

# EMASESA: New twist on future flow

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Municipal water utility EMASESA (wholly owned by the City of Seville) has closed the first forward receivables deal of its kind in Spain - a Eu96.15 million non-recourse structured financing arranged by Dexia Sabadell Banco Local (Dexia SBL) and Ahorro Corporacion Financiera.

The deal, begun in 2001 when Dexia approached EMASESA with the idea, comprises the sale of improvement fees (canon de mejora). The canon are usage-based water surcharges established under a decree by the regional government of Andalucia that EMASESA adds to its retail and commercial invoices to fund upgrades to water and sanitation infrastructure both in Seville and its environs.

The innovation in the transaction is that the financing is structured as a purchase of EMASESA's rights to charge improvement fees - not the fees themselves. As a sale of rights, the deal is non-recourse and consequently has no balance sheet impact on the level of indebtedness of the municipality - an aspect that is certain to make the template very popular with other cash-strapped municipals.

Although commercially bankable, of the total Eu96.15 million funding the European Investment Bank (EIB) has put up Eu60 million with a tenor of 14.25 years. Surprisingly, the EIB loan comes with a wrap from monoline FSA (a Dexia subsidiary). Pricing has not been released but according to Rene Kassis, director, infrastructure project finance, Dexia Credit Local, the combined strengths of EIB and the wrap create "significantly cheaper pricing and a longer maturity. You have a bond tenor without a bond."

On the commercial tranche, Dexia SBL has a take of Eu18.08 million with three Spanish savings banks - El Monte, Unicaja and Caja San Fernando - holding Eu6.03 million each for a tenor of eight years. The canon fees are sized to cover all interest and principal payments to the lenders by December 2010 for the commercial tranche and December 2016 for the EIB.

The intercreditor agreements in the deal are well-balanced. The EIB tranche has senior ranking in terms of rights to the canon proceeds because of its longer tenor. However, the commercial banking tranche benefits from an earlier amortisation schedule, allowing full repayment before the EIB tranche starts to amortise. The resulting compromise is that under a base case scenario the banks get fully repaid before 2012 and the EIB in 2016, while the EIB enjoys a senior access to the canon proceeds in downside and default situations. Garrigues provided common legal counsel while the EIB was represented by Clifford Chance.

There is increasing demand for quality water services in the Seville area, which has put significant pressure on the existing network. EMASESA manages the water supply and sewage services for the city of Seville (fourth largest city in Spain) and 13 municipalities in its metropolitan area. The improvement works that need to be carried out until 2004 focus on the upgrading of mains, pumping stations, and treatment plants. They are designed to improve the quality of the water supply, allow for the reduction of water losses in the grid, the increase of water pressure, and provide for a better treatment of residues.

The success of the deal relies heavily on the solid history of the canon income stream and its design. The canon fee concept is already well-established in the region of Andalucia. It was first introduced in 1994 by regional decree to finance investment during 1994-96. It was subsequently adjusted and extended in 1998 for a second phase of works. Consequently the canon de mejora payment system has an eight-year credit record. In order to finance the latest investment programme, and at the request of EMASESA, Andalucía issued a further decree in July 2001 increasing the fee

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in terms of eur/m3 and extending its applicability from 2006 to 2016.

Having purchased the rights on those proceeds, the banks will pay EMASESA an amount equal to the NPV of the future income from the canon. The purchase amount will be paid in installments between the deal closing date and the forecast end of the investment period (July 2004), in order to match disbursements to be made by EMASESA.

A key feature of the decree is a provision for revising the canon rates to compensate should certain economic assumptions of the base case scenario - water consumption, interest rates - result in a shortfall under the bank repayment schedule. It is an unlikely scenario claims Kassis: "The assumptions per capita are quite conservative and if it drops below a certain amount then revision of the rates kicks in."

Consequently, the canon system leaves the financial institutions mainly exposed to legal and regulatory/political risks - unlikely at best. Nevertheless, lenders get even more comfort from contractual provisions that allow for the resale of the rights to EMASESA (and therefore a recouping of the purchase price) should there be material changes to the legal environment of the transaction threatening the existence of the canon, its scope, or its applicability. Whilst this also implies that the financiers would be taking certain credit risks on EMASESA itself, these are considered acceptable given the legal status of the municipal company and the essential service it provides.

Given that it is the first example of using a purchase of rights on improvement fees to finance water infrastructure investments on a non-recourse basis, it seems likely the EMASESA model will be followed by other regional governments both in Spain and without (if the legal system is similar). Dexia already claims to have further Spanish deals in the pipeline with another close forecast for first quarter 2003.

## **EMASESA**

Status: Closed November 2002

Description: Eu96.15 million sale of water receivables

Location: Seville, Spain

Sponsor: EMASESA

Arrangers: Dexia Sabadell Banco Local, Ahorro Corporacion Financiera

Debt providers: EIB, Dexia, El Monte, Unicaja, Caja San Fernando

EIB guarantor: FSA

Tenor: 14.25 years EIB, 8 years commercial tranche

Common legal counsel: Garrigues

EIB counsel: Clifford Chance

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