Draft Guidelines for Infrastructure Project Financing (IPF)

Banking Policy Department

State Bank of Pakistan

The last date of submitting suggestions/recommendations in the draft guidelines to the Housing Finance & Infrastructure Development Division, Banking Policy Department, is **30th November 2004**. For details and further assistance please contact:

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PREFACE

In order to facilitate banks/DFIs for undertaking financing of infrastructure projects Guidelines for **Infrastructure Project Financing (IPF)** have been devised. These guidelines will enable the private sector participation and funding of infrastructure projects, especially those under long-term government concession agreements. It is significant to note that traditional corporate finance demands that the primary source of repayment for investors and creditors is the borrowing company backed by its entire balance sheet and not just the net realizable value of the project alone. Whereas, IPF ideally requires 'non-recourse financing', wherein the lenders look solely to the cash flows of the project for debt service. However, in the context of Pakistan 'limited-recourse financing' is preferable, wherein lenders in addition to the cash flows generating ability of the project for debt repayment also have access to the sponsor's credit/legal security for debt servicing.

Infrastructure projects, by their nature and design, require relatively large investment, besides needing longer gestation period for development, construction, start-up and operation. Therefore, IPFs are characterized with high cost of capital equipment along with large transaction costs for structuring that inevitably needs long term financing. At the same time, IPF may benefit primarily those sectors or industries in which projects can be structured as a separate entity, apart from sponsors. Therefore, keeping in view the distinctive features of infrastructure projects, the guidelines have been devised to highlight certain important aspects of the IPF.

It is hoped that these guidelines will help banks/DFIs to develop expertise for financing of infrastructure projects, essentially by evaluating the intrinsic cash flow generating ability of these projects on the basis of sectoral and sub-sectoral studies and other data regarding volume of expected use and future cash projections of infrastructure projects.

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PART- A
D E F I N I T I O N S

For the purpose of these guidelines:

1. **'Asset Securitization'** means a process whereby any Special Purpose Vehicle raises funds by issue of Term Finance Certificates or any other instruments with the approval of Securities and Exchange Commission of Pakistan (SEC), for such purpose and uses such funds by making payment to the Originator and through such process acquires the title, property or right in the receivables or other assets in the form of actionable claims.

2. **'Asset Securitization through Special Purpose Vehicle (SPV)'** means asset securitisation through SPV as laid down in BPD Circular No. 31 of November 14, 2002.

3. **'Bank'** means a banking company as defined in Banking Companies Ordinance, 1962.

4. **'Borrower'** means Concessionaire/Licensee/Project Company of an Infrastructure Project on whom bank(s)/DFI(s) has (have) taken any exposure during the course of business, including their successor(s) also.

5. **'Concession Agreement'** means an agreement, usually with the government authority, to operate the project or provide the specified services for a certain period of time.

6. **'Concessionaire/Licensee'** means legal entity, incorporated by sponsors of an Infrastructure Project, to whom a Concession/License is awarded by a government agency, including their successor(s) in the titles and assignments also.

7. **‘Contractor(s)’** means the various entities, who may be awarded the contract for construction, supply of materials, operation and maintenance of an Infrastructure Project by the Concessionaire/Licensee/Project Company.

8. **‘DFI’** means a Development Financial Institution viz. Pakistan Industrial Credit and Investment Corporation, Pak Kuwait Investment Company (Pvt.) Ltd., Pak Libya Holding Company Ltd., Pak Oman Investment Co. (Pvt.) Ltd., Saudi Pak Industrial & Agriculture Investment Ltd.

9. **‘Federal Government’** means the Government of the Islamic Republic of Pakistan and its duly authorized representatives.

10. **‘Financing Agreement (s)’** means the agreement (s) to be entered into between the Concessionaire/Licensee/Project Company and the Lenders for the purpose of providing the funds necessary to carry out an Infrastructure Project, including any and all agreements/documents providing security of such financing.

11. **‘Financial Completion’** means project’s ability to produce below a certain unit cost or minimum traffic volume above a certain level or compliance of any similar conditionality for a specified period of time, such as six months; to have a minimum level of working capital and achieve a certain current ratio; and to achieve a minimum debt-service coverage ratio or debt-to-equity ratio for a certain period, such as one year as per the Financial Agreement(s).

12. **‘Government Agency’** means:
    (a) a division, department, attached department, bureau, section, commission, board, office or unit of the Federal Government or a Provincial Government;
    (b) a development or a local authority, company or corporation established or controlled by the Federal Government or Provincial Government.

13. **‘Infrastructure Project’** means one of the followings:

    (a) A road, including toll road, fly over, bridge project;

    (b) A mass transit, urban bus, urban rail project;

    (c) A rail-bed, stations system, rail freight, passenger services project;

    (d) A telecommunication local services, long distance and value added project;

    (e) A power generation project;

    (f) A power transmission or distribution project by laying a network of new transmission or distribution lines;

    (g) A natural gas exploration and distribution project,

    (h) A LPG extraction, distribution and marketing project;

    (i) A LPG import terminal, distribution and marketing project;

    (j) A water supply, irrigation, water treatment system, sanitation and sewerage system or solid waste management system project;

    (k) A dam, barrage, canal project;

    (l) A primary and secondary irrigation, tertiary (on-farm) irrigation project;

    (m) A port, channel dredging, shipping, inland waterway, container terminals project;

    (n) An airport;

    (o) A petroleum extraction, refinery, pipeline project;

    (p) Any other infrastructure project of similar nature, notified by SBP.

14. **‘Infrastructure Project Financing (IPF)’** means financing for an Infrastructure Project.

15. **‘Lender’** means a bank/DFI providing, raising or making available, directly or indirectly, finance or refinance (however, such finance and refinance shall not include amounts subscribed for equity share capital of the shareholders of the Concessionaire/Licensee) for the performance of the works, and shall include Concessionaire/Licensee and their respective successors in title and assigns. The term lenders shall also include consortium of lenders, if any, a trustee or a security agent appointed by the lenders.

16. **‘License’** means a permission granted by a government agency to a private sponsor for undertaking an Infrastructure Project.

17. **‘Limited-Recourse Financing’** means a form of project financing in which lenders look mainly to the cash flows of a project to repay debt service but where, under certain conditions (legal or financial), lenders may also have access to the sponsor’s assets for repayment.

18. **‘Liquid Assets’** means assets which are readily convertible into cash without recourse to a court of law and mean encashment/realizable value of government securities, bank deposits, certificates of deposit, shares of listed companies which are actively traded on the stock exchange, NIT Units, certificates of mutual funds, Certificates of Investment (COIs) issued by DFIs / NBFCs rated at least ‘A’ by a credit rating agency on the approved panel of State Bank of Pakistan, listed TFCs rated at least ‘A’ by a credit rating agency on the approved panel of State Bank of Pakistan and certificates of asset management companies for which there is a bookmaker quoting daily offer and bid rates and there is active secondary market trading. These assets with appropriate margins should be in possession of the banks/DFIs with perfected lien. Guarantees issued by domestic banks/DFIs when received as collateral by banks/DFIs will be treated at par with liquid assets; whereas, for guarantees issued by foreign banks, the issuing banks’ rating, assigned either by Standard & Poors, Moody’s or Fitch-Ibca, should be ‘A’ and above or equivalent.

19. **‘Local Authority’** means any agency set up or designated by the Federal Government or a Provincial Government, by notification in the official Gazette, to be a local authority.

20. **‘Non-recourse Financing’** means a form of project financing in which lenders look solely to the cash flows of a project to repay debt service. Non-recourse structures are used only where the project is clearly capable of supporting debt, even under adverse scenarios.

21. **‘Physical Completion’** means the project’s ability to sustain production at a certain capacity for a specified period of time, such as one month or one quarter of the operating year. Before this, the project would also be certified as technically complete, that is, as meeting all technical design specification.

22. **‘Project Account (s)’** means one or more Project Accounts for the purpose of depositing contributions towards the equity of the Concessionaire/Licensee/Project Company and the disbursement of loans by the Lenders under the Financing Agreement(s). The Project Account(s) can also be utilized for depositing surplus receipts after appropriations for debt servicing, project maintenance and any other appropriations as per the Financing Agreement(s) from the Project Collection Account. Moreover, all expenditure made with respect to the due performance of its obligation by the Concessionaire/Licensee/Project Company shall be through such Project Account (s).

23. **‘Project Capital Cost’** means the total construction costs of a project on an un-leveraged (all-equity) basis, which includes project development cost, land, owners’ costs of construction, and initial working capital.

24. **‘Project Collection Account’** means an account opened for the exclusive collection/deposit of all revenue receipt of an infrastructure project that shall be operated by the Concessionaire/Licensee/Project Company in accordance with financing agreements with the lenders. Any amounts standing to the credit of the Project Collection Account, after appropriations for debt servicing, maintenance and other appropriation(s) as per the Financing Agreement(s) shall be remitted to the Project Account (s).

25. **‘Project Company’** means the legal entity, which owns and operates a project. In project financing, this company has assets that include the project’s physical assets and the underlying contracts supporting the project.

26. **‘Project Debt Reserve Account’** means an account created for the period of financing provided by the Lenders that shall be funded by the Concessionaire/Licensee/Project Company as per the Financing Agreement(s) from the Project Account and/or the Project Collection Account to amortize debt.

27. **‘Project Escrow Account’** means an account maintained by the Concessionaire/Licensee/Project Company for the entire remaining tenure of the Concession/License/Right of Way, wherein every month a portion from the total proceeds of revenue receipts of the Infrastructure Project shall be deposited by way of remittance from the Project Collection Account. The amounts standing to the credit of the Project Escrow Account shall be solely utilized for the routine and periodic maintenance of the Infrastructure Project.

28. **‘Project Finance’** means a form of either ‘non-recourse’ or ‘limited recourse’ financing, wherein lenders look solely or primarily to the cash flows of a project to repay debt service and to all of the underlying project assets (including all physical and contractual assets) as collateral for the loan.

29. **‘Project Cost’** means the total financing (debt and equity) required to complete construction of a project. Includes capital costs, financing fees, interest that accumulates during the construction period, and any amounts required to be set aside to be available to pay debt service when a problem develops.

30. **‘Project Funds Agreement (PFA)’** means an agreement, usually by sponsors, to provide additional funds as needed until project completion or other agreed date. However, burden of additional funds may be shared amongst sponsors, creditors and suppliers as per their mutual consent under a PFA.

31. **‘Project Sponsor’** means the primary beneficiary and proponent of a project. A party interested in supporting a project financing. A party providing the credit to support a project financing.

32. ‘**Provincial Government’** means the Government of Punjab, Sindh, NWFP and Balochistan.

33. **‘Public Utilities’** means water supply, electricity supply, telecommunication system, sewerage system, petroleum, gas supply and other utilities and amenities for the benefit of the public.

34. **‘Right of Way’** means the existing corridor already available with a government agency and any additional land which may have to be acquired by a government agency for the purposes of the Infrastructure Project.

35. **‘Special Purpose Vehicle’** means a special purpose vehicle registered by the SEC for the purpose of Securitization;

36. **‘Sponsor(s)’** means promoter of an infrastructure project, whose equity participation in the project company is 10% or more.

37. **‘Structured Finance’** means a financial instrument tailored to the risk-return and maturity needs of the investor, rather than a simple claim against an entity or asset, where the financier does not look at the entity as a risk: but tries to align the financing to specific cash flow of the borrower.

38. **‘Subordinated Loan’** means an unsecured loan extended to the borrower by its sponsors, subordinate to the claim of the bank / DFI taking exposure on the borrower and documented by a formal sub-ordination agreement between provider of the loan and the bank/DFI. The loan shall be disclosed in the annual audited financial statements of the borrower as subordinated loan.

39. **‘Term Sheet’** means a document that outlines in general terms the key agreements to be contained in a legal document; other terms loosely associated and often used

interchangeably are a letter of understanding (LOU) and a memorandum of understanding (MOU).

PART - B
G U I D E L I N E S

G.1 CREDIT APPRAISAL

The need of conducting credit appraisal of an IPF by banks/DFIs is of utmost importance because this helps in identifying project risks, besides assessing its technical and environmental feasibility to ascertain whether the project will be able to function as per plans. Assessment of financial and economic viability of the project is also needed to determine whether the project will be able to generate sufficient cash flows to repay debts and produce a satisfactory rate of equity return. Therefore, banks/DFIs are encouraged to develop the requisite expertise for appraising technical feasibility, financial viability and bankability of infrastructure projects, with particular reference to the risk and sensitivity analysis.

As IPF calls for special appraisal skills and expertise on the part of lending agencies, banks/DFIs may consider constituting appropriate screening committees/special Divisions/Department for appraisal of credit proposals and monitoring the progress/performance of the projects. Often, the size of the funding requirement would necessitate financing by more than one bank under consortium or syndication arrangements. In such cases, participating banks/DFIs may, for the purpose of their own assessment, refer to the Appraisal Report or Information Memorandum prepared by the lead bank/DFI or have the project jointly appraised.

Moreover, in order to ensure timely and adequate availability of credit, which is a pre-requisite for successful completion of infrastructure projects, banks are advised to clearly delineate the procedure for approval of loan proposals and institute a suitable monitoring mechanism for reviewing loan applications pending beyond the specified period. Multiplicity of appraisals by every institution involved in financing, which may lead to delays in financing an infrastructure project may be avoided, if possible therefore,

banks are encouraged to consider broadly accepting technical parameters laid down by any leading domestic financial institution in accordance with international best practices.

G.1.1 Minimum Information Requirements

Banks/DFIs, for the purpose of suitably conducting credit appraisal shall obtain comprehensive/detailed Feasibility Report of Infrastructure Project before sanctioning the loan. The Feasibility Report, which needs to be endorsed by an Auditing Firm either approved by SBP or on the panel of SBP, shall contain the information relating to project's anticipated economic conditions, capital investment, and financing. Moreover, Banks/DFIs may obtain minimum information to their satisfaction regarding an Infrastructure Project in accordance with the **Annex-A (IPF: Checklist for Minimum Information Requirements).**

G.1.2 Assessment of Infrastructure Projects

Infrastructure projects usually go through development, construction, start-up, and operation stages, therefore, during the credit appraisal process, banks/DFIs should assess these stages separately for risk mitigation, the details of which are as under:

G.1.2.1 Development Phase: In this phase the risk is usually very high, therefore, only equity capital from the main sponsors should be the primary funding source. In the development phase, the prospective sponsor essentially assesses the project's scope, seeks any necessary regulatory and concession approval from the government or municipal authorities, and attempts to attract financing. Moreover, if lenders decide to provide funding during this phase they should critically evaluate the possibility of risks arising from unclear government policies, if any, that can lead to long delays and even force sponsors to abandon an otherwise sound project.

G.1.2.2 Construction and Start-up Phase: In this phase, risk is high and large volumes of finance are required, typically in a mixture of equity, senior debt, subordinated debt, and guarantees. The major risk is that construction will not be completed on time, or have large cost overruns or will not meet the specifications set for the project. A project may fail to reach completion for any of a number of

reasons, ranging from technical design flaws to mismanagement of the project, financial problems, or changes in government regulations. Therefore, the lending bank(s)/DFI(s) is (are) advised to encourage the project companies to hedge construction risk by using fixed-price, certain-date construction contracts (including turnkey contracts), with built-in provisions for liquidated damages if the contractor fails to perform, and bonuses for better than expected performance. The project company may also be required to take appropriate measures (including insurance) to cover the risk, which may include construction contingency in the total cost of the project, besides building-up some excess capacity to allow for technical failures that may prevent the project from reaching the required capacity.

As lenders cannot control the construction process, therefore, Banks/DFIs are advised to negotiate that risks during completion phase of the project be the responsibility of the project company, its sponsors, contractors, equipment suppliers, and insurers.

At the same time, in order to protect against the risk of physical and financial incompletion of an infrastructure project, banks/DFIs are advised to closely observe following issues for risk mitigation:

i. **Project Funds Agreement (PFA):** As the most common threat to physical completion of a project is cost overruns, i.e. costs significantly exceed the initial financing plan, which affects the project's financial rate of return, and if these cost overruns cannot be financed, these may even lead to abandonment of the project. Therefore, to ensure that unexpected costs do not jeopardize the project' s physical completion, creditors and minority investors may insist on a commitment for a standby financing as part of the initial financial package. This may be provided by sponsors through contractual agreement, i.e. **Project Funds Agreement (PFA),** *which is a standby subordinated loan or equity, wherein sponsors may either provide or arrange the bulk of the financing facility.*

ii. **Financial Completion Agreement (FCA):** It is pertinent to emphasize that a new project may reach physical completion but not become

financially healthy or self-sustaining for any number of reasons, such as supply problems or weak market demand. If financial completion is not achieved, profitability will suffer, and the project is likely to encounter debt-service difficulties. Project documentation, therefore, may include a **Financial Completion Agreement (FCA)**, *which specifies, in contract form, the initial financial projections of the project against which creditors and investors are willing to invest funds.* Under a financial completion agreement, the sponsors typically provide subordinated loans or additional equity to the project until the agreed financial performance is achieved. By requiring sponsors to meet project financial completion, lenders greatly reduce the default risk of a project. In the light of international experiences, it is emphasized that there have been a number of instances wherein financial completion was not achieved until several years after physical completion, during which time the sponsor was called upon to provide additional financial resources to the project. The lenders may, at their own discretion, require the sponsors to arrange suitable insurance cover, if available, for covering this risk.

iii. **Project Insurance:** In order to ascertain the fulfillment of obligations of sponsors under PFA/FCA, banks/DFIs are advised that the obligations of sponsors under PFA/FCA sponsors are backed-up by a letter of credit, bond or guarantee for a creditable third party. However, for mitigating force majeure, which cannot be contractually allocated, banks/DFIs are advised to ascertain purchase of risk insurance by the sponsors so as to mitigate both direct and indirect types of force majeure (i.e. one that affects the project directly, as in the case of an earthquake or fire; the other indirectly, as in the case of a natural calamity that prevents a supplier from fulfilling its commitments to the project, respectively).

G.1.2.3 Operation Phase: In this phase, the risk is generally lower because the project is almost in the final stage and it may be possible to refinance senior bank debt in the capital markets with cheaper, less restrictive bonds. As most of the projects funded under a project finance structure are long-term enterprises, and

during this time significant changes may take place that undermine the project's viability, e.g. availability and cost of inputs, the technical performance and management of the project, market demand for the project's output etc, therefore, banks/DFIs while undertaking IPF are advised to encourage the sponsors of the project to prearrange long term purchase contracts (where applicable) for important inputs, such as raw materials or energy supplier, to limit the impact of price volatility, particularly in the case of primary commodities. The project company may also be encouraged by banks/DFIs to ask its suppliers for performance guarantees on technical components and may subcontract the project's operation and maintenance to a specialist company, with penalty payments if performance is not up to the standard.

G.1.3 Monitoring of Infrastructure Projects

Banks/DFIs are encouraged to set up a mechanism for ongoing monitoring of the project implementation for ensuring that the credit disbursed is utilized for the purpose for which it was approved. Accordingly, proper scrutiny/audit shall be ensured of the Project Account(s), Project Collection Account, Project Debt Reserve Account, Project Escrow Account and any other accounts deemed necessary for the operation of an Infrastructure Project, as per the Financing Agreement between the Project Company and Lenders.

G.1.3.1 Monitoring for Assignment of Project Receivables and Payments for Damages: As the primary source of repayment is project cash flows, lenders need to secure the loan by obtaining an assignment of project receivables, which enables creditors to determine how project funds will be used if the project runs into difficulties. A project usually has many other kinds of agreements covering such matters as government concession, management, and supply. Premature termination of any of these agreements could adversely affect the project and usually a party terminating an agreement prematurely pays for the damages caused to the other parties. Therefore, keeping in view such an adverse eventuality, banks/DFIs may institute necessary monitoring measure so as to

ensure the assignment of project receivables and payments on account of damages.

G.1.3.2 Monitoring for Ensuring Enforcement of Security: In order to ensure that the project company will not create security on fixed assets in favor of third parties, banks/DFIs may require the project company to create a negative pledge on its fixed assets. This will ensure that if and when lenders want to have recourse to the security, the fixed assets of the company are unencumbered and available.

G.1.3.3 Project Escrow Accounts for Monitoring Repayment of Debt: In 'limited recourse financing', the importance of escrow account increases due to the fact that the primary security is the project receivables/cash-flows. A project may generate sufficient cash flows to repay its debt; however, sponsors could divert these flows to serve other purposes within or outside the project to the detriment of the lenders. Therefore, establishment of an escrow account is essential for ensuring that the project's free cash flows are used first of all for debt service or other pre-agreed expenses. An escrow account not only ensures that contract obligations are met, but also help control project expenditures. Therefore, banks/DFIs are encouraged to institute a mechanism for repayment of project debts through an escrow account, which shall preferably be pledged by the project company in favor of lenders for improving the project's overall security package.

G.2 COLLATERAL ARRANGEMENTS AND SECURITY PACKAGE

G.2.1 Acceptance of Concession/License as Collateral

In order to promote 'limited recourse financing', which is essential for the funding of infrastructure projects in the private sector, banks/DFIs are encouraged to accept a "Concession Agreement/License" issued by a Government Agency as a collateral for infrastructure project financing, in the overall collateral arrangements worked out with the debtors, subject to the following stipulations:

i. The Concession Agreement/License is free of all encumbrances, irrevocable and does not contain any term or condition which may be detrimental to the interest of the lenders;
ii. The Concession Agreement/License should be assignable to lenders in the event of default;
iii. The Government Agency that has issued the Concession Agreement/License undertakes to facilitate lenders in the transfer of Concession Agreement/License in case of default;
iv. Public utilities are shifted appropriately from the area by the Government;
v. Commercial banks/DFIs, on the basis of studies and other data regarding volume of expected use and future cash projections, are satisfied regarding the secure nature of Concession Agreement/License, the expected source of repayment and the overall collateral arrangements.

G.2.2 Security Package

In order to observe prudence, while undertaking 'limited recourse financing' for the infrastructure projects, banks/DFIs shall secure their interest by Primary Security/Collateral, besides either one or a combination of the Secondary Securities/Collateral, the details of which are as under:

G.2.2.1 Primary Security/Collateral: First charge on all the receivables and Project Account(s), Project Collection Account, Project Debt Reserve Account, Project Escrow Account and Bank Accounts maintained by the Project Company and accounts of the contractors.

G.2.2.2 Secondary Securities/Collateral:

a. First mortgage over all the immovable and movable assets of the project company and that of the contractors;
b. First assignment of all insurance policies to cover major and minor risks including political and force-majure;
c. First pledge of sponsor's share in the company, besides ensuring that sponsor's holding does not fall below 51% of equity capital without prior approval of the lender(s);
d. First assignment by way of security of all government approvals and agreements, the implementation agreement and the government undertaking;
e. First assignment by way of security of the company's rights under project agreements such as project funds agreements, retention account agreement, and shareholder agreement;
f. First charge/assignment of corporate/bank guarantees furnished by the contractors to the project company for claiming liquated damages.

G.3 REGULATORY COMPLIANCE

In order to facilitate participation of private sector in infrastructure projects, which are capital intensive and require heavy capital outlay, banks/DFIs are advised to adhere to the following regulatory measures (however, those regulatory matters that are not covered in these guidelines will continue to be governed by the Prudential Regulations for Corporate/Commercial Banking)

G.3.1 EXPOSURE LIMIT

G.3.1.1 Per Party Exposure Limit

a. The exposure to a single borrower for IPF will not exceed 30 per cent of bank's/DFI's equity, with maximum limit on funded facilities up to 20 per cent of bank's/DFI's equity (as disclosed in the latest audited financial statements).

b. Exposure to any group in various infrastructure projects should not exceed 50 per cent of bank's/DFI's equity, with maximum limit on funded facilities up to 35 per cent of bank's/DFI's equity.

G.3.1.2 Total Exposure to IPF

Banks/DFIs shall ensure that at no time their total exposure to IPF exceed their equity.

For the purpose of Regulation G.3.1, exposure shall be calculated in the manner as described in Regulation R-1 of Prudential Regulations for Corporate/Commercial Banking **(Annex B)**.

G 3.2 DEBT-EQUITY

Banks/DFIs while taking any exposure on an infrastructure project, shall ensure that the total exposure (fund-based and non-fund based) availed by any borrower from financial institutions does not exceed 10 times of borrower's equity as disclosed in its latest audited financial statements. However, Banks/DFIs shall themselves decide the respective share of fund based and non-fund based lending in the total exposure to an infrastructure project. Moreover, subordinated loans shall be counted as equity of the

borrower and Banks/DFIs should specifically include the condition of subordinated loan in their Offer Letter. The subordination agreement to be signed by the provider of the subordinated loan, should confirm that the repayment of subordinated loan will require prior approval of bank(s)/DFI(s).

However, banks/DFIs while making the exposure decision are advised to ensure substantial financial commitment by main sponsors, which can help in the success of the project, in the following ways:

a. making it expensive for the sponsors to abandon the project, thus encouraging them to take a strong and lasting interest in the project and to seek to remedy difficulties that may arise;
b. expediting decision making, particularly where the sponsors holds a majority share; and
c. increasing the confidence of other parties in the project.

G.3.3 FUNDING OF INFRASTRUCTURE PROJECTS

G.3.3.1 Maximum Duration of Loan: Banks/DFIs are free to extend loans for IPF upto a maximum period of 20 years.

G.3.3.2 Asset Liability Management: Banks/DFIs are encouraged to develop in-house system for prudently managing interest rate risk and liquidity risk due to adverse movement in interest rates and maturity mismatches arising from locking their assets in long term IPF undertaking. Banks/DFIs may either enter into a *sell down* financing arrangement with other banks/DFIs or arrange consortium/syndicate to effectively match their assets and liabilities, wherein banks/DFIs financing the infrastructure projects may have an arrangement with other banks/DFIs of the consortium/syndicate for transferring to the latter the outstanding in their books on a predetermined basis.

G.3.3.3 Long Term Funding: As a measure of Asset Liability Management (ALM), banks/DFIs are also encouraged to float Infrastructure Bonds to match the tenure of infrastructure loans, besides churning their infrastructure loan portfolio through securitization/sell down. Banks/DFIs have already been allowed to securitised their assets pertaining to lease financing, mortgage financing and toll

road financing vide BPD Circular No. 31 of November 14, 2002. However, for the purpose of IPF the scope of Assets Securitization through Special Purpose Vehicle (SPV) laid down in the aforesaid BPD Circular has been extended to all types of Infrastructure Projects as defined at Clause 13, Part A, of these Guidelines. This would help banks/DFIs in originating IPF and afterwards securitising their IPF portfolio through SPV.

G.3. 4 PROVISIONING REQUIREMENTS

The banks/DFIs shall classify and make provisioning for IPF as per provision requirements illustrated at **Annex C.**

ANNEX A

IPF: CHECKLIST FOR MINIMUM INFORMATION REQUIREMENTS

1. PROJECT DESCRIPTION

i. Proposed ownership structure and sponsor information
ii. Legal status of project and status of government approvals (including government and/or local authorities attitude toward project, exemptions/advantages to be enjoyed by project, licenses, permissions required, proposed measures/actions that could affect the project).
iii. Project's anticipated economic contributions (e.g. in the generation of foreign exchange, employment, technology transfer)

2. CAPITAL INVESTMENT

i. Project site
   a. Legal agreements for land use rights
ii. Civil works and buildings
iii. Major and auxiliary equipment
iv. Project Management
v. Pre-operating requirements and costs
vi. Contingencies (physical) and escalations (financial)
vii. Initial working capital requirements
viii. Contracting and purchasing procedures to be used

3. PROJECT SCHEDULES

i. Construction, startup, operations
ii. Expenditures
iii. Funding (including timing of funds needed during project implementation)
iv. Regulatory compliance

4. ENVIRONMENT IMPACT

i. Description of environment impact
ii. Health and safety issues

5. FINANCING

i. Total cost of project (including details on major items of fixed assets and working capital)
ii. Background statement on all sponsors and participants, showing their financial or other interest in the project in construction, in operations, and in marketing
iii. Capital structure
   a. Proposed debt/equity structure
   b. Equity
      - Shareholder structure
      - Long term plans (stay private/go public)
      - Quasi-equity (subordinated debt)

c. Debt
    - Long-term debt/working capital
    - Domestic/foreign
    - Desired terms and conditions
    - Funding sources already identified

d. Overrun/standby arrangements

iv. Financial Projections

a. Projected financial statements including cash flows
b. Clear statement of all assumptions
c. Sensitivity analyses under different scenarios like interest rate risk etc

6. LEGAL DOCUMENTATION

i. Joint venture agreements (if applicable)
ii. Articles of association
iii. Government approval documents/concession/business license
iv. Land certificate/red line map
v. Mortgages, if any
vi. Loan agreements
vii. Major contracts including

a. Off-take agreements
b. Supply agreements
c. Technical assistance agreement
d. Management agreement

ANNEX B

GUIDELINES REGARDING LIMIT ON EXPOSURE TO A SINGLE PERSON UNDER REGULATION R-1

In arriving at exposure under Regulation R-1:

A) 100% of the deposits placed with lending bank / DFI, under perfected lien and in the same currency, as that of the loan, shall be excluded.

B) 90% of the following shall be deducted;

i. deposits placed with the lending bank/DFI, under perfected lien, in a currency other than that of the loan;
ii. deposits with another bank/DFI under perfected lien;
iii. encashment value of Federal Investment Bonds, Pakistan Investment Bonds, Treasury Bills and National Saving Scheme securities, lodged by the borrower as collateral; and
iv. Pak. Rupee equivalent of face value of Special US Dollar Bonds converted at inter-bank rate, lodged by the borrower as collateral.

C) 85% of the unconditional financial guarantees accepted as collateral and payable on demand by banks/DFIs, rated at least 'A' or equivalent by a credit rating agency on the approved panel of State Bank of Pakistan, Standard & Poors, Moody or Fitch Ibca, shall be deducted. Similar weightage to guarantees issued by the International Finance Corporation (IFC), Commonwealth Development Corporation (CDC) Deutsche Investions and ntwicklungsgesellschaft nbH (DEG), Netherland Financierings Maatschappijvoor Ontwikklelingslanden N.V (FMO) and Asian Development Bank (ADB) shall also apply.

D) 50% of listed Term Finance Certificates held as security with duly marked lien shall be deducted. The TFCs to qualify for this purpose should have been rated at least 'A' or equivalent by a credit rating agency on the approved panel of State Bank of Pakistan.

E) Weightage of 50% shall be given to;

i. documentary credits opened by banks / DFIs;
ii. guarantees / bonds other than financial guarantees;
iii. underwriting commitments.

F) The following different weightages will be applicable to exposure taken against commercial banks / DFIs in respect of placements;

i. 10% weightage on exposure to banks / DFIs with 'AAA' rating.
ii. 25% weightage on exposure to banks / DFIs rated 'A' and above.
iii. 50% weightage on exposure to banks / DFIs rated 'BBB' and above.

The banks / DFIs shall, however, ensure that the overall limit for each financial institution in respect of inter-bank placements is invariably approved by their Board of Directors.

2. For the purpose of this regulation, exposure shall not include the following:

i. Loans and advances (including bills purchased and discounted) given to the Federal Government or any of their agencies under the commodity operations programme of the Federal Government, or guaranteed by the Federal Government.
ii. Obligations under letters of credit and letters of guarantee to the extent of cash margin held by the bank / DFI.
iii. Letters of credit, which do not create any obligation on the part of the bank / DFI (no liability L/C) to make payments on account of imports.
iv. Letters of credit opened on behalf of Federal Government where payment is guaranteed by State Bank of Pakistan / Federal Government.
v. Facilities provided to commercial banks / DFIs through REPO transactions with underlying SLR eligible securities.
vi. Pre-shipment / post-shipment credit provided to finance exports of goods covered by letter of credit/firm contracts including financing provided from the bank's / DFI's own resources.
vii. Letters of credit established for the import of plant and machinery.

ANNEX C

PROVISION REQUIREMENTS FOR IPF

Classification	Determinant	Treatment of Income	Provisions to be made
OAEM	Where the amount recovered is less than 75% of the amount receivable and it has become overdue by more than 180 days.	Unrealized mark-up / interest to be put in Suspense Account and not to be credited to Income Account except when realized in cash	No provisioning is required.
Substandard	Where the amount recovered is less than 60% of the amount receivable and it has become overdue by more than one years.	As above	Provision of 20% of the difference resulting from the outstanding balance of principal less the realizable value of liquid assets
Doubtful	Where the amount recovered is less than 40% of the amount receivable and it has become overdue by more than 2 years.	As above	Provision of 50% of the difference resulting from the outstanding balance of principal less the realizable value of liquid assets
Loss	Where the amount recovered is less than 20% of the amount receivable and it has become overdue by more than 3 years.	As above	Provision of 100% of the difference resulting from the outstanding balance of principal less the realizable value of liquid assets