

FEATURES

JTB STEPS ON THE INDONESIAN GAS

LATHAM & WATKINS, INTERNATIONAL LEGAL COUNSEL TO THE SPONSOR AND THE BORROWER IN THE FINANCING OF THE JAMBARAN-TIUNG BIRU PROJECT, PROVIDES AN OVERVIEW OF THE DEAL AND INSIGHT INTO SOME OF ITS NOTABLE FEATURES. BY **CLARINDA TJIA-DHARMADI**, PARTNER, **TIM G FOURTEAU**, COUNSEL, AND **MEREDITH STRIKE**, ASSOCIATE.

The Jambaran-Tiung Biru Project (JTB Project) is among the largest upstream oil and gas projects to reach financial close in Indonesia in the past decade, and marks several important milestones for project financings in the region.

The limited recourse project financing utilised a trustee borrowing structure (TBS) and is the first project financing in the region to comprise conventional interest-bearing tranches with Islamic financing tranches.

It is also the first limited recourse project financing to feature a subsidiary of Indonesian state-owned oil and gas company PT Pertamina (Persero) (Pertamina), namely PT Pertamina EP Cepu (PEPC), as the anchoring sponsor.

Containing extensive Indonesian participation throughout the structure, it is also the first oil and gas project financing in Indonesia to be supported by an all domestic offtake, with no government support, solidifying the trend set by the 2017 Tangguh Expansion Project TBS financing, which similarly featured a relatively high degree of domestic involvement.

Before the 2017 Tangguh Expansion Project TBS financing, most large-scale oil and gas projects in Indonesia were financed primarily on the basis of export sales with international banks. In contrast, the JTB Project is underpinned entirely by domestic sales and financed by both domestic as well as international financial institutions, demonstrating the increasingly important role of local banks in major project financings in the republic.

Project overview

The JTB Project involves the development of proven gas reserves, as well as the construction and operation of a gas processing facility and pipelines. It is located in the unitised Jambaran-Tiung Biru field (JTB field) in Bojonegoro Regency, East Java Province, Indonesia.

The JTB Project is supported by gas sales of up to 192 million standard cubic feet per day under a long-term, fixed-price and fixed-volume take-or-pay gas sales agreement with the offtaker, Pertamina. Project completion is scheduled to occur in 2021.

The development scope covers the drilling of six development wells that will produce

315m standard cubic feet per day of raw gas, the designing and installing of gas processing facilities with a maximum capacity of 330m standard cubic feet per day and the development of gas flow lines from the wells to the gas processing facilities and sales gas pipelines from the gas processing facilities to the Gresik-Semarang pipeline.

PEPC and PT Pertamina EP (PEP), a wholly-owned subsidiary of Pertamina, are sponsoring the development of the JTB Project (though PEP is not a party to the financing). PEPC will operate and maintain the JTB Project, including the gas fields, pipelines and gas processing facilities.

PEPC and PEP own 92% and 8% of the unit interests in the unitised JTB field, respectively, and will share a proportionate amount of project revenues, capital costs and operating expenditures.

Apart from the offtake arrangements, under which Pertamina undertakes to purchase all gas production of the JTB Project on a 90% take-or-pay basis over the entire project life, Pertamina indirectly holds a 100% unit interest in the JTB Project via its subsidiaries.

The JTB Project secured more than US\$1.84bn in debt commitments, split into conventional and Islamic finance tranches. Each of the conventional and Islamic finance tranches consists of a 10-year tranche and a 15-year tranche.

The lender group comprises both international and domestic financial institutions. The international banks participating in the conventional tranches include two Malaysian banks, CIMB and Maybank; two Japanese banks, MUFG and Sumitomo Mitsui Banking Corporation; one Chinese bank, Bank of China; one Singaporean bank, DBS; and one Italian bank, Intesa Sanpaolo.

The domestic banks participating in the conventional tranches comprise three state-owned Indonesian banks – Bank Mandiri, Bank Negara and Bank Rakyat Indonesia – and one private Indonesian bank, Bank BTPN. MUFG (Malaysia) Berhad participated as Wakala investor for both Islamic finance tranches.

Trustee borrowing scheme

First developed and employed by Pertamina and its production-sharing contractors in 1984, the TBS is a proven and tested financing structure with a track record of successful implementation in Indonesia for over 30 years. Lenders draw comfort from this well-established structure, without the need for a traditional security package.

Under the TBS, loans are repaid by a trustee from an agreed portion of proceeds under identified revenue contracts. Lenders look solely to this source of debt service for payment, with no recourse to the project and no security interest in the project assets or contracts.

The trustee (HSBC Bank USA, in the case of the JTJ Project) is the borrower under the loan agreements with the lenders, and debt service payments are made from trust accounts or accounts held in the name of the trustee on trust for the lenders and PEPC as the trust beneficiaries, in New York.

In the JTJ Project, Pertamina as offtaker will pay PEPC's portion of the gas and condensate revenues to the trust accounts directly. These revenues will be paid by the trustee to the lenders for repayment of principal and interest (or fixed investment return in the case of the Islamic finance tranches). This source of debt service functions as the primary security for the lenders.

Notable features

- *Islamic finance tranches* – The JTJ Project is the first limited recourse project financing in the region to include Islamic finance tranches alongside conventional interest-bearing tranches. The JTJ Project's Islamic finance tranches are based upon a Wakala structure, whereby the principal (the muwakeel) contributes capital to the agent (the wakeel) to transact on its behalf when investing in an identified asset or business.

The economics of the conventional tranches are substantively mirrored in the Islamic tranches. Under the Wakala structure, the investors mandate the trustee to invest amounts advanced by them in the identified business, ie, the engineering, procurement and construction contract and the gas sales agreement. The trustee then sub-delegates this agency role to PEPC, which receives the funds from the investors and injects them into the JTJ Project.

The Wakala investors specify an expected profit rate, which is benchmarked to Libor and subject to an applicable margin. The principal of each investment is redeemed by the trustee according to a pre-determined schedule, which mirrors the principal repayment schedule under the conventional financing agreements.

The inclusion of Islamic finance tranches alongside conventional tranches in the JTJ Project reflects the growing role of Islamic financing in South-East Asian projects. The project's Wakala structure will serve as a model

for future financings in Indonesia and the region.

- *Pertamina subsidiary as sponsor* – In addition to the novel inclusion of Islamic finance tranches, the JTJ Project is the first TBS project to be sponsored by a Pertamina subsidiary rather than Pertamina. PEPC is a wholly-owned subsidiary of Pertamina, established in 2005 to engage in the upstream oil and gas sector, including exploration, exploitation and production.

PEPC is an experienced, creditworthy sponsor with an established track record of oil and gas project development in Indonesia, and PEPC is considered to have strategic importance to Pertamina. The credit aspects of the JTJ Project are considerably enhanced by PEPC's provision of robust contingent support. PEPC's position as sponsor in the JTJ Project provides a basis for other Pertamina subsidiaries to play major roles in future TBS financings.

- *Loans with multiple tenors, Day 1 IRS hedging* – The JTJ project is among the first TBS financings to feature loan facilities with different tenors and day-1 interest rate hedging. Specifically, the JTJ project includes 10-year tranches and 15-year tranches, with several banks separately procuring political risk insurance coverage to participate in the 15-year tranches. The borrower hedged 50% of its Libor exposure shortly after financial close, which is uncommon for TBS financings where Libor risk exposure has often been fully assumed by projects.

- *Domestic offtake and bank participation* – In addition to the milestones described above, the JTJ Project financing is noteworthy for its relatively high degree of Indonesian participation in the offtake and project debt.

The JTJ Project financing is the first oil and gas project financing to be supported exclusively by domestic sales, with no government support, and demonstrates the international bank market's growing comfort with domestic revenue risk, confirming the trend set by the 2017 Tangguh Expansion Project, which was primarily financed on the basis of sales to PLN.

Before 2017, most large-scale oil and gas projects in Indonesia were underpinned almost exclusively by export sales. Further, the participation of four Indonesian banks underscores the growing comfort of the domestic banking sector with project financing.

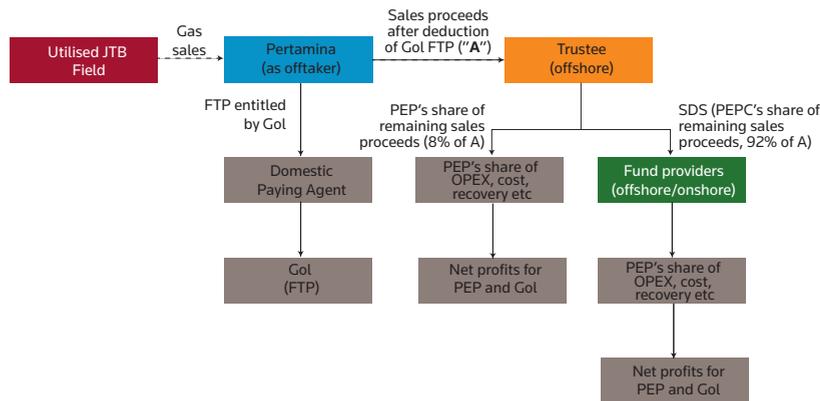
Conclusion

As the first limited recourse project financing in the region to feature conventional interest



TBS is a proven and tested financing structure with a track record of successful implementation in Indonesia for over 30 years

FIGURE 1 - JT B PROJECT'S TRUSTEE BORROWING SCHEME



bearing tranches alongside Islamic finance tranches as well as a Pertamina subsidiary as sponsor and multi-tenor loans, and the first oil and gas project financing to be supported by an all domestic offtake with no government support, the JT B Project is a landmark financing that will serve as a template for other oil and gas projects in Indonesia.

It will bring employment and gas needed for Indonesia's national energy plan, and spur domestic consumption – at least 40% of the engineering, procurement and construction contract will utilise domestic content.

It is a critical part of Pertamina's gas value chain, supporting power plants and industrial end-users in East Java. Given the value of the JT B Project to the Indonesian economy, the Indonesian government has justifiably, and unsurprisingly, designated it as a National Strategic Project.

Latham & Watkins represented PEPC as sponsor and HSBC USA as trustee borrower. Milbank was the international legal counsel to the lenders. UMBRA Strategic Legal Solutions was Indonesian legal counsel to PEPC and Ali Budiardjo Nugroho Reksodiputro was Indonesian legal counsel to the lenders. ■



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