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Application of the Concept of Project Finance in Iraq- A Comparative and Analytical Study

Faris K. Nesheiwat

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Cover Page Footnote

Ph.D. University of Durham, J.D. Seton Hall University School of Law. The author would like to thank Professor Bernard Freamon, Ms. Elizabeth Williams, Mr. Fabrizio Lelli and Mr. Ali Shaikley for their comments. Thanks also goes to the Editors and Staff of the Fordham Journal of Corporate & Financial Law for their efforts.



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APPLICATION OF THE CONCEPT OF PROJECT
FINANCE IN IRAQ – A COMPARATIVE
AND ANALYTICAL STUDY

Faris K. Nesheiwat

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*Faris K. Nesheiwat**

ABSTRACT

Many scholars and experts have addressed the issue of project finance, but one area that remains without detailed examination is its legal treatment under the legal systems of developing countries. The legal concepts applied under project finance are Western and are not necessarily identical to or compatible with legal concepts in Middle Eastern countries in general or Iraq in particular. In that sense, project finance is a transplanted legal concept when examined in the Middle Eastern legal framework. Although this Paper tackles the legal and strategic issues arising from the use of project finance in Iraq, its analysis and comparative approach is equally applicable to many other Middle Eastern countries whose legal systems are based on the civil code.

This Paper establishes priorities and examines the factors for completing a project finance in Iraq. It can be used as a “road map” in understanding those factors while, at the same time, it addresses the special needs and interests of the lenders (private banks and international lending agencies), the sponsors (private or governmental entities championing the project and creating a special purpose vehicle (“SPV”) acting as the borrower) and the Iraqi counterparts. It focuses on risk factors, permits and concessions, ownership structures, the taking of collateral, and dispute resolution. Further, this Paper seeks to explain the legal framework for these categories and enhance project finance parties’ capacity to provide management and oversight.

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INTRODUCTION

A common feature of project finance is the creation of an SPV by sponsors. The SPV is an incorporated entity, with no other or previous operations other than the business of the project. Its assets are comprised solely of the assets of the project itself, and absent other arrangements, recourse to those assets will represent to the lenders their final recourse option.

More specifically, project finance can take two forms, recourse and non-recourse.¹ Non-recourse project finance is a type of financing in

1. Scott Jazyanka, Presentation at the IP3 MENA, Amman, Jordan, "Introduction to Project Finance: Rationale, Structure and Financing Characteristics" (Feb. 26, 2007), available at http://www.escwa.un.org/divisions/ictd/events/2_5SJ_21Financeand

which the lender has no ability to make claims against the sponsor in excess of the value of the SPV collateral if such collateral is insufficient to repay the debt.² A recourse financing structure, on the other hand, gives the lenders the ability to make claims against the sponsor in excess of the SPV collateral, if such collateral is insufficient to repay the debt.³

In an underdeveloped market like Iraq,⁴ project finance agreements are sometimes called upon to play both a contractual and a regulatory role among the involved parties. One example arises in the area of power generation, where project finance augments the existing power generation grid, either through public or private models. Because the Iraqi market is lacking in competition regulation, project finance documents should attempt to fill in the gaps created by deficiencies in market regulation and competition law.⁵ For instance, such power generation schemes may include long-term contracts for the sale of the generated power to credit worthy purchasers. When such arrangements are used, they are secured via an off-take agreement that creates the type of long-term commitment needed by the power producer for the buyer to purchase the power produced at a set price.⁶ Similar utility for project finance can also be found in projects involving pipelines, storage facilities, refineries, waste disposal, water and telecommunications, just to name a few areas of application.⁷

Another point of interest in markets like Iraq is the enforceability of the project finance terms, which is predicated on the predictability of the legal, regulatory and political environment. Unstable markets are not

Investment.pdf.

2. See generally JEFFREY DELMON, PROJECT FINANCE, BOT PROJECTS AND RISK (Illustrated ed. 2005); Stewart E Rauner, *Project Finance: A Risk Spreading Approach to the Commercial Financing of Economic Development*, 24 HARV. INT'L L.J. 145 (1983).

3. *Id.*

4. Republic of Iraq Financial Sector Review, WORLD BANK.ORG, xv, [http://site/resources.worldbank.org/MENAEXT/Resources/Financial_Sector_Review_English_Summary.pdf](http://site.resources.worldbank.org/MENAEXT/Resources/Financial_Sector_Review_English_Summary.pdf).

5. Nagla Nassar, *Project Finance, Public Utilities, and Public Concerns: A Practitioner's Perspective*, 23 FORDHAM INT'L L.J. S60 (1999).

6. Rogerio De Miranda, *Offtake Agreements: Role, Features and Alternatives for Project Finance*, CAR CEPMLP ANNUAL REVIEW, 2001, art. 9.

7. *Id.*

good candidates for security and contractual enforcement, and therefore project finance documents must be specific in addressing potential regulatory and legal problems, as well as in allocating risk and responsibility.

I. RISKS

Even though project finance can cover areas with varying technologies, needs and circumstances, there are four distinct phases of risk common to all areas of project finance which can be discerned: development, construction, start-up and operation or commencement of the project.⁸

For each phase there are different parties to whom risk can be allocated and whose involvement can influence the outcome. Project sponsors represent the primary risk takers in the development phase, joined by the contractor and the lenders in the construction phase. This group is later potentially joined by suppliers and the providers of various guarantees in the start-up and the operation phase.⁹ Often the contractor's involvement in the funding risk ends with the conclusion of the construction phase.

For Iraqi projects, there are additional risks pertaining to regulatory, legal and cultural issues cutting through all four phases mentioned above. For starters, whereas the Iraqi legal system continues to be less developed than those in industrial countries, lenders who have to contemplate the enforcement of their rights face a higher level of uncertainty.¹⁰ In this respect, therefore, the impartiality of the judicial system and the enforceability of foreign judgments and arbitral awards are two major areas of concern. These considerations are of great importance even if the choice of law is not that of the local jurisdiction because local law must still be examined to determine if local courts will enforce the foreign choice of law.

Additionally, even if foreign law governs the project finance documents themselves, any agreements with local entities or the local

8. See *What is Project Finance*, EAGLETRADERS.COM, http://www.eagletraders.com/loans/loans_what_is_project_finance.htm; SCOTT L. HOFFMAN, *THE LAW AND BUSINESS OF INTERNATIONAL PROJECT FINANCE* (Cambridge Univ. Press 2008).

9. *What is Project Finance*, *supra* note 8; HOFFMAN, *supra* note 8.

10. See generally, Michael W. Gordon, *Of Aspirations and Operations: The Governance of Multinational Enterprises by Third World Nations*, 16 U. MIAMI INTER-AM. L. REV. 301-53 (1984).

government have a good chance of being governed by local law. Agreements with the host country can also give rise to the sticky issue of sovereign immunity, which can require the government's consent prior to any legal action or otherwise necessitate the waiver of such a doctrine if allowed under local law. It is also worth noting that the legal training of U.S. and U.K. attorneys is mostly based on common law, while that of Iraqi and other Middle Eastern practitioners is based on civil law. The concept of project finance itself originated outside the Middle East and, therefore, was framed by legal concepts that are not necessarily fully reflected or existent in Middle Eastern legal traditions; in that sense, project finance is a transplanted legal concept. These issues and differences impact the goals, expectations, risk allocation and predictability of the Iraqi legal system as a whole for project finance arrangements and has particular relevance with respect to the role of *stare decisis* and its applicability, which is often limited and inconsistent.¹¹ These issues make it that much more important for local counterparties to understand the roles of the foreign lenders and foreign investors.

A. RISK FACTORS

Overall, the following elements must be factored into the legal, political and economic stability analysis:¹²

1. **The degree of political stability.** Iraq has undergone a period of considerable turmoil over the past eight years, but has managed to navigate that period through the use of several political institutions that have become instrumental in keeping the political situation in check. The fact that various political factions participated in the electoral process, and thus have parliamentary representation, helps assure that political differences are resolved within the political process and not outside it.

11. Common law legal scholars view precedent as the main pillar of the concept of the Rule of Law. For a dated but passionate counter argument, see Robert L Henry, *Jurisprudence Constante and Stare Decisis Contrasted*, 11 A.B.A. J. 15 (1929).

12. HOFFMAN, *supra* note 8.

2. **Government attitudes towards foreign investment.** The Central Bank of Iraq (“CBI”) has responsibility over exchange rate policy.¹³ The Iraqi Dinar (“IQD”) is stabilized by the CBI against other currencies, especially the U.S. dollar, using monetary policy.¹⁴ It does this through a daily foreign currency auction that stabilizes the exchange rate and can also adjust it when needed.¹⁵ Further, there are no restrictions on the repatriation of foreign funds, and there is a clear taxation policy.¹⁶ The telecommunications sector is one area where private companies have been engaged in healthy competition, but it still needs more customer-oriented regulatory oversight.¹⁷ Various ministries control all the State Owned Enterprises (“SOEs”), with the cement sector seeing some movement towards privatization.¹⁸ The main obstacles towards the privatization of the majority of SOE’s have been concerns about employee lay-offs, legislative constraints and uncertainty about their actual worth.¹⁹ Moreover, there is an Investment Promotion Law, enacted in 2006, which granted tax and tariff incentives for investments that secured an investment license from the Federal or the provincial Investment Commissions.²⁰ Certain recent amendments to that law granted the right to acquire state land for housing

13. CENTRAL BANK OF IRAQ, <http://www.cbi.iq/index.php?pid=TheCbi> (last visited September 1, 2012).

14. United States of America Dep’t of Commerce, *Doing Business in Iraq: 2009 Country Commerical Guide for U.S. Companies*, U.S. COMMERCIAL SERVICE, http://www.buyusainfo.net/docs/x_3691804.pdf.

15. *Id.*

16. CENTRAL BANK OF IRAQ, *supra* note 13; *Investment Promotion Law, No. 13, 2006; Kurdish Investment Promotion Law, No. 4, 2006.*

17. Roger Field, *Mixed fortunes for Iraqi Telecoms*, ITP.NET (Apr. 8, 2011), <http://www.itp.net/584421-mixed-fortunes-for-iraqi-telecoms>.

18. Helen Power, *Iraq draws up plans for privatisation gold rush*, THE TELEGRAPH (U.K.), July 1, 2007, <http://www.telegraph.co.uk/finance/migrationtemp/2811359/Iraq-draws-up-plans-for-privatisation-gold-rush.html>.

19. The World Bank, *State Owned Enterprises Reform in Iraq* (Reconstructing Iraq, Working Paper No. 2, 2004).

20. *Investment Promotion Law, No. 13, 2006*, available at <http://www.investpromo.gov.iq/index.php?id=88>.

projects.²¹ The Kurdistan region has its own investment promotion law, with equally accommodating terms to those under the central government's 2006 law.²² The Iraqi government will need to continue to work on trade and investment reforms to maintain foreign interest in development and investment.²³ Kurdistan, which as a result of its more stable security situation, sees itself as one of the prime beneficiaries of foreign direct investments into Iraq must also work on several issues; security alone is not a good enough incentive if the procedures governing company registration, tax payment and collection, and legal tensions with the central government, to name but a few issues, are not clarified.

3. **The extent of the government's involvement in the country's economy.** Although Iraqi SOEs are not at the cutting edge of technology anymore, they remain a source for providing consumer goods and industrial products.²⁴ Numbering around 192 and grouped under 11 ministries they constitute a large portfolio.²⁵

In addition to the above, consideration must be given to the roles and responsibilities of the various governmental agencies.²⁶ Given the increased risks caused by the factors discussed above, non-recourse and limited recourse project finance become increasingly difficult in Iraq. Indeed, more attention must be given to risk allocation and risk management, even to areas considered standard such as force majeure.

21. *First Amendment to Investment Promotion Law, No. 2, 2010.*

22. *Kurdish Investment Promotion Law, No. 4, 2006, available at* <http://www.krg.org/articles/detail.asp?nr=107&lngnr=12&anr=12626&smap=04030000>.

23. U.S. DEPARTMENT OF STATE, *MEASURING STABILITY AND SECURITY IN IRAQ*, vii (2010).

24. *State Owned Enterprises Reform in Iraq, supra* note 19.

25. *Id.*

26. HOFFMAN, *supra* note 8.

B. FORCE MAJEURE

There is a tendency to incorporate boilerplate type force majeure language into contracts.²⁷ Such use must be avoided and instead careful consideration should be given to the use of force majeure language as a risk allocation tool.²⁸ It is safe to say, for example, that sand storms, labor strikes, work stoppage due to demonstrations and protests, and acts of terrorism are not unforeseeable in Iraq. Thus, one must consider if such occurrences should be included in a general force majeure definition or whether they should be dealt with in specific provisions. It is important to remember that force majeure clauses are intended to excuse a party only if the failure to perform could not be avoided by the exercise of due care by that party.²⁹

Whereas force majeure clauses often allow for time to cure before a force majeure event results in contract termination, consistency of force majeure clauses among various agreements and contracts is of critical importance. Such consistency can serve to balance the force majeure clauses in various contracts such that no party enjoys a wider possibility of being discharged from its obligations.³⁰ Relief granted under a contract must be carried through to all subsequently time-dependent agreements such as off-take and supply agreements; otherwise, inconsistencies will result in the possible termination of some related contracts.³¹ Moreover, the incorporation of a resurrection clause is especially useful in this context. Under a resurrection clause, force majeure inconsistencies are addressed thereby assuring that no contractor can receive relief that is greater than would otherwise be available under other relevant contracts.³²

27. *Force Majeure* literally means “greater force”. These clauses excuse a party from liability if some unforeseen event beyond the control of that party prevents it from performing its obligations under the contract. Typically, *force majeure* clauses cover natural disasters or other “Acts of God,” war, or the failure of third parties—such as suppliers and subcontractors—to perform their obligations to the contracting party.

28. Tomás Chevallier-Boutell, *Use of Force Majeure as a risk allocation mechanism in the context of international project finance*, CAR CEPMLP ANNUAL REVIEW, Apr. 21 2010.

29. Nassar, *supra* note 5, at S60; Delmon, *supra* note 2; GRAHAM D. VINTER & GARETH PRICE, *PROJECT FINANCE: A LEGAL GUIDE* (Sweet & Maxwell 2006).

30. Chevallier-Boutell, *supra* note 28, at 1 (“Force Majeure is now widely used as a risk allocation mechanism in project finance.”).

31. *Id.*

32. *Id.*

I. PERMITS & CONCESSIONS**A. REDUNDANCIES & JURISDICTION**

Obtaining necessary governmental permits for the construction and operation of a project is one of the most significant concerns for the project participants. Necessary permits are dependent on a variety of factors, chief among them the type and number of governmental agencies with jurisdiction over the project. In the case of Iraq, which is a nascent federal state, there are separate jurisdictional spheres for the provinces/regions and the central government.

The Iraqi constitution outlines the areas that are the exclusive province of the central government,³³ and the areas that are shared between the regions and the central government.³⁴ All powers not

33. Article 110 of the Iraqi constitution states that the federal government shall have exclusive authority in the following matters:

1. Formulating foreign policy and diplomatic representation; negotiating, signing, and ratifying international treaties and agreements; negotiating, signing and ratifying debt policies and formulating foreign sovereign economic and trade policy.
2. Formulating and executing national security policy, including establishing and managing armed forces to secure protection, guarantee the security of Iraq's borders and to defend Iraq.
3. Formulating fiscal and customs policy; issuing currency; regulating commercial policy across regional and governorate boundaries in Iraq; drawing up the national budget of the State; formulating monetary policy; and establishing and administering a central bank.
4. Regulating standards, weights and measures.
5. Regulating issues of citizenship, naturalization, residency and the right to apply for political asylum.
6. Regulating the policies of broadcast frequencies and mail.
7. Drawing up the general and investment budget bill.
8. Planning policies relating to water sources from outside Iraq and guaranteeing the rate of water flow to Iraq, as well as its just distribution inside Iraq in accordance with international laws and conventions.
9. General population statistics and census.

Iraqi Constitution, 2005, art. 110 (author translation).

34. Under Article 113, the following areas are shared between the regions and the central government: Antiquities, archeological sites, cultural buildings, manuscripts and coins shall be considered national treasures under the jurisdiction of the federal authorities, and shall be managed in cooperation with the regions and governorates, and this shall be regulated by law.

stipulated in the exclusive powers of the federal government belong to the regions and governorates.³⁵ With regard to powers shared between the federal government and a regional government, the law of the region(s) will have priority in the case of a dispute.³⁶

Further, under Article 121 of the constitution, the regions shall have the right to exercise executive, legislative, and judicial powers in accordance with the Constitution, except for those authorities stipulated in the exclusive authorities of the federal government (*i.e.*, Article 110).³⁷ And, in case of a contradiction between regional and national legislation regarding a matter outside the exclusive authorities of the federal government, the regional power has the right to amend the application of the national legislation within that region.³⁸

In practice, however, jurisdictions are not always well defined. This is not an issue that will be resolved soon, and duplicate work might be needed even where such redundancy is not called for under existing laws. Project managers, therefore, should be prepared to submit duplicate and redundant sets of documents; this is unavoidable until the legal landscape is improved. At the moment, a case in point is the need to re-register a company in the Kurdistan Region, even if the company was already registered with the Company Registrar in Baghdad at the Ministry of Trade. Legally speaking there should be no need to file for

Under Article 114, the following competencies shall be shared between the federal authorities and regional authorities:

To manage customs, in coordination with the governments of the regions and governorates that are not organized in a region, and a law shall regulate this.

1. To regulate the main sources of electric energy and its distribution.
2. To formulate environmental policy to ensure the protection of the environment from pollution and to preserve its cleanliness, in cooperation with the regions and governorates that are not organized in a region.
3. To formulate development and general planning policies.
4. To formulate public health policy, in cooperation with the regions and governorates that are not organized in a region.
5. To formulate the public educational and instructional policy, in consultation with the regions and governorates that are not organized in a region.
6. To formulate and regulate the internal water resources policy in a way that guarantees their just distribution, and a law shall regulate this.

Id. arts. 113-114 (author translation).

35. *Id.* art. 115.

36. *Id.*

37. *Id.* art. 121.

38. *Id.* art. 121(2).

another registration process, but the Kurdish Regional Government (“KRG”) requires such a filing before the commencement of commercial operations.

Another key jurisdictional issue relates to the authority to grant investment licenses under the Federal Investment Law No. 13 (2006). Not only does the KRG have its own investment law No. 3 (2006), but the federal law stipulates the creation of a Provincial Investment Commission (“PIC”), in addition to the National Investment Commission (“NIC”) located in Baghdad.³⁹ The jurisdictional divide between the PIC and the NIC was clarified through regulations, but the severe underdevelopment of the PIC has limited its effectiveness, allowing the NIC to claim more jurisdictional territory in practice.

For large infrastructure projects such as power generation and the exploitation of natural resources, not obtaining necessary permits and concessions is detrimental to the project. In Iraq’s non-centralized, federal governmental structure, the support granted from one governmental structure, *i.e.*, a province or a region, could be compromised by the central government’s refusal to support that permit process. The oil concessions signed by the KRG are a case in point, as they were rejected by the central government in Baghdad.⁴⁰ By refusing to allow oil from Kurdish wells to be transported by the oil pipe into Turkey, the central government effectively froze the project demanding that the KRG oil contracts be converted from production-sharing to service contracts.⁴¹ Similar scenarios can apply in other areas controlled by the central government such as airports, railroads, ports and national power grids. It is therefore prudent to secure the approval of the central government for any project arrangement that is expected to have a national or cross-regional dimension.

39. *Investment Promotion Law, No. 13, 2006.*

40. *KRG Oil Contracts Under Threat From Iraqi Government*, OIL AND GAS INSIGHT, March 2008, <http://www.oilandgasinsight.com/file/62470/krg-oil-contracts-under-threat-from-iraqi-government.html>.

41. *Shahristani Denies KRG Oil Contracts Agreed*, IRAQ-BUSINESS NEWS, Feb. 7, 2011, <http://www.iraq-businessnews.com/2011/02/07/newsflash-Shahristani-denies-krg-oil-contracts-agreed/>.

B. ENVIRONMENTAL REGULATIONS

Corporate and environmental permits in Iraq are not as well developed as those in developed countries. Nevertheless, there are developments and attempts to upgrade the legal framework as evidenced by the newly enacted Environment Protection & Improvement Law No. 27 (2009)⁴². This law mandates that every industrial project must present an Environmental Impact Assessment Study prior to starting the project.⁴³ Additionally, any facility that causes environmental pollution is required to maintain a log of all pollutant level measurements to be reviewed and tracked by the Ministry of Environment at its discretion.⁴⁴ The Environment Protection & Improvement Law also states that the responsibility for environmental contamination falls not only to the entity that caused the contamination, but also to any entity that contributed to the initial causation through negligence or failure to act to prevent any continued contamination.⁴⁵ A duty to act stems from, among other things, the transfer of ownership of a contaminated site to a new owner. The liability issue, under the law, is presumed against the new owner of the land, and it is up to the new owner to prove that he neither caused the contamination nor contributed to it through negligence or failure to act.⁴⁶

The Environment Protection & Improvement Law also introduced instances in which the corporate veil may be pierced in order to prevent abuses of the corporate form to shift or deny liability for environmental contamination.⁴⁷ These new exceptions are grounded in the legal responsibility of the parent company to supervise the entities it controls, as well as the individuals controlled by those entities. Iraqi law presumes that the parent company is responsible, and the parent company must prove otherwise by showing that it neither caused the contamination directly, nor that it was negligent in monitoring the acts of the subsidiaries and their employees.⁴⁸

42. The Kurdish region has a similar law, *No. 8, 2008*.

43. *The Environment's Protection & Improvement Law No. 27, 2009*.

44. *Id.* art.23.

45. *Id.* art. 24.

46. *Id.*

47. *Id.* art. 32.

48. *Id.*

C. CONCESSION AGREEMENTS & ASSIGNMENTS

Concession agreements, which are sometimes referred to as licenses, service contracts or development agreements, are of particular importance in development projects. This includes oil exploration projects—the area in which they were first used.⁴⁹

A concession agreement with the government is not only a contractual agreement with business terms; it is also a sovereign act which is often regulated and restricted by statutory and constitutional approvals. Executive approval of the concession or the license for the lender should not be considered sufficient in Iraq, even though in some instances it has been as was the case with the oil auctions through the Ministry of Oil.⁵⁰

From a lender's perspective, the need for ongoing consents and approvals by the host government is vital to assure the continued commercial viability of the project. Specifically, the lender must be able to take a security interest in the concession or license, to cure defaults by the project company under the concession and to operate the project in the case of default by the project company. Each of these requirements will mandate, in addition to pledges and mortgages, the execution of assignments.

Under the Iraqi Civil Code there are two types of assignments.⁵¹ The assignment of right allows lenders to assume the rights of the SPV against a third party.⁵² The assignment of debt allows lenders to assume the SPV's debt before a third party.⁵³ It is logical that lenders will be interested in the former, as they are keen on receiving rights owed to the

49. J. Dapray Muir, *Changing Legal Framework of International Energy Mangement*, 9 INT'L LAW. 605 (1975); Jahangir Amuzegar, *OPEC in the Context of the Global Power Equation*, 221 DENV. J. INT'L L. & POL'Y 4 (1974).

50. Interview with Abdul Karim Luaibi, Oil Minister, Republic of Iraq (Dec. 9, 2011), available at <http://www.iraqenergy.org/library/interviews.ph?detailof=74&content=Interview-with-Oil-Minister-Abdul-Karim-Luaibi.>; Vivienne Walt, *U.S. Companies Shut Out as Iraq Auctions Its Oil Fields*, TIME, Dec. 19, 2009; Andrew Kramer, *Deals With Iraq Are Set to Bring Oil Giants Back*, N.Y. TIMES, June 19, 2008.

51. *Iraqi Civil Code*, arts. 339, 362.

52. *Id.* art. 365.

53. *Id.* art. 339.

SPV by third parties if the SPV defaults, and they are not generally interested in assuming the debts of the SPV in the case that it defaults.

The assignment of right agreement is different from a lien or a mortgage as it does not involve or require registration of the assignment agreement.⁵⁴ While the perfection of a mortgage or a lien requires its registration with the relevant government agency or department (*e.g.*, the Land Registry Office or Vehicle Registration Department), the assignment is perfected by notice to, and acknowledgement by, the debtor (*i.e.*, the third party of the assignment agreement).⁵⁵

The enforceability of the assignment of right against the SPV requires the approval of the assignee and the assignor.⁵⁶ The assignee will typically be the lender and the SPV is the assignor, while the debtor is the third party entity delivering the assigned right (*e.g.*, an insurance company). For the assignment of right to be legally binding on the SPV, it must have a date certain and the assigned right must be well defined and not hypothetical or speculative.⁵⁷ The assignment's legality does not require the approval of the third party.⁵⁸ Nevertheless, for it to be enforceable against the third party, the third party should be informed of it which can be done either by the third party acknowledging it in writing, or by serving the third party with notice of its execution through service of process.⁵⁹ An assignment, therefore, is *legally binding on the SPV* once signed with the lender, but is not *enforceable against the third party until the third party debtor acknowledges it*.

In terms of rights and obligations, the assignment creates both legal rights for the lender/assignee and obligations on the SPV/assignor. Because those rights and obligations are specific to the lenders and the SPV respectively, their enforcement does not require the consent or approval of the third party/debtor.⁶⁰ Such legal obligations owed by the SPV include guaranteeing the assigned right against any action taken by the SPV, such as its sale, attachment or reassignment to others.⁶¹ Moreover, lenders receive the right to claim restitution in case the assigned right falls under provisional attachment issued by a court, or if

54. *Id.* art. 363.

55. *Id.*

56. *Id.* art. 362.

57. *Id.* arts. 363-64.

58. *Id.*, art. 363.

59. *Id.*, art. 367.

60. ABDUL RAZZAK SANHOURI, 3 AL WASEET (AlNahda Almesrea 1958).

61. *Id.*

the assigned right “did not exist” at the time of the assignment.⁶² The latter case occurs if the instrument creating the assigned right is void, or if, for example, the SPV had previously assigned the same right to a third party.

Furthermore, the assignment can be structured so that the SPV guarantees the solvency of the third party debtor at the time of the assignment’s execution and/or at the time the assignment is exercised.⁶³ Such a guarantee allows the lenders to claim the SPV’s share in the third party’s insolvency proceedings up to the value of the assigned right.⁶⁴

In addition, the enforcement of the assignment agreement against a third party who might, for example, come seeking foreclosure on the assigned right in the case of debtor’s bankruptcy requires that the assignment first be perfected. This can be achieved by having the assignee acknowledge the assignment either in writing or by acceptance of delivery of the assignment notice by court service.⁶⁵ More specifically, this requires either the debtor’s acknowledgment of the assignment agreement in writing, or service of process on the debtor of its execution. Such perfection is important to exclude the assigned right from enforcement by the creditors of the SPV in case it becomes insolvent, whereas it is subject to the assignment’s perfection date preceding the insolvency date.⁶⁶ Perfection also excludes subsequent reassignments of the same right, thus excluding any rights claimed by other alleged third party assignees that did not perfect their assignment, or perfected their assignment *post facto*.

II. TAKING OF SECURITY

As discussed earlier, a key factor in project finance lending is the robustness and certainty of the SPV’s projected revenue stream. Next in importance are project-based security liens for the benefit of the lenders, which will typically include all of the SPV’s assets. The collateral package should include a lien on all the movable and immovable assets

62. *Id.*

63. *Id.*

64. *Id.*

65. *Iraqi Civil Code* art. 363.

66. SANHOURI, AL WASEET, 3, *supra* note 60.

of the SPV, security over the project's cash flow including bank accounts, intellectual property, permits, licenses, concessions, contracts, insurance proceeds, and guarantees by any party, as well as any rights the SPV might have to liquidated damages. Assignment agreements, discussed earlier in this Paper, are the prime way for securing an interest in the SPV's contracts and agreements with third parties.

A. TYPES OF SECURITY INTEREST

1. *Possessive Mortgages*

Security over movable assets is taken by a possessive mortgage, which requires for perfection that the assets be specifically identified on a date-certain and physically transferred to the possession of the mortgagee (*i.e.*, the lenders).⁶⁷ This is essentially a form of pawning. Fortunately, the lenders do not have to assume possession of every single movable asset of the project company, as the law allows for leasing back of the mortgaged assets to the SPV.⁶⁸ Because Iraqi law requires that the mortgaged assets be specifically identified on a date-certain and physically transferred to the possession of the mortgagee,⁶⁹ it follows that it does not recognize the concept of a floating possessive mortgage, and further, that for the purposes of a possessive mortgage deed/agreement a complete and detailed list of the mortgaged assets must be prepared. The possessive mortgage is only effective as to the listed items.

Specifically, maintenance and/or purchases must be added to the list, which must in turn be given a date-certain before a notary public. There is no system of constructive notice for possessive mortgages, and the law does not protect the lender against bona-fide purchasers with no knowledge of a possessive mortgage. The mortgaged movable assets should therefore be identified as such once on the project's premises.

2. *Security Mortgages*

In contrast to a possessive mortgage, a security mortgage affects registered assets (*i.e.*, assets for which there is a national registry—

67. *Iraqi Civil Code* arts. 1322, 1342(2), 1352.

68. *Id.* art. 1323.

69. *Iraqi Civil Code* arts. 1322, 1342(2), 1352.

namely real estate, vehicles and securities).⁷⁰ The perfection of a possessive mortgage, therefore, requires registration of the mortgage with the relevant registry.⁷¹ Priority over such a mortgage among various mortgagees is time related, with older liens having first priority.⁷² In order to minimize payments to other creditors, the lenders should request that the borrower, at the risk of triggering a default event, not place any liens on any of its assets without the lenders' prior written consent.

Under Iraqi law, a lien cannot be placed over an indeterminate amount, and since Iraqi law does not allow for floating charges there is no possibility of having a perfected security over bank accounts, which have changing balances. As such, the lenders should assure that any bank accounts operated by the SPV be established with one of the lenders' banks. Further, they should explicitly prohibit the opening of any other accounts by the SPV with any other banks without the written consent of the lenders. The SPV's bank account should be in the name of the lender, with the SPV granted checking privileges that can be revoked in the event of a default.

Alternatively, lenders may set up the bank account in the name of the SPV and not the lender, with the SPV agreeing to give the lenders the authority to freeze the SPV's account and to transfer any funds therein to the lenders account upon notification. Under this option, however, the account remains in the name of the SPV therefore creating a risk of having a third party foreclose on the account before the lenders can act. Foreclosure on the SPV by third party suppliers or other creditors can give those other creditors immediate access to the SPV's bank account.

B. ENFORCEMENT OF SECURITY RIGHTS

Enforcement of security rights under Iraqi law can be broadly divided into two categories: enforcement under a default, and enforcement under a liquidation or bankruptcy.

70. *Id.* art. 1285.

71. *Id.* art. 1286.

72. *Id.* art. 1304.

In the case of a default, Iraqi law does not allow the lender, on its own, to complete the sale of the troubled SPV asset. Self-help remedies are not allowed; rather the pledge documents must be presented for execution at the court's Execution Department.⁷³ A request should be filed and evidence of the security perfection presented before an execution officer. If the debtor denies the debt then the matter will be moved to a court which allows for foreclosure on the asset for the benefit of the lender, and if there are several debtors, allows for the auctioning of the asset with the proceeds divided pro rata among the various creditors.⁷⁴ If the SPV goes into insolvency proceedings, the court appoints a receivership.⁷⁵

In certain instances, where a power of attorney is granted by the SPV to the lender over a certain asset, the need for court action can be bypassed by having a separate agreement (*i.e.*, a document separate from the pledge agreement). This agreement provides for the issuance by the SPV of an irrevocable power of attorney that allows the lender to sell the pledged asset. The text of the power of attorney itself should be unconditional (*i.e.*, it cannot refer to the occurrence of an event of default). That approach also works for taking over the management of the project, which can be done by a series of power of attorney documents covering the various areas of operation of the project that the lenders can immediately fall back on, in the case of a default, to continue running the troubled project. Similarly, a power of attorney can be secured over assignment agreements, securities and even real estate, where upon the relevant power of attorney can be used by the lender immediately, as opposed to going to court to seek the right to sell the troubled assets.

Iraqi law allows for the SPV, its creditors or its unpaid employees to file for the SPV's insolvency before a court of law.⁷⁶ Once a court declares the SPV insolvent, it must set the insolvency date, which is the time at which the SPV stopped paying its commercial debts. At any rate, the court cannot set the insolvency date more than two years prior to the date on which the court declared the SPV insolvent.⁷⁷ The claw back

73. *Execution Law, No. 45*, 1980, art. 15.

74. *Id.* art. 26.

75. *Commercial Code No. 149*, 1970, arts. 566-791.

76. *Id.* art. 570. The insolvency court is the First Instance court before which the insolvency request is filed.

77. *Id.* art. 578.

period, under which a payment or the giving of a security can be voided by a court, extends 90 days prior to the insolvency date,⁷⁸ and it⁷⁹ includes the voiding of (i) any donations made by the SPV; (ii) the prepayment of loans before their due date including the issuing of checks or commercial paper for the payment of such debt; (iii) payment of any debts in a manner or mode other than previously agreed to between the SPV and the third party; and (iv) any lien or mortgage guaranteeing a previous debt.

Therefore, the claw back measures represent a risk of avoidance for an action conducted by the lenders under the powers of attorney discussed earlier because a sale of any assets is prohibited once the insolvency is declared without the approval of the court.⁸⁰ Insolvency does not affect, however, the validity of contracts of non-personal nature entered into prior to the insolvency.⁸¹

III. INSURANCE & GOVERNMENTAL GUARANTEES

A. POLITICAL RISK INSURANCE

Cash-flow risk mitigation can be done by design, as in capturing revenue streams abroad, and by using loan repayment guarantees through political risk insurance programs such as those offered under the U.S. Overseas Private Investment Corporation (“OPIC”) and the Japan Export-Import Insurance Department. While these programs suffer from shortcomings in that they are narrow in scope and have protracted claims procedures, they do offer a service that is hard to come by in troubled areas such as Iraq, where the private insurance sector is still nascent, and not fully developed while international insurance companies have internal and external barriers to market entry.⁸²

78. *Id.* art. 614.

79. *Id.* art. 613.

80. *Id.* art. 660. All insolvency matters are governed by articles 566-791 of Commercial Code No. 149 (1970), which is otherwise superseded in all of its other articles by Commercial Code No. 30 (1984).

81. *Id.* art. 638.

82. See Paul E Comeaux & N. Stephen Kinsella, *Reducing Political Risk in Developing Countries: Bilateral Investment Treaties, Stabilization Clauses, and MIGA & (and) OPIC Investment Insurance*, 1 N.Y.L. SCH. J. INT’L & COMP. L. 15 (1995); S.

OPIC does not have a requirement that U.S. investors own the foreign facility, however, it only insures the part of the investment in the facility that is made by the U.S. investor. Eligibility for OPIC insurance is governed by statute⁸³ and includes only (i) citizens of the United States; (ii) U.S. corporations; (iii) foreign business entities owned at least 95% by U.S. citizens; or (iv) other qualified U.S. companies.⁸⁴

The Multilateral Investment Guarantee Agency (“MIGA”), of which Iraq is a member, is another option. MIGA is designed to promote foreign investment in member countries by providing guarantees, in the form of insurance, co-insurance and reinsurance, against non-commercial risk.⁸⁵ If MIGA finds for the insured investor, it will pay the compensation to which the investor is entitled under the guarantee.⁸⁶ Under the terms of the international convention establishing MIGA, it is permitted to seek reimbursement of such payments from the host government, which means that before MIGA coverage is issued, approval must be obtained from the host country.⁸⁷ MIGA’s grant of authority allows it to provide limited insurance against losses relating to (i) currency transfer restrictions; (ii) expropriation; (iii) war and civil disturbance; (iv) breach of contract; and (v) non-honoring of sovereign financial obligations.⁸⁸

The World Bank offers a similar service by providing guarantees to loans made by commercial lenders if the country’s government issues a counter-guarantee.⁸⁹ Such guarantees do not provide any coverage for expropriation, or for war, revolution or civil disobedience; rather they only cover losses attributable to currency convertibility and transfer,

Linn Williams, *Political and Other Risk Insurance: OPIC, MIGA, EXIMBANK and Other Providers*, 59 PACE INT’L L. REV. 5 (1993).

83. Congressional statement of purpose; creation and functions of Corporation, 22 U.S.C. § 2191.

84. What We Offer (Application for Political Risk Insurance), OPIC, <http://www.opic.gov/what-we-offer/political-risk-insurance/apply>.

85. Convention Establishing the Multilateral Investment Guarantee Agency, Oct. 11, 1985, art. 2.

86. *Investment Guarantees: Guarantees Overview*, MULTILATERAL INVESTMENT GUARANTEE AGENCY, WORLD BANK GROUP, <http://www.miga.org/investmentguarantees/index.cfm?stid=1796> (last visited Sept. 1, 2012).

87. Convention Establishing the Multilateral Investment Guarantee Agency, Oct. 11, 1985, art. 12(a), (b).

88. HOFFMAN, *supra* note 8.

89. *Id.*

breach of contract by the local government and changes in regulations affecting debt repayment.⁹⁰

B. GOVERNMENT GUARANTEES

The above options can be pursued in conjunction with guarantees granted by the host government itself, often referred to as sovereign guarantees. The scope of such a guarantee depends on the level of risk involved, and it can take several forms, such as an off-take purchaser agreement, or commitment to undertake certain legal or regulatory reforms.⁹¹ Lenders should seek enforceable promises, such as guaranteeing private debts needed for the project, or providing counter-indemnities to guarantor-parties.

Governments, on the other hand, will and should resist giving out anything but the most essential guarantees.⁹² Risks should be allocated to those best placed to manage them. Governments should carefully value the guarantees being considered, and how aspects of public-sector management should be modified to improve the quality of guarantees provided.⁹³ In the case of financing by the World Bank, a sovereign repayment agreement is mandatory for the provision of a World Bank loan, which requires repayment indemnity by the host country.⁹⁴

C. ASSIGNMENT AND USE OF INSURANCE PROCEEDS

As the insurance market in Iraq is extremely underdeveloped and not functional except in the area of car insurance, a few words are in order regarding the assignment of insurance proceeds and policies.⁹⁵ Generally, each lender should endeavor to add its name as an additional

90. *Id.*

91. TIMOTHY IRWIN, GOVERNMENT GUARANTEES ALLOCATING AND VALUING RISK IN PRIVATELY FINANCED INFRASTRUCTURE PROJECTS (The World Bank 2007); Delmon, *supra* note 2; Vinter & Price, *supra* note 29; HOFFMAN, *supra* note 8.

92. LLANTO GILBERTO & CECILIA SORIANO, GOVERNMENT GUARANTEES IN INFRASTRUCTURE PROJECTS: A SECOND, THIRD LOOK AT THE POLICY (Philippine Institute for Development Studies 1997).

93. IRWIN, *supra* note 91.

94. *Id.*

95. Misbah Kamal, *Iraq's Difficult Journey*, POLICY, Jan. 24, 2010.

insured party/beneficiary in the policy contract, thus enabling itself to receive benefits under the policy.⁹⁶ Certificates issued for an additional insured commonly face a problem if the certificate conflicts with the coverage limitation in the policy contract because courts may allow the policy contract to prevail over the certificate.⁹⁷ Therefore, the decision for a lender to clearly identify itself as an insured is of great importance.

Furthermore, a loss payee clause will afford the lenders access to insurance proceeds up to the amount of the debt.⁹⁸ A non-vitiating or breach of control clause is an important companion to the loss payee clause. It helps prevent the insurer from voiding a policy or refusing to make payment to the lenders as loss payee; and without a non-vitiating clause, a loss payee clause might not be very effective.⁹⁹ Reinsurance, especially if insurance is procured from local companies, can address questions as to the Iraqi insurer's credit-worthiness. A cut-through arrangement makes the reinsurance proceeds directly payable to the lenders, which in turn makes the lender's collateral over the insurance policies even more robust.¹⁰⁰ The cut-through arrangement is not in violation of any Iraqi laws, but it is a contractual arrangement and therefore can be treated as a voidable preference upon the bankruptcy of a local insurer.¹⁰¹

Finally, the project lenders should have an express defense against any subrogation claims via a waiver of subrogation clause or agreement which effectively prohibits the insurer from pursuing the project lender as a potential third party responsible for a loss in order to recover any paid insurance proceeds.¹⁰²

96. Douglas R. Richmond & Darren S. Black, *Expanding Liability Coverage: Insured Contracts and Additional Insureds*, 781 DRAKE L. REV. 44 (1996).

97. Thomas M. Hamilton, *Problems Arising from Additional Insureds Endorsements*, 384 DEF. COUNS. J. 62 (1995).

98. *Loss Payee*, IRMI.com, <http://www.irmi.com/online/insurance-glossary/terms/l/loss-payee.aspx> (last visited Sept. 9, 2012).

99. Noam Ayali, *Using Commercial Insurance to Avoid Project Risk*, 17 INT'L FIN. L. REV. 19 (2000).

100. Larry Schiffer, *Cut-Through Provisions in Reinsurance Agreements*, IRMI.COM, Mar. 2001, <http://www.irmi.com/expert/articles/2001/schiffer03.aspx>.

101. Vinter & Price, *supra* note 29.

102. Gary E. Snodgrass, *Waiver of Subrogation and Allocation of Risk in Construction Contracts*, 95 DEF. COUNS. J. 62 (1995).

IV. OWNERSHIP STRUCTURES

Selection of the form of business organization for the project company is an important decision in the project's development. The SPV, as the single-purpose corporate subsidiary, remains the most common project financing structure. Under this structure, the sponsor incorporates an entity to develop, construct, own, operate and maintain a project at a specific site. Apart from environmental liability established under a very recent law, and discussed earlier in this Paper,¹⁰³ piercing the corporate veil is not addressed under Iraqi corporate law. Nonetheless, in light of potential developments to the existing companies law,¹⁰⁴ officers of the SPV should conduct business of the SPV in the SPV's name and not that of the parent company. Further, the SPV should be the entity identified as the contracting party, with a clear distinction between the parent company and the SPV.

A. TYPES OF COMPANIES

Iraqi law allows for the incorporation of private companies, owned by private parties, as well as for mixed companies, in which the government owns not less than 25% of the shares.¹⁰⁵ The law namely allows for three forms of unlimited companies: single-owned projects, which are essentially a one-person partnership; general partnerships; and simple partnerships, which have no capital requirements and are simply created before a notary public.¹⁰⁶ The law further allows for two forms of limited liability companies: limited liability companies and public shareholding companies.¹⁰⁷

Unlimited companies structured as general partnerships in which all partners share proportionally in income, loss and the management of the business, provide for the joint and several liability of the partnership members, and therefore, are not suitable for an SPV in a project finance scenario.

103. *The Environment's Protection & Improvement Law No. 27, 2009.*

104. *Companies Law No. 21, 1997.*

105. *Id.*

106. *Id.* art. 8(3).

107. *Id.*

Iraqi law does not provide for limited liability partnerships, which allow for unlimited liability for managing partners and limited liability for the non-managing partners.

A limited liability SPV, on the other hand, allows its members limited liability up to their equity, but it does not allow for a board of directors. Rather, the managing director, who is appointed by the general assembly (*i.e.*, all of the shareholders), exercises the authority typically granted to a board of directors.¹⁰⁸ This is obviously problematic from a management point of view for the shareholders. Short of the Iraqi Parliament amending the current Companies law to allow for boards of directors in limited liability companies, the partners can have a shareholders' agreement amongst themselves, effectively creating a shadow board of directors. Alternatively, the partners can form a foreign company that allows for a board of directors. Such foreign company, in turn, wholly owns the limited liability company in Iraq. This latter approach allows for an actual board of directors under the foreign law, which has the benefit of giving partners greater control over the managing director position.

B. DUE DILIGENCE CONSIDERATIONS

From a due diligence point of view, it is important to verify the validity of incorporation and statutory existence of the specific business organization of the target (*e.g.*, ensuring its certificate of incorporation did not expire or that the company was not dissolved). Issues related to a company's good standing include meeting the statutory requirement of filing annual audited financial statements and holding the general assembly meeting for at least the minimum number of times annually, which for a limited liability company is biannually.¹⁰⁹ Any general assembly resolutions must be filed with the Companies Registrar within four days from their passing.¹¹⁰ As the concept of *ultra vires* is not well established in Iraq, the authority of a signatory to sign for a company must always be verified, preferably through a power of attorney or a general assembly authorization.

The articles of incorporation should be carefully reviewed to ascertain that the company has the power to conduct business in the

108. *Id.* art. 123(2).

109. *Id.* art. 86.

110. *Id.* art. 99.

desired areas, particularly whereas a foreign company must be registered in Iraq to do business. Registration can take place by incorporating under one of the types of companies mentioned earlier, or by establishing a branch office, which is only possible if a governmental contract is awarded to the company.¹¹¹ The branch office, however, will lose its legal standing once the existing governmental contract concludes and a new governmental contract is not awarded.¹¹² Therefore, if a tender is awarded, a branch office gives foreign companies the option to apply for other governmental tenders without being incorporated in Iraq.

V. DISPUTE RESOLUTION

Dispute resolution for project finance projects in Iraq presents unique challenges. The anticipation of disputes and the method of resolving them should not be perceived by international financiers as a straightforward exercise, which simply consists of the incorporation of a standard dispute resolution clause into the transaction. To the contrary, dispute resolution clauses should be one of lenders' first concerns when they enter into negotiations, particularly in Iraq. Drafting a dispute resolution clause requires both comprehensive knowledge of the project and dispute resolution mechanisms to be used by project participants, as well as accurate anticipation of the risks incurred.¹¹³

For instance, within the Iraqi context, the enforceability of international arbitration awards is problematic. Articles 251-276 of the Iraqi Code of Civil Procedure, according to which any matter capable of amicable settlement may be subjected to arbitration, regulates arbitration.¹¹⁴ However, the code of civil procedure does not contain provisions for foreign arbitral awards. Iraq is a signatory to the Riyadh Convention for judicial cooperation,¹¹⁵ but it has not yet adhered to the

111. *Regulation Governing Branches & Offices of Foreign Companies*, No. 5, 1989.

112. *Id.*

113. Christopher Dugué, *Dispute Resolution in International Project Finance Transactions*, 24 *FORDHAM INT'L L. J.* 1064 (2000).

114. *Iraqi Code of Civil Procedure No. 83*, 1969.

115. Riyadh Arab Agreement for Judicial Cooperation, 1983, available at http://adala.justice.gov.ma/production/Conventions/ar/Conv_Arabe/CA_Entraide_judiciaire.htm (Arabic translation), <http://www.unhcr.org/refworld/docid/3ae6b38d8.html> (English translation) [hereinafter Riyadh Arab Agreement]; *Iraq expresses readiness to*

New York Convention,¹¹⁶ or joined the International Centre for Settlement of Investment Disputes (“ICSID”).

As a result, the Iraqi commercial dispute resolution environment currently lacks a legal basis for the direct enforcement of foreign arbitration awards except under the Riyadh Convention.

A. COURT AWARDS

Iraqi law defines a foreign judgment as one that is rendered by a non-Iraqi court.¹¹⁷ It allows for the enforcement of foreign judgments, which can occur under the Enforcement of Foreign Judgments Law No. 30,¹¹⁸ or under the Riyadh Convention, which provides that contracting states should recognize and enforce the judgments rendered in any other contracting state.¹¹⁹ The Riyadh Convention, however, excludes administrative decisions.

To enforce a foreign judgment in Iraq, the judgment must be final, meaning that the foreign highest court rendered its non-appealable judgment, or that an appeal is time-barred. Nevertheless, even a final foreign judgment cannot be enforced if any of the following conditions is met:¹²⁰

1. if the defendant was not notified to appear before the court which issued the judgment or was not duly or properly served with notice,
2. if the court which passed the judgment was without competent jurisdiction,
3. the verdict is civil in nature,
4. if the defendant is able to establish to the court that the judgment is not final, or

extradite Jordanian prisoners, NEWS, ENGLISH.XINHUANET.COM (Feb. 2, 2010), http://news.xinhuanet.com/english2010/world/2010-02/02/c_13160635.htm.

116. Convention on the Recognition and Enforcement of Foreign Arbitral Awards, 1958, *available at*, http://www.uncitral.org/uncitral/en/uncitral_texts/arbitration/nyconvention_status.html.

117. *Iraqi law for enforcement of foreign judgments No. 30*, 1928.

118. *Id.*

119. Riyadh Arab Agreement, *supra* note 115, art. 25(b).

120. *Iraqi law for enforcement of foreign judgments No. 30*, 1928, art. 6 (author translation).

5. if the judgment was for a case which the courts in Iraq are not allowed to hear because it is against public policy or morality.

In addition to the above, the Enforcement of Foreign Judgments law requires reciprocity for enforcing foreign judgments,¹²¹ and it is not clear how Iraqi courts will interpret this requirement. Specifically, it is not clear what type of evidence will be required to show that such reciprocity exists. Accordingly, and pending a more developed jurisprudence on the enforcement of foreign judgments, the value of having a contract governed by Iraqi law and subjecting any disputes to Iraqi forums, should be carefully explored.

B. ARBITRAL AWARDS

The enforcement of foreign arbitral awards can occur directly under the Riyadh Convention, but only if the award was made by a tribunal in a member state.¹²² Therefore, there is not a direct mechanism for the enforcement of foreign arbitration awards issued by a tribunal that is not a member state of the Riyadh Convention. One way to work around this obstacle is to use the Law for Enforcement of Foreign Judgments to re-characterize the arbitration award as a court judgment.

Nonetheless, even under the Riyadh Convention, an arbitral award will not be enforced under the following circumstances:¹²³

1. If the law of the requested party does not permit the settlement of the subject of the dispute by arbitration.
2. If the adjudication of the arbitrators is made in execution of a condition or arbitration contract that is void or has not become final.
3. If the arbitrators are non-competent under the contract, condition of arbitration or under the law on the basis of which the adjudication was made.
4. If the litigants have not been served subpoenas in the proper manner.

121. *Id.* art. 11.

122. Riyadh Arab Agreement, *supra* note 115, art. 37.

123. *Id.* (author translation).

5. If any part of the adjudication is in contradiction with the provisions of Islamic Shari'a law, the public order or the rules of conduct of the requested party.

On the other hand, if Iraq moves in the direction of acceding to the New York Convention, that can strengthen foreign investors' confidence in the enforcement of arbitral awards by creating a direct legal obligation to honor and enforce them. The New York Convention will facilitate enforcement of international arbitration agreements and standardize the enforcement of arbitral awards. Iraq's accession to the New York Convention will require the enactment of an implementing law in order to put it into force, and the judiciary will need to be trained on its implementation in order to achieve uniform outcomes. This is particularly important for the Convention's public order exception,¹²⁴ and for determining when an award is considered to be final by the law under which it was made.¹²⁵

124. Kristin T. Roy, *New York Convention and Saudi Arabia: Can a Country Use the Public Policy Defense to Refuse Enforcement of Non-Domestic Arbitral Awards*, 18 FORDHAM INT'L L.J. 920 (1994).

Article 5.2(b) of the UN Convention on Enforcement and Recognition of Foreign Arbitral Awards ("NY Convention") and the UNCITRAL Model Law on International Commercial Arbitration ("UNCITRAL Model Law"), provide that a court may refuse to recognize or enforce an arbitral award if "the award is contrary to the public order." UNCITRAL Model Law on International Commercial Arbitration, 1985; Convention on Enforcement and Recognition of Foreign Arbitral Awards, 1958.

125. The New York Convention provides in Article V that:

1. Recognition and enforcement of the award may be refused, at the request of the party against whom it is invoked, only if that party furnishes to the competent authority where the recognition and enforcement is sought, proof that:

- (a) The parties to the agreement were, under the law applicable to them, under some incapacity, or the said agreement is not valid under the law to which the parties have subjected it or, failing any indication thereon, under the law of the country where the award was made; or

- (b) The party against whom the award is invoked was not given proper notice of the appointment of the arbitrator or of the arbitration proceedings or was otherwise unable to present his case; or

- (c) The award deals with a difference not contemplated by or not falling within the terms of the submission to arbitration, or it contains decisions on matters beyond the scope of the submission to arbitration, provided that, if the decisions on matters submitted to arbitration can be

CONCLUSION

This Paper examined the legal and procedural challenges surrounding project finance in Iraq, using the SPV as a common thread for each area discussed. The Paper addressed several issues that arise as a result of applying the legal concepts of project finance, which are based on Western legal notions, in the Middle East and specifically Iraq, which is governed by legal concepts that are not necessarily identical to or even compatible with Western legal concepts.

Project finance assets play an important role in getting requested financing from the lenders, but the key decision rests with the project's ability to generate revenue. This is a key distinguishing feature of project finance as compared to the more common type of collateral-only based lending. As a result, the assets of the SPV play a role in the decision to offer the loan, but a much bigger role is played by the robustness and certainty of the expected revenue stream of the SPV,

separated from those not so submitted, that part of the award which contains decisions on matters submitted to arbitration may be recognized and enforced; or

(d) The composition of the arbitral authority or the arbitral procedure was not in accordance with the agreement of the parties, or, failing such agreement, was not in accordance with the law of the country where the arbitration took place; or

(e) The award has not yet become binding on the parties, or has been set aside or suspended by a competent authority of the country in which, or under the law of which, that award was made.

2. Recognition and enforcement of an arbitral award may also be refused if the competent authority in the country where recognition and enforcement is sought finds that:

(a) The subject matter of the difference is not capable of settlement by arbitration under the law of that country; or

(b) The recognition or enforcement of the award would be contrary to the public policy of that country.

Convention on Enforcement and Recognition of Foreign Arbitral Awards, 1958, art. 5.

The New York Convention provides in article VI that a court may stay or postpone decision on an enforcement petition in case an action to set aside the award is pending in a court at the seat of the arbitration. These are commonly termed the articles V and VI defenses. See Michael H. Jr. Strub, *Resisting Enforcement of Foreign Arbitral Awards under Article V(1)(e) and Article VI of the New York Convention: A Proposal for Effective Guidelines*, 68 TEXAS L. REV. 1031 (1990).

which if deemed sufficient by the lenders, will result in a non-recourse type of financing.

If, on the other hand, the lenders feel that the SPV's expected revenue stream is promising but not certain or robust enough, then the lenders will require credit enhancement from a third party. More often than not, this third party is the project sponsor, which is the entity that champions the project before the creditors thus resulting in a recourse type of financing. Under such a scenario, the third party guarantor will be required to produce letters of credit, guarantees and potentially capital contribution commitments that will be triggered if certain benchmarks are not met.

The level of risk involved often determines the level of recourse in a project. The allocation of risk within the project is not only party-specific, but also time-specific. A common form of allocation of risk by sponsors and third parties is requesting equity injections in the early parts of the project, such as the construction phase, after which time recourse to the project sponsor's assets ceases and the lender's funding kicks in. After that phase, the loan is usually completely non-recourse, as the project is then expected to be able to generate its own revenue.

Such a structuring of the project's finances to include a contribution component by the project sponsor is an efficient way for the lenders to reduce the default risk of the SPV. During all the phases in which there are risk mitigation requirements by the sponsor through contribution and guarantees, the project is recourse. Further, once the project is completed according to the timeline in the project finance documents, the financing shifts to a non-recourse loan.

This Paper further argued that while the political process in Iraq provides assurances that economic stability will continue to develop along with the political process, more clarity is needed in the areas governing company registration and resolving legal tensions with the central government. As a result of the unique risks for project finance in Iraq, this Paper called for a careful review of any force majeure articles. Additionally, this Paper surveys available options for political risk insurance and concluded that, along with international loan guarantees, they provide an additional, albeit not complete, mitigation of risk.

This Paper's analysis of the constitutional power-sharing scheme in Iraq between the central and provincial and regional authorities concluded that it is prudent to secure the approval of the central and provincial governments for any project arrangement that is expected to have a national or cross-regional dimension. This Paper further

presented a comprehensive discussion of the legal and practical aspects for assignment of agreements and contracts within the scope of project finance.

Finally, the enforcement of foreign arbitral awards remains a concern as there exists no clear mechanism for enforcement and the enforcement of court decisions is subject to reciprocity. In order to move forward with meaningful enforcement mechanisms, Iraq should move towards joining the New York Convention, which will strengthen foreign investors' confidence, facilitate enforcement of international arbitration agreements and standardize the enforcement of arbitral awards.