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Contents

SZA Schilling, Zutt & Anschütz advises domestic and international clients in all areas of corporate and commercial law, with currently around 100 attorneys. Over the last few years, the firm's clients have included 14 of the 30 enterprises listed on the DAX. The firm is legal counsel for leading industrial and trade enterprises, banks, insurance companies and financial services providers as well as large family-owned businesses and wealthy private clients. The firm has offices in Frankfurt am Main, Mannheim, Munich and Brussels, the finance department is based in Frankfurt am Main and currently consists of three partners, one counsel and five associates. In addition to issues dealing with general finance, project finance, bank and bank supervisory law, the firm advises clients in all matters concerning financing transactions such as the (tax-optimised) structuring of financing and financing instruments, including corresponding capital market products. The SZA finance team covers a broad array of projects, domestically as well as cross-border, where it advises lenders, borrowers or sponsors on project finance transactions.

Authors

Dietrich F. R. Stiller advises clients in the areas of banking and capital markets law, privatisations and cross-border investments. In particular he specialises in lending transactions including corporate finance, national and international project finance, BOT structures as well as in export finance and refinancing of distressed enterprises, together with regulatory law. A partner at SZA, Dietrich advises enterprises, sponsors, project companies and banks in a wide range of finance transactions, many of which are transnational and involve ECA or other guarantees. He is the SZA representative to IPFA and the LMA and has published widely on project finance.

Andreas Herr is a counsel at SZA. Prior to joining Andreas worked for several years in the Frankfurt am Main and London offices of a leading German law firm as well as for an investment bank in London. He advises German and international clients in the areas of corporate law, M&A, banking & finance and capital markets law. A focus of his practice is advice to borrowers and lenders in various kinds of debt financings, including project and acquisition finance, financing of real estate transactions as well as restructuring. He also has experience advising on questions of regulatory law, in particular under the German Banking Act (KWG) and the German Capital Investment Code (KAGB).

Michael Maxim Cohen is an associate at SZA who advises German and international clients in the areas of M&A, corporate law, capital markets law and banking & finance, including project finance, acquisition finance, financing of real estate transactions as well as restructuring. Prior to joining SZA Schilling, Zutt & Anschütz Michael worked in the Frankfurt am Main office of a leading London based international law firm.

1. Project Finance Panorama

1.1 Recent Trends and Development

Project finance represents an important sector of the German finance market, not only for domestic projects and transactions but also for cross-border transactions which either physically cross the German border or which are located outside of Germany but contain a German element. Among those projects, which are located within the German territory or the German exclusive economic zone (EEZ), renewable energy projects (including on-shore and off-shore wind farms and photovoltaic energy) and federal highway financing play a predominant role.

Furthermore, the financing of international joint ventures within Germany may take the form of project finance if the sponsors aim to keep the financing off-balance-sheet. This applies accordingly to infrastructure projects that involve the territory of multiple jurisdictions, EEZs and the high seas (ie, international waters). One representative example is the financing of the NordStream 1 pipeline between Vyborg and Greifswald.

Another important type of project where project finance becomes the preferred finance option are cross-border projects, either in the private sector or in the form of public-private partnerships (PPPs), where the project may be physically located in any part of the world but involves strong German elements such as German sponsors, German exports or German lenders taking a leading position.

In the case of large-scale projects project finance may be combined with export finance, untied loans (*ungebundene Finanzkredite;* UFKs) or finance schemes eligible for other forms of government support such as, but not limited to, investment guarantees for equity-like loans.

Except for purely domestic projects, all of these transactions usually involve the laws of many different jurisdictions. Depending on the composition of the sponsors group and the syndicate of lenders, German law and English law represent the most common choices for the governing law of the facility agreement, while the governing law of security agreements is heavily dependent on the type and location of the relevant security.

Although the share of project finance transactions in the German domestic market is limited, project finance remains as an indispensable option for eligible projects. In particular the contemplated phase-out of nuclear power plants keeps the demand for renewable energy projects at a high level. In addition, the financing of large real estate projects, which can be perceived as a special type of project finance, real estate finance, remains very active in view of the continuing construction activities in the real estate market.

However, the limited number of transactions in this area of finance leads to a concentration of the relevant market on a number of specialised key players, bearing in mind that project finance is complex and not every institution can afford the costs of building up and maintaining the required in-house expertise. Furthermore, low interest rates and redundant liquidity in the market continue to affect the demand for project finance, and existing sanctions as well as sanctions threats have an impact on the project finance market for sponsors, exporters and lenders.

As project finance, because of its complexity, involves higher transaction costs than other forms of finance, it remains predominantly a form of finance for large-scale and megaprojects, but is not necessarily suitable for smaller transactions. In this context, project finance plays a particularly strong role during the structuring and construction phase of projects as well as during the first years of the operation phase of complex projects. After a project has been successfully implemented, and has proven its sustainability during the initial part of the operation phase, the sponsors may consider refinancing the then-existing project finance, wholly or in part, through project bonds or other less complex forms of finance that reflect the different risk profile of an ongoing successful project. For this reason many project finance arrangements are repaid before their final maturity date.

Project finance will hence continue to play a key role for complex large-scale and megaprojects, while the statistics will remain volatile because – due to the number of transactions and the volume of individual megadeals – single transactions or a change of their timing tend to have a tangible impact on the relevant figures.

1.2 Sponsors and Lenders

Medium-sized projects usually involve one sponsor or a small group of sponsors including at least one knowledge investor from the relevant industry area. This key sponsor may form a syndicate with other sponsors, which are equally involved in the implementation of the project, such as the engineering, procurement and construction (EPC) contractor or other parties. In the case of large and megaprojects the sponsors group normally consists of a group of joint venture partners originating from the relevant industry, but including also finance investors such as equity or pension funds. In this context the risk profile, as reflected in sponsors undertakings such as the commitment to provide additional equity or mandatory holding periods agreed with the lenders, may also have an impact on the eligibility of the project for pure finance investors. In general, it can be observed that the participation of finance investors tends to increase once a project successfully enters the operation phase.

In medium-sized transactions, projects are often financed by one single German financial institution as lender, but for large transactions and mega-transactions it is usually a syn-

dicate of lenders that provides the senior lending. In cases of complex megadeals it is also common to have different facilities such as an export credit agency (ECA) facility, an untied loan facility and a commercial facility, each of which is granted by different syndicates and interlinked by means of an intercreditor agreement. Here, one of a number of German financial institutions with experience in the area of project finance frequently takes the lead as arranger or agent, but there is also a considerable number of foreign banks with a strong presence in Germany, that are equally active and successful in project finance in Germany. In particular, the role of the agent for facilities covered by guarantees issued by the German government (export guarantees, untied loans or investment guarantees for equity-like loans) is normally taken by German financial institutions or experienced foreign banks with a strong presence in Germany.

In the case of development projects abroad with a strong German element, German development finance institutions, sometimes in a syndicate with foreign development finance institutions, play a leading role.

1.3 Public-Private Partnership Transactions

According to data published by the European Investment Bank (EIB), in Europe, financing agreements for 39 PPP projects totalling EUR14.6 billion were concluded in 2018 (EUR15.2 billion in 2017). Of the transactions closed in 2018, 51% were government-pay PPPs. 21 of the 39 completed PPP transactions were funded by institutional investors (insurance companies, pension funds, etc), compared to 13 out of 44 projects in the previous year. As a whole, the number of projects in 2018 declined by 11% compared to the previous year making it the lowest number of transactions since 1997. The market volume of PPP projects also decreased, only by 4% compared to 2017, however. Further, the average transaction size increased to EUR375 million compared to EUR345 million in 2017. Within Europe, Germany ranked sixth (together with Belgium, Ireland, Austria and Spain) in terms of the number of transactions that reached financial close, and it ranked fourth in terms of aggregate projects value.

While Turkey was the largest PPP market in terms of value, the largest number of transactions were closed in France. In Europe, the transport sector remained the largest in value terms with over EUR7 billion worth of transactions (EUR7.6 billion in 2017). However, only seven transactions were closed in the transport sector in 2018, the lowest number in the last 20 years.

The EU, national governments and public financial institutions (both domestic and supranational) continued to play a significant role with regard to financing in 2018. The A355 Strasbourg West bypass (France), the A10/A24 Neuruppin-Pankow motorway (Germany), the Afsluitdijk dam and the Blankenburg tunnel (Netherlands) all benefitted from the support of the European Fund for Strategic Investments (EFSI). Four of the 39 PPP projects that reached financial close during the year were financed by the EIB, reaching an aggregate lending volume of EUR1 billion.

With regard to the 2018 PPP projects in Germany, the transport sector dominated, followed by construction related to health care and education.

With regard to transportation infrastructure, the motorway BAB A10/24 project in Brandenburg between Neuruppin and Pankow with BAM and HABAU as sponsors was closed on 15 February 2018 – a EUR650 million project with a term of 30 years. The project debt is financed via long-term bonds, a structured finance facility provided by the EIB and short-term loans provided by BayernLB, DekaBank, DZ Bank, Rabobank and Tecta.

Other motorway PPP projects presently in a tendering procedure include the motorway BAB A3 project between interchange Biebelried and interchange Fürth/Erlangen, motorway BAB A49 between interchange Fritzlar and merging point Ohmtal, as well as two smaller projects on federal highway B247. In addition, at least seven further motorway expansion projects are presently in the project pipeline.

With regard to health-care-related PPP projects, the University Hospital Schleswig-Holstein, the Particle Therapy Centre Kiel, the Hochtaunus-Kliniken (hospitals) and the West German Proton Therapy Centre in Essen represent landmark projects of a considerable size. The Proton Therapy Centre in Essen underwent a successful financial restructuring a few years ago. In addition, many smaller projects have been implemented or are in the pipeline.

There are a large number of PPPs in the education sector with Berufliche Schulen Hamburg (vocational schools of the city of Hamburg), the fourth PPP package of schools in the city of Cologne, two schools PPPs of the city of Offenbach, a school PPP of the city of Frankfurt am Main, schools and day-care centres in Braunschweig (EUR70 million), schools in Nuremberg (EUR65 million) and Duisburg (EUR74 million) as outstanding landmark projects (cf, the project data bank published by Partnerschaft Deutschland).

Germany has no PPP law or concessions law of general application, for which reason PPP projects are usually subject to general public procurement law, budget law, competition law, rules and regulations governing state subsidies and general contract law.

Important sectoral legislation includes the Hospital Finance Act (*Krankenhausfinanzierungsgesetz*), the Energy Industry Act (*Energiewirtschaftsgesetz*), the Act for the Promotion of Renewable Energies (*Gesetz zur Förderung Erneuerbarer Energien*), the Act for the Development and Promotion of

Offshore Wind Energy (*Gesetz zur Entwicklung und Förderung der Windenergie auf See*) and the Federal Act Governing the Construction and Finance of Federal Highways through Private Entities (*Fernstraßenbauprivatfinanzierungsgesetz; FStrPrivFinG*). However, it should be noted that recent motorway projects do not include a toll component and hence were structured under the general legislation.

Other legislation of general application includes the Act against Restraints in Competition (*Gesetz gegen Wettbewerbsbeschränkungen*), the Regulation on the Award of Public Contracts (*Vergabeverordnung*), the Procurement Regulation for Public Works (*Vergabe- und Vertragsordnung für Bauleistungen*; VOB/A), the Procurement Regulation for Public Supplies and Services (*Vergabe- und Vertragsordnung für Leistungen*; VOL/A), the Procurement Regulation for Professional Services (*Vergabeordnung für freiberufliche Dienstleistungen*; VOF) or Article 106 of the Treaty on the Functioning of the European Union, together with other national and EU regulations regarding procurement, and the Capital Requirements Regulation (CRR).

1.4 Structuring the Deal

Project companies in Germany will normally take the form of a special purpose vehicle (SPV). This special purpose vehicle is usually organised as a limited liability company (GmbH) or as a limited partnership with a limited liability company acting as general partner (GmbH & Co KG). Limited liability companies are particularly suited to SPVs as this legal form allows a limitation of liability and, at the same time, enables its shareholder(s) – ie, the sponsor(s) – to issue binding instructions to the management. Further details of the structure will normally depend on the question of whether there is only one single sponsor and shareholder, or whether there is a group of sponsors and shareholders that uses the SPV as an incorporated joint venture company (JVC). In the case of multiple sponsors the articles of association of the SPV, which are publicly available, will normally be short and concise and focus only on those issues which under applicable law must be regulated by the articles themselves, while all other issues relating to the relationship between the sponsors/shareholders and between the shareholders and the SPV, according to common practice, will be regulated in a separate shareholders' agreement, which is not open to the public.

This does not mean that other legal forms are not available, but other legal forms are quite unusual for project finance because they either give rise to a direct liability for the sponsors, which is in conflict with the concept of limited or non-recourse finance, or they grant, from a sponsors' view, too much independence to the management of the SPV. In exceptional cases, in particular where multi-layered structures are involved, more complex structures may be chosen where such structures normally also provide for a limitation of liability. In cases where structures involve multiple sponsors, those sponsors may, in exceptional cases, prefer to have independent management of the SPV and consequently opt for the legal form of a stock corporation.

In addition, tax considerations also play an important role for the details of the ultimate structure.

In cases of cross-border projects, the relevant project SPV may also be domiciled in other jurisdictions. By way of example, the relevant project company for the NordStream pipeline is domiciled in Switzerland. Other cross-border projects where the physical project is located outside Germany, will have a legal structure determined in accordance with the legal requirements of the host state of the investment and will normally, but not necessarily, involve a local SPV. In addition, tax considerations as well as investment protection issues (eg, the existence or absence of a bilateral investment treaty) may have an important impact on the structuring of the project. While tax considerations may, in particular cases, support holding structures, most bilateral investment treaties protect only direct investments, with limited exceptions.

Furthermore, in the case of cross-border projects involving ECAs or multilateral lenders, the requirements of those ECAs or lenders may also have an impact on the final project structure.

Another important consideration for the structuring of the project is the question of whether the project SPV is going to operate the project by itself, or whether operation shall be contracted out to a separate operation SPV and, in the latter case, whether that operation SPV is fully controlled by the project SPV or whether this must be an independent third party, either because the project per se does not include operation or because public procurement laws, competition law or other legal requirements dictate a separation of the operator function.

2. Guarantees and Security

2.1 Assets Available as Collateral to Lenders

The security package in project finance transactions is typically based on ring-fencing. This concept serves not only the purpose of creating a comprehensive security package but also prevents third parties from acquiring prior-ranking security rights. Project finance borrowers are mostly organised as SPVs. In the event that these SPVs have any subsidiaries, those subsidiaries are usually included into the ring-fencing.

Most project finance arrangements are based on limited recourse or (less frequently) non-recourse concepts. In the case of limited recourse, security and/or quasi-security granted by the sponsors is frequently limited to the construc-

tion period and sometimes the first year(s) of the start-up period and may take many forms from hard guarantees on first demand to comfort letters or restrictions on the repayment of structurally subordinated funds like shareholder loans or mezzanine capital.

Typical collateral in a project finance transaction includes a pledge of shares in the project company, a pledge of project accounts as well as a pledge or, more commonly, security assignment of receivables under contracts which relate to the project (eg, engineering, construction, operation, maintenance and insurance contracts). Further, ownership of movable assets such as machinery will usually be transferred as security. If the project company owns real estate on which the project is being built or operated, that real estate will typically be encumbered by a land charge. Finally, the security package will often include corporate or bank guarantees to secure, for example, equity-contribution commitments or to mitigate the risk of cost overrun or payment delays. Completion guarantees with regard to the finalisation of the project are also a common means of security.

A pledge of shares in a GmbH requires notarisation under German law. A land charge over real estate has to be granted in notarial form and registered in the land register in order to become valid. For all other security mentioned above, no specific form requirements apply. However, written form is standardly used. A pledge of accounts (or other receivables) needs to be notified to the third-party debtor (in the case of an account, the account-holding bank). This notification is a validity requirement. In contrast, in the case of a security assignment the obligor generally does not need to be notified to create a valid assignment.

Furthermore, particularly in the case of large projects or megaprojects, it is not uncommon that the overall finance structure includes one or more facilities that are supported by government guarantees. These may be export credit guarantees issued by one or more ECAs, or (in the case of Germany) untied loan guarantees or investment guarantees for so-called equity-like loans. Less common in the German environment, but not insignificant, is private risk insurance. In addition, the lenders might take security over investment guarantees issued to the sponsors.

2.2 Charges or Interest over All Present and Future Assets of a Company

German law does not recognise the concept of floating charges. However, it is generally possible to also extend security interests to future-acquired assets. In this context, it is important that the asset to be encumbered or transferred for security purposes (eg, a future claim or revolving inventory) can be identified at the time of the conclusion of the security agreement in a manner that ensures its determinability when acquired.

2.3 Registering Collateral Security Interests

For the registration of a land charge in the land register, a registration fee has to be paid. The amount of the fee depends on the amount of the land charge to be created. Moreover, where notarisation is required in order to create security – eg, a pledge of shares in a GmbH or creation of a land charge – notary fees are incurred. The amount of the notary fees depends on the value of the encumbered assets and is calculated according to a statutory fee schedule. Under German tax law there are no stamp duties.

2.4 Granting a Valid Security Interest

German law generally requires that each item of collateral is individually identified in the security document or that it is, at least, identifiable, in order to grant a valid security interest in that item. A general description of the types of collateral covered is generally not sufficient. This requirement results from the so-called "in rem principle of legal certainty" (*sachenrechtlicher Bestimmheitesgrundsatz*). Hence, any general description used, needs to be of a nature that ensures individual identifiability.

The precise and identifiable description of the assets is, in particular, a challenge in connection with the security transfer of inventory. In these cases, the agreement will frequently be either all-inclusive, refer to a certain area on the business premises and state that title to all assets located therein will be transferred, or list individual inventory in an explicit way.

2.5 Restrictions on the Grant of Security or Guarantees

Capital maintenance rules may limit a company's ability to grant security or guarantees. In the case of a limited liability company, no assets may be paid out to shareholders that are required for the maintenance of the statutory share capital. In the case of a stock corporation, any repayment of shareholders' contributions is prohibited. These restrictions do not only apply to direct payments, but also to the grant of security or guarantees. Exemptions apply under domination and profit transfer agreements, if a valid reimbursement claim exists against the shareholder, or where a shareholder loan or comparable loan is repaid.

In the case of public entities acting as security grantors, the applicable restrictions under procurement law, budget law, and state subsidy law need to be strictly observed.

2.6 Absence of Other Liens

Only land charges and mortgages are registered in a public register (land register *(Grundbuch)*). A creditor who is able to explain a legitimate interest to the land register will be entitled to inspect the entries in the land register in order to verify if any liens with higher priority are registered. With regard to other liens, no registers or records are available. A creditor will usually demand respective guarantees from the debtor with regard to the ranking of its collateral. However,

the recovery achievable under such guarantees might be limited if the debtor is short of funds.

2.7 Releasing Forms of Security

German law differentiates between "accessory" security interests – sureties *(Bürgschaften)* or pledges – that depend on the existence of the underlying secured claim, and "non-accessory" security interests that may exist irrespective of a secured claim. Accessory security interests are automatically terminated/released by operation of law upon satisfaction of the secured claim. With regard to other security interests, a separate contractual release (eg, in the form of a reassignment of claims or retransfer of assets) is necessary. In the case of a land charge, a creditor's consent to the deletion thereof *(Löschungsbewilligung)* as well as deregistration from the land register are necessary.

3. Enforcement

3.1 Enforcement of Collateral by Secured Lender

Enforcement of collateral requires that the secured claim is unpaid despite being due. Pledged security is generally sold in a public auction, which is a formal proceeding and requires prior notification of the owner of the pledged security, at least one month before the public auction takes place. If the asset has a market price, pledged security can be enforced by way of a private sale at the choice of the pledgee. Banks prefer private sales as they usually lead to better results and are less formalistic.

Land charges and mortgages are enforced by way of a public auction *(Zwangsversteigerung)* or forced administration *(Zwangsverwaltung)* in formal proceedings organised and conducted by the court *(Vollstreckungsgericht)*. However, the parties may agree on alternative forms of enforcement (eg, private sale) in order to realise better results.

Assigned receivables against third parties are generally realised by collecting them from the debtor, which does not entail specific formalities.

The realisation of a guarantee depends on its agreed content. In the case of a guarantee on first demand (*auf erstes Anfordern*), the beneficiary may require payment from the guarantor – generally without having to demonstrate any further conditions for payment, but subject to possible ex post challenges and further subject to safeguards imposed by relevant jurisprudence to avoid abuse.

3.2 Foreign Law

According to paragraph 1 of Article 3 of Regulation (EC) No 593/2008 on the law applicable to contractual obligations (Rome I), which is applicable in Germany, a contract will be governed by the law chosen by the parties. A specific link to a foreign jurisdiction is generally not required in order for the choice of law to be valid. However, in cases where the only link to a foreign jurisdiction is the law chosen by the parties, mandatory provisions of the jurisdiction to which the case is linked will apply irrespective of the chosen law. Further, the application of provisions of the law chosen by the parties may be refused if such application is manifestly incompatible with the public policy (*ordre public*) in Germany. Finally, the freedom of choice of law may be limited with regard to collateral and the underlying agreements. For example, in rem security is mandatorily governed by the law of the location of the property (lex rei sitae). Apart from the aforementioned limitations, German courts will recognise foreign law chosen by the parties for the contract and enforce the respective provisions.

German law will also generally recognise the submission to a foreign jurisdiction (see Article 25 of Regulation (EU) No 1215/2012 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters).

3.3 Judgments of Foreign Courts

With regard to the courts of EU member states, the recognition of judgments is governed by Regulation (EU) No 1215/2012 on jurisdiction and recognition and enforcement of judgments in civil and commercial matters. According to Article 36 of this regulation, a judgment given in a member state will be recognised in the other member state without any special procedure being required. However, the party who wishes to invoke a judgment given in one member state in another member state needs to produce a copy of the judgment, which satisfies the conditions necessary to establish its authenticity as well as a certificate to be issued pursuant to Article 53 of the regulation containing certain information with regard to the court proceedings. In addition, the court may require the party to provide a translation of the certificate or the judgment. On application of a party, the recognition of a judgment may be denied in certain cases – eg, in case of an evident breach of the German *ordre public* (see Article 45 of the regulation).

With regard to courts of a non-EU member state, the recognition of judgments would be governed by the provisions of the German Code of Civil Procedure (*Zivilprozessordnung*; ZPO). Such judgments will generally be recognised, subject to limited exceptions –eg, if the foreign judgment violates the German *ordre public* (see Section 328 of the ZPO) and further subject to international treaties which are in place with regard to certain matters or with specific countries.

According to Section 1061 of the ZPO, the recognition and enforcement of foreign arbitral awards in Germany is governed by the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards, dated 10 June 1958. On that basis, foreign arbitral awards will generally be recognised and enforced without re-examination of the

merits of the case. Certain exceptions apply, as set out in the New York Convention.

3.4 A Foreign Lender's Ability to Enforce

As set out in **3.2 Foreign Law**, provisions of the German *ordre public* might limit a foreign lender's ability to enforce its rights under a loan or security agreement in Germany. In addition, sanctions laws may have an impact on the enforcement of rights.

4. Foreign Investment

4.1 Restrictions on Foreign Lenders Granting Loans

Generally, there are no restrictions for foreign lenders with regard to the granting of loans. However, the extension of loans in a commercial manner, or to an extent requiring a commercial organised business, requires a German (or an EEA member state) banking licence according to the German Banking Act (*Kreditwesengesetz*, KWG). No distinction is made between foreign and domestic lenders, nor between banks and non-banks, if the loans are granted in Germany and in the aforementioned manner. Non-compliance with these licensing requirements is a criminal offence under German law and may, in addition, be sanctioned by fines. Furthermore, foreign equity investments may be subject to restrictions under the German Foreign Trade and Payments Ordinance (*Außenwirtschaftsverordnung*, AWV), depending on the target company's field of activities.

4.2 Restrictions on the Granting of Security or Guarantees to Foreign Lenders

Generally, there are no restrictions regarding the granting of security or guarantees to foreign lenders. However, the requirement for a banking licence under the German Banking Act, set out above in **4.1 Restrictions on Foreign Lenders Granting Loans**, applies in the same way to the assumption of guarantees if this is done in a commercial manner or to an extent requiring a commercially organised business.

Furthermore, sanctions laws may restrict transactions with certain foreign lenders.

4.3 Foreign Investment Regime

Pursuant to the German Foreign Trade and Payments Act (*Außenwirtschaftsgesetz*, AWG) and the German Foreign Trade and Payments Ordinance (*Außenwirtschaftsverordnung*, AWV), foreign acquisitions of a controlling share (ie, 25% or more) of the voting rights in a German company may be examined and prohibited by the competent German authorities – the Federal Ministry of Economic Affairs and Energy (*Bundesministerium für Wirtschaft und Energie*, BMWi). The option to examine and prohibit certain acquisitions is not limited to specific sectors. The individual transaction must not negatively affect the public policy or the public security of the Federal Republic of Germany. Therefore, in order to guarantee transaction security, it is not uncommon for foreign investors to apply for and obtain a clearance certificate *(Unbedenklichkeitsbescheinigung*) from the BMWi with regard to AWG and AWV prior to the closing of the envisaged acquisition.

4.4 Restrictions on Payments Abroad or Repatriation of Capital

Generally, there are no restrictions on payments abroad or repatriation of capital by foreign investors. However, certain cross-border transfers of funds must be notified under the AWV. Furthermore, sanctions to the extent recognised by, and applicable in, Germany may apply to some payments, cross-border or domestic.

4.5 Offshore Foreign Currency Accounts

While it is permissible for a project company to maintain offshore foreign currency accounts, it is uncommon as the euro is an anchor currency and convertible in almost all jurisdictions, and offshore accounts are usually viewed with scepticism as they are often brought in connection with tax evasion practises.

5. Structuring and Documentation Considerations

5.1 Registering or Filing Financing of Project Agreements

In general, under German law, financing or project agreements do not need to be registered or filed with any government authority. However, depending on the type of the financing/security agreement, there are certain formal requirements to be observed. For example, a pledge of shares in a German limited liability company and the creation of a land charge or mortgage require notarisation. Security encumbering real property needs to be registered in the land register.

5.2 Licence Requirements

Ownership of land as such does not require a licence. However, certain activities typically connected with the ownership of land – e.g., activities in the area of property development – may require a licence under the German industrial code (*Gewerbeordnung*). Foreign entities may operate in Germany, either directly or by establishing a subsidiary or a branch, and hold a respective licence. The exploitation of certain natural resources may also require a licence. Thus, the exploitation of minerals, for example, requires a government licence under the Federal Mining Act (*Bundesberggesetz*). The same applies to cables and pipelines on the continental shelf. The right to exploit natural resources is not necessarily tied to title in land and depends on the nature of the relevant resource. Foreign entities may hold exploitation licences even if they are not owner of the relevant land.

5.3 Agent and Trust Concepts

Agent concepts are recognised in Germany. It is common practice that an entity acting as security agent holds security on behalf of the whole group of lenders participating in the financing.

In case of accessory security which is legally inseparable from the secured claim (eg, a pledge), parallel debt structures are frequently used in order to facilitate the transferability of the security and to enable changes in the consortium of lenders/security holders. In such case, in addition to the secured claim, a second claim is created as abstract acknowledgment of debt entitling the security agent to an amount corresponding to the amount of the secured claim. The claim secured by the accessory security and the claim under the abstract acknowledgement of debt will only be fulfilled once –ie, if the secured claim has been fulfilled, the security agent may not realise its claim under the abstract acknowledgement of debt. German courts have not yet confirmed the validity of parallel debt structures, as these have never been questioned in court proceedings.

5.4 Competing Security Interests

The rules governing the priority of competing security interests depend on the type of security. The order of priority of security encumbering real property (eg, a land charge) is determined on the basis of the sequence of entries or, if the entries are made in different sections of the land register, the date of the entries. The parties are free to agree on a different ranking, however. This requires the consent of the person taking lower priority. In an insolvency of the security provider, the priority remains unaffected. Under certain conditions, the insolvency administrator may have a right to challenge the agreement regarding the priority.

The ranking of contractual security (eg, a pledge) depends on the date of the creation of the security. However, the parties may contractually agree to treat each other in a way deviating from the priority established by law.

Debtor and creditor may agree on the subordination of a creditor's claim for payment, which will then also be recognised in possible insolvency proceedings. This is frequently done with regard to claims for repayment of shareholder loans in order to avoid the over-indebtedness of the debtor, which would otherwise constitute a compelling reason for the opening of insolvency proceedings.

Furthermore, the allocation of proceeds from the realisation of security among different lenders' groups is frequently governed and modified by intercreditor agreements.

5.5 Local Law Requirements

German law does not require that the project company is organised under the laws of Germany. However, if a foreign company outside the European Union transfers its administrative office to Germany without transferring the registered seat, the company may face difficulties in being recognised as a foreign company in Germany.

The legal forms most commonly used in Germany are the limited liability company (*Gesellschaft mit beschränkter Haftung*, GmbH) and the limited partnership (*Kommanditgesellschaft*; KG). A limited partnership consists of at least one general partner which is personally liable for the company's debt and at least one limited partner. Due to such personal liability of the general partner, a GmbH is often used as general partner; such a KG would then be a "GmbH & Co KG".

The decision on the legal form of a project company depends on various factors, including the degree of influence shareholders wish to exercise over the management, the protection against liabilities incurred by the project company or tax-related issues.

6. Bankruptcy and Insolvency

6.1 Company Reorganisation Procedures

A company may be reorganised outside of insolvency proceedings or in the context of insolvency proceedings. Outside of insolvency proceedings, a company may be reorganised, for example, by selling it in an asset deal, share deal, or via instruments such as debt equity swaps. In the context of insolvency proceedings, the German Insolvency Code (Insolvenzordnung, InsO) provides for several options to reorganise a company.

There are different types of insolvency proceedings. In general, a distinction is made between insolvency proceedings taking place under the control of an insolvency administrator *(Fremdverwaltung)* and insolvency proceedings taking place under the debtor's own control *(Eigenverwaltung)*. The insolvency administrator is generally appointed by the insolvency court with the participation of the preliminary creditors' committee and – as the case may be – the creditors' meeting. However, the debtor may, under certain conditions, request that the insolvency proceedings take place under the debtor's own control, supervised by a trustee *(Sachwalter)*. This may also apply during the opening proceedings. Insolvency proceedings under the debtor's own control are often advantageous for the debtor as the existing management can continue the business as conducted before, which often results in time and cost savings.

Additionally, so-called "protection proceedings" *Schutzschirmverfahren*) are available to a debtor who is over-indebted *(überschuldet*) or imminently insolvent (*drohend zahlungsunfähig*), but still able to pay its current debt, if a financial recovery of the debtor is not obviously without a chance of success. In such a case, the debtor may apply for proceedings under its own control and may be granted a period of up to three

months for the preparation and submission of an insolvency plan. The insolvency court shall – upon the debtor's request – prohibit or provisionally stop individual enforcement measures against the debtor except for enforcement in immovable property and shall entitle the debtor to enter into obligations encumbering the insolvency estate *(Masseverbindlichkeiten*).

Irrespective of the type of insolvency proceedings, there are several options to restructure the insolvent company in the context of such proceedings. One commonly used option is a sale of the debtor's assets by way of an asset deal (*übertragende Sanierung*). Depending on the status of the insolvency proceedings, this may require the consent of certain parties involved – eg, the creditors' committee *(Gläubigerausschuss*). The creditors of the insolvent company participate in the proceeds resulting from such sale on a pro rata basis.

A further option – not only in the so-called "protection proceedings" – is the submission of an insolvency plan. Issues such as the satisfaction of the insolvency creditors, the distribution of the insolvency estate, the insolvency procedure and debtor's liability may be covered by an insolvency plan, in relation to which the InsO allows considerable flexibility. This gives the debtor the opportunity to achieve a kind of "settlement" with its creditors and other involved parties.

6.2 Impact of Insolvency Process

The lender's rights to enforce its loan, or any security or guarantee, may be affected by the commencement of insolvency proceedings over the assets of the borrower or security provider, as individual enforcement measures are prohibited after the opening of insolvency proceedings and the insolvency creditors have to file their claims with the insolvency administrator. However, certain creditors of the insolvent company may have the right to preferential treatment (*Absonderungsrecht*) – eg, creditors whose claims are secured by a pledge in the debtor's assets.

6.3 Priority of Creditors

Under German insolvency law, owners of certain assets have a right to segregation *(Aussonderungsrechte*) and may claim that their assets are not part of the insolvency estate. Secured creditors, such as pledgees or holders of a land charge, will be satisfied with priority *(Absonderung*). Only after satisfaction of the secured creditors, will the unsecured creditors be satisfied on a pro rata basis from the remaining assets. In addition, subordination agreements may lead to downward adjustments of creditors' rankings in the distribution waterfall. The debtor's shareholders will be satisfied last.

6.4 Risk Areas for Lenders

In an insolvency of the borrower, the borrower will most probably not be in a position to fully repay the loans to its lenders. The claims of insolvency creditors with no preferential rights will be satisfied on a pro rata basis from the insolvency estate and creditors will generally only be able to recover a small part of their receivables.

Further, under German law, an insolvency administrator may contest *(anfechten*) certain legal transactions made within certain time periods prior to (the filing for) the opening of the insolvency proceedings. Generally speaking, legal transactions which are detrimental to insolvency creditors may be contested – eg, transactions granting unjustified security or satisfaction to a certain creditor (and thereby harming other creditors) or transactions which are made with the intention to harm other insolvency creditors. The repayment of shareholder loans within the last year prior to the request for the opening of insolvency proceedings or thereafter may also be contested. The consequence of a contestation is that any assets transferred by the debtor in connection with the contested transaction must be returned by the creditor to the insolvency estate.

If security is granted by a third party and not the insolvent borrower, this security is – in general – not affected by the opening of insolvency proceedings over the assets of the borrower.

6.5 Entities Excluded from Bankruptcy Proceedings

In general, individuals and legal persons, but also entities without legal personality, may be subject to insolvency proceedings under German law. However, insolvency proceedings may not be opened over the assets of certain legal entities governed by public law (eg, the federal states and municipalities). Entities operating in certain economic sectors may be subject to specific provisions (eg, financial institutions).

7. Insurance

7.1 Restrictions, Controls, Fees and/or Taxes on Insurance Policies

Generally, there are no restrictions on insurance policies over project assets located in Germany. However, insurance companies require a licence issued by the German Federal Financial Supervisory Authority (*Bundesanstalt für Finanzdienstleistungsaufsicht*, BaFin) in order to offer insurance for projects located in Germany. This also applies to foreign (non-EU) insurance companies offering insurance in Germany. EU and EEA-based and licensed insurance companies do not require a separate German licence; they must undergo, however, a notification procedure with the BaFin in order to operate in Germany.

An Insurance Premium Tax of 19% applies to insurance premiums collected in Germany. This Insurance Premium Tax is also applicable if the insurer is located outside of Germany but within the EU or EEA and the insurance agreement con-

cerns, for example, immovable assets (especially buildings and plants) located in Germany, or is entered into with a client located in Germany. The same applies to an insurer who is located outside of the EU or EEA and has an insurance agreement with clients located in Germany. However, an agreement under which an insurer is only obliged to issue a guarantee or other security does not qualify as an insurance agreement and is therefore not subject to the Insurance Premium Tax.

For the avoidance of doubt, guarantees issued by the Federal Government of Germany covering exports, untied loans or investments do not qualify as insurance in terms of the Insurance Premium Tax Act or otherwise, although they are, in jargon or in English translations, sometimes referred to as "insurance".

7.2 Foreign Creditors

Generally, insurance policies over project assets are payable to foreign creditors. However, certain cross-border transfers of funds must be notified under the German Foreign Trade and Payments Ordinance (*Außenwirtschaftsverordnung,* AWV). Furthermore, sanctions to the extent recognised by, and applicable in, Germany may apply to some payments, cross-border or domestic.

8. Tax

8.1 Withholding Tax

Generally, there is no requirement under German tax law to deduct or withhold tax from payments of principal, interest payable on loans, or payments made out of the proceeds of a claim under a guarantee or of the enforcement of security, provided the loan has no profit-link feature and is not securitised as fungible debt instrument.

However, interest payments to a foreign lender may be considered German-sourced income, provided the loan is directly or indirectly secured by real estate located in Germany, comparable rights or ships registered in Germany. In such cases, the foreign lender might be under an obligation to file a tax return (at least, where an applicable double taxation agreement also permits Germany to tax such income) and German tax authorities have the discretion to require the obligor to withhold tax. The tax rate for a corporate taxpayer is 15.825%. Any tax withheld might be credited or refunded upon tax assessment on the foreign lender. Domestic lenders are subject to regular taxation.

8.2 Other Taxes, Duties, Charges

Except for (potential) income taxation (see **8.1 Withholding Tax**) there are no specific taxes, duties or other charges, which would apply to lenders making loans to entities incorporated in Germany. The granting of a loan is subject to VAT at a rate of 19%, but is generally, based on an optional exemption, exempt from VAT. Under German tax law there are no stamp duties. See **2.3 Registering Collateral Security Interests**, for information on notary and registration fees which may apply in connection with the creation of certain securities, pledges of shares and land charges for example.

8.3 Limits to the Amount of Interest Charged

Generally, parties to a loan agreement are free to agree on the amount of interest to be charged for the loan. However, interest payments in an amount or at a rate that would be considered as violating "good morals" are not recognised as valid in Germany according to general civil law principles. Furthermore, compound interest is not permitted under German law.

9. Applicable Law

9.1 Project Agreements

According to paragraph 1 of Article 3 of Regulation (EC) No 593/2008 on the law applicable to contractual obligations (Rome I), which is applicable in Germany, a contract will be governed by the law chosen by the parties. In the case of a project situated in Germany, the parties will generally choose German law as the law governing the project agreement. This might be different with regard to projects situated abroad or involving foreign parties.

9.2 Financing Agreements

See **9.1 Project Agreements**. If the financing is provided by German banks, the financing agreements will generally be governed by German law. International projects (eg, a banking consortium with a majority of non-German banks, foreign sponsors and/or a project situated abroad) often have financing agreements governed by English law.

9.3 Domestic Laws

Despite the choice of law made by the parties to an agreement, mandatory rules of the jurisdiction where a contractual obligation has to be performed will apply according to the Rome I regulation. Further, the security documentation regarding assets located in Germany has to be governed by German law (lex rei sitae). A pledge of shares will be governed by the law applicable to the articles of association of the respective company – ie, by German law in the case of a German limited liability company.

SZA Schilling, Zutt & Anschütz

Rechtsanwaltsgesellschaft mbH
Taunusanlage 1
D-60329 Frankfurt am Main
Germany

SZA
SCHILLING, ZUTT & ANSCHÜTZ

Tel: +49 69 9769601 160
Fax: +49 69 9769601 411
Email: dietrich.stiller@sza.de
Web: www.sza.de