, the Developer will generally be required to demonstrate a specified Residual Life for each major long-life Element, such as structural foundations, and if these Elements are not performing as expected, the Developer must repair them before the end of the Term. For Elements that generally wear out more quickly (and will likely have been replaced at least once during the Term) such as road signs, the Developer is generally not required to renew each such Element immediately before handback (provided the Element remains serviceable) but instead may be asked to pay an amount to the Department that will depend upon the condition, Useful Life, and age of each such Element. For these short-life Elements, a formula-based approach to determining the amount payable to the Department will generally be adopted. In addition, the operation and maintenance requirements in the Concession Agreement may require that short-life and medium-life Elements have a minimum Useful Life at the time of replacement or renewal to prevent the Developer from taking a sub-par approach to renewals during the final years of the Term.

8.2.2 *Residual Life*

The primary component of the Handback Requirements will generally stipulate the condition each Element of the Project must be in at the end of the Term. The condition of the Project and each of its Elements is generally evaluated by reference to the Residual Life of the asset at the end of the Term, being the period remaining until the relevant Element of the Project requires reconstruction, rehabilitation, restoration, renewal, or replacement.

The Handback Requirements will generally prescribe the following matters:

- ▶ How to calculate the Residual Life of each Element of the Project at each year during the Handback Period and at the end of the Term. This calculation will generally include an agreement to put in place a Residual Life Methodology toward the end of the Term, generally commensurate with the length of the Handback Period, containing the criteria to be adopted for the calculation of the Residual Life of each Element. The Residual Life Methodology should be described in general terms and should not place undue reliance on current technologies for the testing of Elements. A specific Residual Life Methodology is not generally put in place at the beginning of the Term because the methods and techniques for establishing Residual Life will have progressed by the time the Handback Inspections are performed.
- ▶ The Required Residual Life for each Element of the Project.
- ▶ How to calculate the cost of completing repairs and renewals on each Element to ensure that it will meet the Required Residual Life.
- ▶ How to calculate the handback amount payable to the Department at the end of the Term in respect of any relevant short-life Elements.

The following complexities may arise when setting the Required Residual Life of an Element and determining the corresponding Renewal Work required to achieve the Handback Requirements:

- ▶ Certain assets are difficult to handle at handback if their Useful Life is approximately the same as the Term. This may apply, for example, to bridge decks constructed with conventional reinforcing steel and subject to a regular deicing program, for which a Useful Life of around 50 years (which may coincide

with the length of the Term) appears to be in line with expectation. Specialist advice will often be needed on how best to treat these Elements. It is generally not good practice to specify in the Concession Agreement that Renewal Work such as major bridge deck renewals are to be performed just before handback because (a) the renewal may not in fact be needed at that time and (b) the Developer’s incentive to perform the Renewal Work to the appropriate level of quality at that time will be diminished.

- ▶ Where a Concession Agreement includes significant parts of existing assets within the Developer’s operation and maintenance obligations, such as an “online” widening of an existing roadway where the expectation is that the existing road pavement foundation or existing bridges are to be retained, this adds complexity to the Handback Requirements. For example, it may not be practical or economical to specify a Required Residual Life that exceeds the Residual Life of the existing road pavement. Often in these situations, the Handback Requirements are based on a detailed assessment of the condition of the existing road pavement and the Handback Requirements may be less stringent than those applicable to a “new build” Project.

8.2.3 Additional Handback Requirements

In addition to specific provisions regarding the Residual Life of each Element and a handback amount for short-life Elements, the Handback Requirements will generally require the Developer to prepare a handback plan that will be used to determine the condition and performance of the Project and identify the testing, evaluation, and calculation methods that are to be used to demonstrate to the Department that all equipment and systems function as intended and meet all applicable code and standards of the technical specifications.

The Developer may also be required to put together a Life-Cycle Maintenance Plan that outlines the estimated life of the Project, major maintenance to be undertaken in respect of the Project, pavement deterioration assessments, and how the Developer will meet its performance and Handback Requirements. This plan will be updated annually to take into account developments in each of these areas and reflect updated technologies for, among other things, measuring Residual Life (including potentially the adoption of technologies that are not well-developed at the beginning of the Term). For example, where a Residual Life of 50 years may be specified for concrete and steel Elements, current technologies may not be able to predict the incipient onset of major deterioration and corrosion beyond 10 years. Such a case reinforces the need for the Department to require the Developer to produce a Life-Cycle Maintenance Plan for all Elements and to monitor and report their condition and performance in service throughout the Term.

During the Handback Period, the Developer will generally be required to prepare enhanced annual updates to the Life-Cycle Maintenance Plan that, in addition to the matters described above, will also include the Developer’s calculation of Residual Life for each Element (using the Residual Life Methodology and taking into account the results of inspections during the Handback Period).

The Handback Requirements will also generally outline the Handback Inspections requirements (see Section 8.3 below).

An example handback requirements provision is set forth below.

- (a) *Upon the end of the [Term], the [Developer] will hand back the [Project] to the [Department], at no charge to the [Department], in the condition and meeting all of the [Handback Requirements].*
- (b) *The [Developer] will diligently perform and complete all [Renewal Work] required to be performed and completed prior to transfer of the [Project] to the [Department], based on the required adjustments and changes to the [Life-Cycle Maintenance Plan] resulting from the*

inspections and analysis under the [Handback Requirements].

8.3 Handback Inspections

During the Handback Period, the Developer will generally be required to perform Handback Inspections to determine the condition and Residual Life of each Element of the Project. These inspections may be required to take place annually or in other increments during the Handback Period, and should also take place at the expiration of the Term. The results of such inspections should be used by the Developer and the Department to determine (a) the Residual Life of the long-life Elements, (b) the condition, Useful Life and age of the short-life Elements and (c) the dollar amount of funds to be maintained in the Handback Reserve Account covering the cost of completing maintenance, repairs, and remediation of long-life Elements, as well as any cash payments for the short-life Elements, to ensure that the Project is transferred back to the Department at the end of the Term with the specified Required Residual Life.

The requirements of conducting Handback Inspections are generally detailed in the Handback Requirements in the technical specifications schedule of the Concession Agreement. The approach to the level of detail within the Concession Agreement is varied, with some projects incorporating a detailed outline of the inspection requirements of each Element of the Project and others including a more general requirement for inspections to be conducted with appropriate coverage such that the results are representative of the Project. Generally, the inspections will be conducted by an independent testing agency, and the Department will have the right to be present during the inspections.

An example Handback Inspections provision is set forth below.

Beginning five years prior to the projected expiration of the [Term] and every year thereafter, the [Developer] will conduct annual inspections of the [Project] and provide reports of such inspections to the [Department] pursuant to the [Handback Requirements].

8.4 Handback Reserve Accounts and Letters of Credit

8.4.1 Handback Reserve Account

The Concession Agreement will generally include a provision requiring the Developer to establish and fund a Handback Reserve Account at the beginning of the Handback Period. This reserve account is generally required by the Department as security for the obligation of the Developer to transfer the Project back to the Department in the agreed condition, with each Element having the Required Residual Life.

The Handback Reserve Account should remain funded with the Handback Reserve Amount which generally equals the amount necessary to ensure the Project meets the Handback Requirements at the end of the Term, although it may also include a contingency buffer of 10 percent of such amount. The Concession Agreement will generally either allow the parties to determine the estimated Handback Reserve Amount or will require an independent consultant to determine the amount that it reasonably determines is equal to an amount sufficient to cover all costs necessary to cause the Project to meet the Handback Requirements. In each case, this amount is based on the then-current Residual Life of the Project, the Required Residual Life of each Element of the Project, the Handback Inspections, and other technical parameters outlined in the Handback Requirements. The Handback Reserve Amount will generally be calculated yearly, and the funds in the Handback Reserve Account would be adjusted accordingly if necessary.

The Developer will often have an incentive to underestimate the likely cost of Renewal Work when calculating amounts to be transferred to the Handback Reserve Account. By comparison, the Department will have an incentive to increase the calculation of the Handback Reserve Amount. If Renewal Work is to

be performed by the Department after handback using the proceeds of the Handback Reserve Account, the Department's costs may be higher because of procurement costs and the risk that the Developer may not have adequately priced the Handback Reserve Account. To the extent possible, the pricing of the required Renewal Work should take into consideration what the Department's future commitments may be if required to perform the Renewal Work rather than simply what the Developer estimates.

The Handback Reserve Account will generally be in the name of and controlled by a third-party Escrow Agent or otherwise held by the Developer for the sole benefit of the Department, which allows the Department to control the withdrawals the Developer makes from the account. While the Concession Agreement will generally set out the conditions for the account, an account control (or similar) agreement may also be entered into by the parties shortly following establishment of the account.

The Developer will generally only be able to make withdrawals from the Handback Reserve Account to fund the cost of Renewal Work to ensure the Residual Life of the Project at the end of the Term is equal to the Required Residual Life, though in some cases the Department may permit withdrawals to fund work necessary to meet the Developer's safety compliance obligations. The Department can get comfortable with these types of withdrawals as generally the amount of the withdrawal to pay for repairs or renewal costs would equally reduce the amount the Department would need to cover the costs of such Renewal Work in the event the Developer does not transfer the Project to the Department in the agreed condition. However, even for such withdrawals, the Developer would generally still have to give notice to the Department, along with information surrounding the amount of the withdrawal and associated works, and the Department would have to provide consent prior to the withdrawal being made.

If, at the end of the Term, any Element of the Project does not meet the Handback Requirements or if the Handback Inspection demonstrates that the Residual Life of one or more long-life Elements does not equal or exceed the Required Residual Life, then the Concession Agreement should permit the Department to use the funds in the Handback Reserve Account to pay for the necessary Renewal Work to the extent necessary to meet the Handback Requirements. In addition, the Department will generally retain from the Handback Reserve Account an amount based on a formula for short-life Elements, if applicable. Any residual amounts left in the account following the payment of such costs will generally be paid to the Developer. If the Developer meets all of the Handback Requirements at the end of the Term and no further repairs or Renewal Work are required in respect of the Project, the amounts in the Handback Reserve Account will be paid to the Developer.

8.4.2 Letters of Credit

The Concession Agreement will generally allow the Developer to substitute some or all the Handback Reserve Amount with a letter of credit issued in favor of the Department. This substitution may be preferred by a Developer that wants to free up cash flow during the Handback Period, as the Handback Reserve Amount may be significant and would be locked up in the Handback Reserve Account for 5 or more years.

An example Handback Reserve Account provision, including provisions for substitution of letters of credit, is set forth below. The following example contemplates the use of an independent consultant to determine the appropriate amount, although as noted above the Department and the Developer may agree on the amount without a third party's input.

(a) *No later than the first day of the year that is seven years prior to the expiration of the [Term], and no later than the first day of each subsequent year, the [Department] and the [Developer] will cause an independent consultant to set forth an amount that it reasonably determines is equal to an amount sufficient to cover all costs necessary to cause the [Elements] to meet the [Handback Requirements] at the end of the [Term]. The amount determined in the preceding sentence is the*

Handback Reserve Amount.

- (b) Five years prior to the expiration of the [Term], the [Developer] shall establish the [Handback Reserve Account] for the sole and exclusive benefit of the [Department] to be held and controlled by a third party (the **Escrow Agent**) to be agreed between the parties.
- (c) Concurrently with the establishment of the [Handback Reserve Account], the [Developer] will deposit therein cash, a [Handback Performance Security] or a combination of the two in an aggregate amount equal to at least 100% of all costs necessary to cause the [Elements] to meet the [Handback Requirements] at the end of the [Term] as reasonably determined by the independent consultant pursuant to paragraph (a) above. Within [X] days of the date of each annual determination of the [Handback Reserve Amount], the [Developer] will cause the amount on deposit in the [Handback Reserve Account] to be equal to at least 100% of the [Handback Reserve Amount] so determined. If the sum of the amount available under the [Handback Performance Security] and the amount of cash on deposit in the [Handback Reserve Account] exceeds 100% of the new [Handback Reserve Amount], the [Developer] will be permitted (A) to cause the stated amount of the [Handback Performance Security] to be reduced by an amount equal to such excess, or (B) to direct that the excess cash then on deposit in the [Handback Reserve Account] be transferred to the [Developer].
- (d) At its sole cost, the [Developer] will be permitted to deposit a [Performance Security] (the **Handback Performance Security**) to the credit of the [Handback Reserve Account], which will have a scheduled expiration date no earlier than the first anniversary of the scheduled end of the [Term] (or, if it expires earlier than such date, permits a drawing of the full amount of the [Handback Performance Security] if the [Handback Performance Security] is not renewed or extended at least [X] days prior to its stated expiration date). The [Handback Performance Security] will be considered a part of the [Handback Reserve Account] and the amount available thereunder will be included in any calculations of the amount required to be on deposit in the [Handback Reserve Account]. The [Handback Performance Security] will provide that, if its [Term] is scheduled to expire prior to the termination of the [Handback Reserve Account], then the [Department] may draw thereon in an amount equal to the full amount available to be drawn thereunder. The [Department] will deposit the proceeds of any drawing on the [Handback Performance Security] into the [Handback Reserve Account].
- (e) The [Developer] shall be entitled to withdraw funds from the [Handback Reserve Account] in such amounts and at such times as needed only to pay for the improvement, repair, renewal or replacement of any [Element] to ensure each [Element] has the [Required Residual Life], and otherwise meets the [Handback Requirements], at the end of the [Term].
- (f) Prior to drawing funds from the [Handback Reserve Account], the [Developer] shall give written notice to the [Department] of the amount to be drawn and the purpose for which funds will be used, together with such other supporting information as the [Department] may reasonably require. Within [X] days from the date of the receipt of such notice, the [Department] shall either approve or withhold its approval to [Developer]'s proposed withdrawal. The [Department] may only withhold its approval to any proposed withdrawal from the [Handback Reserve Account] to the extent that:
 - (i) the [Developer] is unable to demonstrate to the reasonable satisfaction of the [Department] that the proposed withdrawal amount will be used to meet costs incurred by [Developer] in undertaking improvement, repair, renewal or replacement of any [Element] to ensure each [Element] has the [Required Residual Life], and otherwise meets the [Handback Requirements], at the end of the [Term]; or
 - (ii) the balance standing to the credit of the [Handback Reserve Account] plus the aggregate amount of all withdrawals made from the [Handback Reserve Account] is less than the [Handback Reserve Amount],

provided, however, that if the [Department] fails to respond within such [X] day period, the [Department] will be deemed to have given its approval to such withdrawal request.

- (g) *On the last day of the [Term], the [Escrow Agent] shall pay any amounts standing to the credit of the [Handback Reserve Account] to the parties in the following order of priority:*
- (i) *first, an amount equal to that required to improve, repair, renew or replace each [Element] to the extent required for the [Developer] to have performed all of its obligations under the [Handback Requirements] as at the end of the [Term], shall be paid by the [Escrow Agent] to the [Department]; and*
 - (ii) *second, the remaining balance standing to the credit of the [Handback Reserve Account] shall be paid by the [Escrow Agent] to the [Developer].*

8.5 Payments in Lieu of Meeting Handback Requirements

Some Projects may include a specific provision in the Concession Agreement allowing the Developer to make a payment to the Department in an amount equal to the cost of performing any necessary repairs or renewals in lieu of meeting the Handback Requirements for some or all of the Elements of the Project. This payment may be in addition to general handback amounts payable to the Department in respect of short-life Elements.

This provision may be particularly relevant if the Equity Investors at the end of the Term have changed from those at the beginning of the Term and these new Equity Investors are mere investors rather than experienced contractors or operators of toll roads (see also Chapter 5 (Changes in Equity Interests)). In such cases, it would be preferable for the investor to arrange for a payment to be made to the Department rather than undertaking management of the Renewal Work needed to restore the Project to the condition that the Handback Requirements dictate.

An example in-lieu payments provision is set forth below.

- (a) *The [Developer] shall have the option to pay an amount equal to the cost of the [Renewal Work] that will be necessary for the [Department] to perform after the end of the [Term] to ensure that the [Residual Life] at the end of the [Term] of the [Element] equals or exceeds the [Required Residual Life] for the [Element] in lieu of the [Developer] itself performing such [Renewal Work] necessary to meet the [Handback Requirements].*
- (b) *The [Developer] shall make the payment required under paragraph (a) by making a deposit into the [Handback Reserve Account] for transfer and release to the [Department] at the end of the [Term], free and clear of all liens, pledges, and encumbrances.*
- (c) *The [Developer] shall deliver written notice to the [Department] prior to the first day of the fifth full calendar year prior to the end of the [Term] setting forth its election to exercise its rights under paragraph (a) above for each [applicable] [Element] of the [Project]. Failure by the [Developer] to deliver such written notice to the Department by such deadline or failure of the [Developer] to include any [Element] in the written notice shall be deemed an election by the [Developer] to perform all [Renewal Work] necessary to ensure that the [Residual Life at Handback] of the [Element] meets or exceeds the [Required Residual Life].*

APPENDIX A – Glossary of Terms

The glossary of terms provided below is designed to be used as an educational tool to assist in understanding the Model Public-Private Partnership Core Toll Concessions Contract Guide. The below terms are illustrative and should not be construed as legal advice, notwithstanding that a number of the terms contained below may also be used in example provisions provided in the Guide.

Term	Description
Account Balances	Amounts held in or credited to certain bank accounts of the Developer which reduce the total amount of Termination Sum payable by the Department.
Applicable Law	Any local, State or Federal laws, rules or regulations that apply to the Developer or the Project.
Appropriations Risk	The risk that a State legislature will not appropriate or allocate to the Department sufficient funds to permit the Department to meet its payment obligations to the Developer under the Concession Agreement.
Base Case Financial Model	The financial model containing agreed projections and calculations regarding revenues, expenses, dividends and repayment of debt and equity relating to the Project as well as agreed economic assumptions. The Base Case Financial Model will be prepared in excel format and may be used, among other things, to calculate the projected Equity IRR over the Term, as may be updated in accordance with the terms of the Concession Agreement.
Benefit-Sharing	The sharing of financial benefits between the Developer and the Department according to the terms of the Concession Agreement, as described in Section 3.1 of the Guide.
Breakage Costs	Any commercially reasonable costs, make-whole payments or other prepayment amounts (including premiums) that the Developer must pay under any Financing Document as a result of the early repayment of such debt prior to its scheduled maturity date.
Caps and Floors	Terms derived from instruments used in the financial markets, which establish a maximum (cap) and minimum (floor) price, such as an interest rate, for a financial instrument. Often used together (in which case, a collar), caps and floors are considered cost-effective ways to financial risks, such as changes in interest rates.
Change in Law	A new or changed Law that is applicable to the Project as compared to that in effect when the Project was procured as described in Section 6.7 of the Guide.
Change in Ownership	A change in the direct or indirect ownership of the Developer, as described in Section 5.2 of the Guide.
Change Order	A written order from the Department to the Developer requesting a change in the Construction Work as compared to the Construction Work originally required to be performed by the Developer under the Project Documents.
Collateral Agent	In circumstances where there is more than one secured Lender involved in a Project, the Lenders will often appoint a Collateral Agent that holds the collateral provided as security for the Project, such as a real property mortgage or an all-asset pledge agreement from the Developer, on behalf of the secured parties.
Compensation Amount	The amount of any compensation payable by the Department to the Concessionaire with respect to any Compensation Event.
Compensation Event	The occurrence of one or more events which delay or increase the cost of the Developer's performance of its obligations under the Concession Agreement or which reduce the Developer's revenue, as described in Section 4.3.1 of the Guide.
Competing Facility	A transportation facility managed or built by the Department in the vicinity of the Project which may give rise to a Compensation Event if the Developer's traffic and revenue are reduced as a result, as described in Section 4.3.2 of the Guide.

Concession	The contractual right granted by the Department to the Developer to design, build, finance, operate and maintain a particular asset owned by the Department, which will be documented and governed by the terms of a Concession Agreement.
Concession Agreement	This term is defined or otherwise described in Section 1.2 of the Guide. This document is also sometimes known in the market as a “Comprehensive Agreement,” a “Concession and Lease Agreement,” or a “Public-Private Partnership Agreement.”
Concession Fee	The amount of any fee payable with respect to benefit-sharing. This fee is also sometimes known in the market as a “permit fee” or “revenue-sharing payment.”
Construction Period	The period starting upon the commencement of construction of the new asset being developed as part of the Project, and ending at the achievement of Substantial Completion.
Construction Work	All Work to build or construct, make, form, manufacture, furnish, install, supply, deliver, landscape or equip the Project.
Cost to Complete	The cost to the Department to complete the Project following a Developer Default prior to Substantial Completion, as described in Section 7.3.4 of the Guide.
Defects Liability Period	A proscribed period (generally 2 to 5 years) following Substantial Completion of the Project during which time the Design-Build Contractor must account to the Developer for defects in the construction of the Project.
Delay Event	The occurrence of one or more events which delay the Developer’s performance of its obligations under the Concession Agreement, as described in Section 4.3.3 of the Guide.
Demand and Revenue Risk	The risk that traffic demand for the relevant Project, and Toll Revenues received by the Developer, do not match the projections used to generate the Developer’s expected rate of return.
Department	The public authority granting rights to the Developer to design, build, finance, operate and maintain the Project in accordance with the Concession Agreement.
Department Default	The occurrence of one or more specified failures of the Department to perform its obligations under the Concession Agreement, as described in Section 7.2.1 of the Guide.
Department Default Termination Sum	The amount payable by the Department to the Developer following a termination of the Concession Agreement for a Department Default, as described in Section 7.2.4 of the Guide.
Design-Build Contract	The contract between the Developer and the Design-Build Contractor pursuant to which the Design-Build Contractor agrees to carry out the design work and the Construction Work and related services on the Project.
Design-Build Contractor	The contractor hired by the Developer to carry out the Construction Work and related services on the Project pursuant to the Design-Build Contract. The Design-Build Contractor may be an affiliate of the Developer.
Developer	The private entity that contracts with the Department to undertake some or all of the design, construction, financing, operations and maintenance relating to a Project that is to become subject to a Concession Agreement.
Developer Default	The occurrence of one or more specified failures of the Developer to perform its obligations under the Concession Agreement, as described in Section 7.3.1 of the Guide.
Developer Default Termination Sum	The amount payable by the Department to the Developer following a termination of the Concession Agreement for a Developer Default, as described in Section 7.3.4 of the Guide.
Direct Agreement	The agreement between the Developer, the Department and the Collateral Agent under which, among other things, the Department provides consent to provision of security over the Developer’s rights in the Project and grants the Collateral Agent step-in rights and cure rights in the event of a Developer Default under the Concession Agreement.
Discriminatory Change in Law	This term is defined or otherwise described in Section 6.5 of the Guide.

Dispute Resolution Mechanism	The provisions contained within the Concession Agreement that outline how the parties will resolve disputes, which generally include an initial good faith effort to reach agreement, when disputes are to be reviewed by a technical advisor and/or disputes review board and the use of arbitration and traditional litigation.
Early Termination	Termination of a Concession Agreement for any reason prior to the original stated expiration of the Term, including by reason of a default by either party or a Force Majeure Event.
Early Termination Date	The effective date of early termination.
Electronic Toll Collection Agreement	An agreement pursuant to which the Department provides toll transaction account management services and other “back office” functions to the Developer.
Electronic Toll Collection System	An automatic electronic system used to collect tolls.
Electronic Tolling	The collection of tolls by a toll operator using an Electronic Toll Collection System.
Element	Each individual component, system, or subsystem of the Project.
Equity Investors	The entities which directly or indirectly own the Developer and invest equity into the Project, also known as “sponsors” or “shareholders.”
Equity IRR	The internal rate of return that the Equity Investors have projected to be derived from the Project in accordance with the Base Case Financial Model, as may be updated in accordance with the terms of the Concession Agreement.
Escrow Agent	A third party hired to hold and control the Handback Reserve Account, as described in Section 8.4.2 of the Guide.
Exempt Vehicles	A class of vehicles (e.g., commuter buses) which is entitled to a discount from otherwise applicable tolls.
Express Toll Lane	A traffic lane subject to tolls that vary with demand in order to maintain average speed at or above a stated level.
Financing Documents	All documentation relating to the financing of the Project (excluding Shareholder Loans), including loan documentation, security documentation, credit support documentation, hedging documentation, and intercreditor documentation.
Financial Close Date	The date on which the conditions precedent to the provision of financing to fund the Project have been met. These conditions include execution of the Transaction Documents, delivery of the Base Case Financial Model, delivery of requisite legal opinions and confirmation that the requisite equity investment or Shareholder Loan/s have been made by the Equity Investors.
Force Majeure Event	One of a set of agreed events outside the control of either the Department or the Developer which may permit the Developer to seek relief under the Concession Agreement, as described in Section 4.3.5 of the Guide.
Force Majeure Termination Sum	The amount payable by the Department to the Developer following a termination of the Concession Agreement for a Force Majeure Event, as described in Section 7.4.2 of the Guide.
Governmental Approval	All approvals, permits, permissions, consents, licenses, certificates and authorizations required from time to time in connection with the Project whether issued by the Department or any Governmental Authority.
Governmental Authority	Any court, Federal, State, or local government, department, commission, board, bureau, agency, or other regulatory or governmental authority, other than the Department.
Greenfield Project	In a P3 context, a greenfield project is a Project that requires the construction of a new asset. The Concession Agreement in respect of the greenfield project will include the design and construction of the new asset, as well as the operation and maintenance of the asset.
Gross Revenues	All amounts received by the Developer in relation to the Project, including Toll Revenues, insurance proceeds (to the extent received to compensate for the loss of tolls and user fees) and interest income.
Handback	The return of the Project to the Department at the end of the Term, as described in Section 8.1 of the Guide.
Handback Inspections	Regular inspections conducted by the Developer during the Handback Period, as described in Section 8.3 of the Guide.

Handback Performance Security	Any performance security the amount of which is credited to the Handback Reserve Account.
Handback Period	The final years of the Term, during which the Developer is required to prepare for and manage the handback of the Project to the Department, as described in Section 8.2.1 of the Guide.
Handback Requirements	The performance standards for the Project's major assets required to be achieved by the Developer prior to handback of the Project to the Department, as described in Section 8.2.1 of the Guide.
Handback Reserve Account	The account in which the Handback Reserve Amount is held, as described in Section 8.4.1 of the Guide.
Handback Reserve Amount	An amount required to be held by the Developer to pay the cost of complying with the Handback Requirements, as described in Section 8.4.1 of the Guide.
Hazardous Substances	Any substance which is considered a contaminant, pollutant, dangerous substance, toxic substance, solid waste, or hazardous material which is deemed hazardous or toxic under, or otherwise regulated by, environmental laws.
High-Occupancy Vehicle (HOV)	A vehicle which contains multiple passengers, generally two or more.
High-Occupancy Toll (HOT) Lane	A high-occupancy vehicle (HOV) traffic lane that includes a road pricing scheme allowing motorists in non-HOVs access to such high-occupancy vehicle lanes if they pay a toll.
High-Occupancy Vehicle Lane	A restricted traffic lane reserved for motorists in HOVs, generally during peak travel times.
Highway Project	The design, construction, finance, operation, and maintenance of an asset comprising a highway.
Insurance Proceeds	Any insurance proceeds available to the Department for the purposes of achieving Substantial Completion.
Key Assets	The assets and contractual rights necessary to enable the Department to continue a Project following a termination of the Concession Agreement, as described in Section 7.6.4 of the Guide.
Key Contractor	The relevant Subcontractor under designated "key contracts" relating to the Project, which will generally include the Design-Build Contract, the Operations and Maintenance Contract and any significant services contract with a value over a designated amount.
Law	All laws, rules and regulations applicable to the Developer or the Project, as described in Section 6.7 of the Guide.
Lenders	Each bank or financial institution, including the U.S. Department of Transportation via the Federal Highway Administration (as lender of a TIFIA loan), or any other entity that provides Project Debt (excluding Shareholder Loans or any other financing provided by Equity Investors).
Life-Cycle	In relation to an asset, the course of the Useful Life of that asset.
Life-Cycle Maintenance / Investments / Costs	In relation to an asset, money or materials invested to maintain the asset during the life-cycle of that asset.
Life-Cycle Maintenance Plan	The Developer's plan to manage its major maintenance and handback obligations during the life of the Project, as described in Section 8.2.3 of the Guide.
Long Stop Date	The date, being a designated period of days following the date Substantial Completion is scheduled to occur, following which time, if Substantial Completion has not occurred, a Developer Default will occur under the Concession Agreement.
Losses	Any losses, liabilities, judgments, damages, fees, penalties, fines, sanctions, charges, or out-of-pocket and documented costs or expenses actually suffered or incurred.
Maintenance Work	Work required to be undertaken by the Developer in relation to the maintenance of the Project, including routine maintenance and Renewal Work.
Major Maintenance Reserve Account	An account established by the Developer which must contain sufficient funds to pay for projected Renewal Work required over a given period in respect of the Project.

Managed Lane Facility	A toll road concession such as a high-occupancy toll lane, an express toll lane or an exclusive/special-use lane with tolls for certain users that vary with demand.
MAP-21	Moving Ahead for Progress in the 21st Century Act.
Net Cost Impact	The increase in the Developer's costs due to a Compensation Event, as described in Section 4.4.3.1 of the Guide.
Net Cost Savings	The decrease in the Developer's costs due to a Compensation Event, as described in Section 4.4.2.1 of the Guide.
Net Project Debt	The amount of the Developer's Project Debt less its Account Balances, as described in Section 7.3.4 of the Guide.
Net Revenue Impact	The net increase or decrease in the Developer's revenue due to a Compensation Event, as described in Section 4.4.2.1 of the Guide.
Nondiscriminatory Change in Law	A Change in Law that is not a Discriminatory Change in Law, as described in Section 6.7 of the Guide.
Operations and Maintenance Contract	The contract between the Developer and the Operations and Maintenance Contractor pursuant to which the Operations and Maintenance Contractor agrees to carry out operations and maintenance services for the Project.
Operations and Maintenance Contractor	The contractor hired by the Developer to carry out the operations and maintenance services on the Project pursuant to the Operations and Maintenance Contract. The Operations and Maintenance Contractor may be an affiliate of the Developer or the Developer may perform the Operations and Maintenance services itself.
Permitted Vehicle	In the context of a managed lane facility, those vehicles that are allowed to use the managed lane for public policy reasons, and generally include motorbikes, buses, transit vehicles, maintenance vehicles of the Department, and emergency vehicles.
Private Activity Bonds (PABs)	A bond issued for the purpose of financing a project. PABs are often issued via a conduit issuer (generally a finance vehicle of the Department), which then on-lends the money to the Developer. The Developer (rather than the Department) is liable for the payment of interest and redemption of the PABs. If issued for a designated purpose and provided other Federal and State requirements are complied with, PABs can be tax-exempt.
Prohibited Person	In the context of Change in Ownership provisions, and depending on the Department's requirements with respect to changes in ownership to particular entities of concern, those entities that give rise to concerns associated with national security, debarment from State or Federal procurement processes or egregious reputation who may not become Equity Investors.
Project	The asset to be designed, constructed, financed, operated and maintained by the Developer pursuant to the terms of the Concession Agreement.
Project Debt	The bona fide indebtedness related to the Project, including bank debt, PABs, TIFIA loans, guarantees, and credit support facilities. Project Debt includes not just principal and interest but also fees, expenses and any breakage costs. Project Debt does not include Shareholder Loans or any other financing provided by Equity Investors.
Project Documents	All documentation relating to the design, construction, operation and maintenance of the Project, including the Concession Agreement, the Design-Build Contract and the Operations and Maintenance Contract.
Project Right of Way	The real property which is necessary for the performance of the Work and operation of the Project.
Project Schedule	The construction schedule for the Project as agreed between the Department and Developer.
Project Value	The fair market value of the Developer's interest in the Project. This fair market value is generally determined by an independent appraiser and based on the projected cash flows and projected costs of the Project as of the date of determination until the end of the original Term.

Proposal Due Date	The due date for potential Developers (or their Equity Investors) to submit their proposals in response to a “Request For Proposals” issued by the Department in relation to an upcoming Project.
Public-Private Partnership /P3/ P3 Transaction	A contractual arrangement between a Department and a Developer as described in Section 1.1 of the Guide.
Qualified Investor	A list of Equity Investors in the Project that the Department has vetted as part of the procurement process and is comfortable with and has an interest in keeping as investors in the Project.
Ramp-Up Period	The initial period of operations for a Project before traffic reaches its expected steady state, as described in Section 7.2.4.2 of the Guide.
Refinancing Gain	The net financial gain the Developer may receive as a result of refinancing some or all of the Project Debt by, for example, securing lower interest rates as part of the refinancing or paying Equity Investors a dividend with the proceeds.
Related Entity	In the context of Change in Ownership provisions, this would generally include each entity in the ultimate ownership structure between the Developer and the Equity Investors, as well as all affiliated legal entities under common ownership and control.
Renewal Work	The renewal, repair or replacement of worn-out, obsolete, damaged, or under-performing components so that the Project does not prematurely deteriorate and remains fully functional.
Required Residual Life	The required Useful Life an Element must have following handback from the Developer to the Department.
Residual Life	The approximate Useful Life of an asset less its age if the asset has performed in service in the manner and with the levels of traffic and wear and tear originally expected by the Developer and if the Developer has properly maintained the asset in accordance with its obligations under the Project Documents.
Residual Life Methodology	The methodology for calculating the Residual Life of an asset at the end of the Term of a Concession Agreement, as described in Section 8.2.2 of the Guide.
Restricted Change in Ownership	A change in the ownership of the Developer that is restricted by the Concession Agreement, as described in Section 5.5 of the Guide.
Return Trigger	Equity IRR levels which trigger revenue sharing provisions in the Concession Agreement, as described in Section 3.2.1.2 of the Guide.
Revenue Sharing	The Developer’s sharing of revenues generated by a Project with the Department in accordance with the terms of the Concession Agreement, as described in Section 3.1 of the Guide.
Revenue Trigger	Levels of revenue which trigger revenue sharing provisions in the Concession Agreement, as described in Section 3.2.1.1 of the Guide.
Service Commencement Date	The date the Project opens for normal and continuous operations and use by the traveling public. This often, but not always, occurs at the same time as Substantial Completion.
Set-Off	The right of one party to deduct, from the amount owed to another party, any amount owed from such other person to the first person.
Shareholder Loans	Equity investments in the Developer which take the legal form of loans from the Equity Investor to the Developer.
Site	The development location of the Project.
State Highway	Any highway designated as a “State Highway” by the relevant State regulations.
Subcontract	An agreement between the Developer and a Subcontractor under which the Subcontractor will perform certain services contracted to be performed by the Developer under the Concession Agreement.
Subcontractor	The subcontractor under a Subcontract, including the Design-Build Contractor and the Operations and Maintenance Contractor.
Subcontractor Breakage Costs	Liabilities incurred in respect of demobilization of Subcontractors and the cancellation of orders for materials and goods which arise as a result of the early termination of the Concession Agreement, as described in Section 7.2.4.4 of the Guide.

Substantial Completion	When the Developer has completed all the Construction Work required by it under the Concession Agreement and the Project is substantially ready for normal and safe use and operation.
Substantial Completion Date	The date Substantial Completion is achieved, usually evidenced by a certificate issued by the Department.
Supervening Events	A set of defined events or circumstances giving rise to a claim for relief under the Concession Agreement, as described in Section 4.1 of the Guide.
Term	The duration of the grant of the concession to the Developer under the Concession Agreement, usually from the date of the Concession Agreement for a fixed period of years, unless terminated early.
Termination for Convenience Termination Sum	The amount payable by the Department to the Developer following a termination of the Concession Agreement for convenience by the Department, as described in Section 7.5.2 of the Guide.
Termination Sum	The amount of compensation payable to the Developer from the Department in the event the Concession Agreement is terminated early, including, depending on the reason for the early termination, the Termination for Convenience Termination Sum, the Department Default Termination Sum, the Developer Default Termination Sum and the Force Majeure Termination Sum.
TIFIA	The program administering loans under the Transportation Infrastructure Finance and Innovation Act, which provides Federal credit assistance in the form of direct loans, loan guarantees, and standby lines of credit to finance eligible surface transportation projects.
Time Impact Analysis	A method used to determine the extent of a delay in the critical path of a construction project, as described in Section 4.4.1 of the Guide.
Title 23 of the United States Code	The United States Code is a codification of the general Federal laws of the United States. Title 23 outlines the role of highways, including Federal-aid and other highways, highway safety and research and technology relating to highways.
Toll Enforcement and Violation Processing Services Agreement	An agreement pursuant to which the Developer secures toll enforcement and violations processing services, usually through existing agreements the Department has with law enforcement and State agencies.
Toll Revenues	The fees, tolls, rates, and other charges generated from vehicles using the Project and other amounts received by the Developer in connection with such revenues, including proceeds of insurance, amounts payable by the Department under the Concession Agreement and amounts awarded as damages or from enforcement action or settlement.
Tolling Rights	The right to establish, assess, collect, enforce (subject to applicable law), and retain tolls paid by users of the Project.
Toll Road Concession	A concession granted to a Developer in relation to a toll road facility.
Transaction Documents	All documentation relating to the Project, including Financing Documents and Project Documents.
Transportation Facilities	Facilities relating to transportation, including bridges, railways, freight ways, highways, and toll roads.
Unknown Endangered Species	Endangered or threatened species found on the Site or other Project Right of Way that were not contained in the site conditions report prepared for the Project or otherwise known (or should have been known) to the Developer.
Unknown Geotechnical Condition	Subsurface or latent geological conditions found on the Site or other Project Right of Way that were not contained in the site conditions report prepared for the Project or otherwise known (or should have been known) to the Developer.
Unknown Pre-Existing Hazardous Substances	Hazardous Substances found on the Site or other Project Right of Way that were not contained in the site conditions report prepared for the Project or otherwise known (or should have been known) to the Developer.
Unknown Utility	Public or private utility systems found on the Site or other Project Right of Way that were not contained in the site conditions report prepared for the Project or otherwise known (or should have been known) to the Developer.

Useful Life	The period a new, renewed, or replaced asset is expected to remain in service under ordinary maintenance until it next requires reconstruction, rehabilitation, restoration, renewal, or replacement.
Video-Based Tolling	The collection of tolls using video technology to capture license plate data.
Work	All services required to be undertaken by the Developer in relation to the Project under the Concession Agreement, including design work, Construction Work and Maintenance Work.
Work Value	The value of completed work for a construction project, calculated as described in Section 7.3.4 of the Guide.