

When Megadeals *Stumble*

Resolving Project Finance and
Arbitration Crossroads



Introduction

In recent times, the growth of complex infrastructure and energy ventures has elevated project finance into one of the most sophisticated financing structures in global commerce. Megaprojects involve multilayered contractual frameworks, extensive security packages, and diverse stakeholder commitments, combined with high risk and capital intensity.¹ As a result, disputes frequently arise even where projects are carefully structured.

Disputes in such projects are inevitable, and certain issues recur in project finance arbitration, irrespective of the project type. This article identifies key flashpoints and outlines strategies for lenders, sponsors, and governments to achieve commercially viable resolutions. It highlights that aligning contractual safeguards with bankability is key to preventing disputes and maintaining project progress.

Three Pillars of Project Finance Risk

01 Contractual Layering

Multi-party agreements, security packages, concession terms.

02 Capital Intensity

High-leverage financing reliant on projected cash flows.

03 Stakeholder Diversity

Lenders, sponsors, States, contractors and operators.

Common Triggers of Project Disputes:

Delay, Default, Force Majeure, and Regulatory Change

Disputes in project finance transactions are usually caused by a handful of stress points that keep reappearing and are deeply embedded in construction and financing agreements.²

One of these stress points is delay. Construction delays, which may range from contractor underperformance to supply chain disruption, changes in design, or even interference from the employer, can disrupt the timelines set by the parties.³ Since financing agreements are set up based on expected cash flows, any delay, however small, can lead to extra costs, penalties, or the need for additional financial commitment from sponsors.⁴

Another major trigger is default. Usually, project finance agreements contain very detailed financial covenants and obligations. A default will usually arise from failure to meet financial targets or any of the obligations agreed by the parties.⁵ A breach of these can be failure to meet a debt service coverage ratio or failure to achieve commercial operation by a certain date, which might be deemed as events of default.⁶ Project sponsors (i.e., the equity investors or project owners) often debate whether a breach is serious or fixable, while lenders consider whether to enforce the rules or allow a waiver to protect value.

In recent years, force majeure provisions have become even more important due to pandemics, geopolitical instability, and extreme weather conditions.⁷ Legal and arbitration cases often focus on whether the incident falls within the contractual definition of force majeure, whether it was foreseeable, and whether the affected parties took reasonable steps to mitigate damages.⁸ The financial effects such as extension of time, payment of costs, or rights to terminate, are of great significance financially.

Another controversial issue is regulatory change, especially in emerging markets. Changes in tariffs, tax regimes, environmental standards, or currency controls can significantly affect project economics. Stabilisation and change-in-law clauses are often the main issues in arbitration because the parties dispute the risk-allocation and the right to compensation.⁹

Tribunal Test

Was the event within the clause?

Was it foreseeable?

Were mitigation steps reasonable?

The Lender's Toolkit:

Security Enforcement vs. Project Rescue

1. Enforcement remedies:

In project finance, lenders commonly take Special Purpose Vehicle (SPV) shares, contract rights, and cash flows as collateral. Enforcement typically involves foreclosure or the sale of these assets. Where lenders offer to accept the collateral in full satisfaction of the debt, they are not required to obtain the borrower's consent before proceeding with foreclosure.¹¹ Under United States (U.S.) law, foreclosure automatically occurs 20 days after notice is given to the borrower, and if the lender does not receive a written objection from the borrower to the proposed foreclosure. Under the English law, a properly structured share pledge under the Financial Collateral Arrangements (FCAR) allows the lender to appropriate the shares outrightly without a court sale.¹² In both cases, the lender (or its nominee) assumes control of the project company and may also take on its liabilities, unless the project is refinanced or restructured.

2. Project-continuity clauses:

To maintain project operations, agreements often give lenders step-in rights. These allow lenders to take over the SPV's contracts or transfer them to an approved replacement operator when needed.¹³ These clauses typically require lenders to remedy any existing defaults before exercising their step-in rights.¹⁴ In concession agreements (e.g. public-private partnership (PPP) contracts) developers typically negotiate that permits and tariffs remain in force and not terminate solely due to a lender enforcement.¹⁵ Model PF terms¹⁶ expressly extend the concession or provide adequate compensation to ensure debt repayment on enforcement.¹⁷

3. Enforcement vs. viability tension:

Aggressive enforcement can threaten project viability. Foreclosure or sale of the SPV may breach change-of-control covenants or trigger defaults, risking project shutdown. In *Cukurova v. Alfa*,¹⁸ the court allowed the lender to take collateral under English law, but required proper notice and fair valuation.¹⁹ Similarly, direct agreements generally require lenders to remedy any project defaults before exercising their step-in rights.²⁰ The primary objective is to preserve the project as an ongoing concern,²¹ so transaction documents typically impose cure periods, notice requirements and consent rights to keep the project running even during enforcement.

Jurisdictional Snapshot — Two Roads to Foreclosure

United States

20

days

Foreclosure occurs automatically 20 days after notice — absent a written borrower objection.

England & Wales

FCAR

A properly structured share pledge under the Financial Collateral Arrangements allows outright appropriation - without a court sale.

Arbitrating Technical Issues:

Experts, Delay Analysis, and Damages Modeling

In project finance arbitrations, technical disputes often determine whether a commercial project succeeds or fails.²² These cases are not just about breaches of contract; they are most often about how delays, construction problems, or underperformance affect the project's complex financing and cash flows.²³

Delay analysis is a fundamental element. Tribunals often review project schedules to figure out what caused the delay, whether delays overlapped, and whether they were excusable.²⁴ Usually, the problem is not whether the delay occurred, it is deciding who will assume liability for the delay when there are several contributors, contractors, sponsors, and even unforeseen regulatory or force majeure events, at the same time.²⁵

Disputes over technical performance require extensive knowledge. Arbitrators determine whether engineering, procurement, and construction (EPC)²⁶ contractors fulfilled their contractual guarantees and whether they met the specified efficiency levels or complied with the requirements for commissioning.²⁷ Minor variations could lead to multimillion-dollar claims unless carefully considered within the contract's tolerance levels.

Similarly, damage modelling converts technical information into its financial consequences. In this process, experts recreate the financial flows, measure the loss of profits, and also consider the risks of overruns, interest during construction, and financing gaps.²⁸ Tariffs, inflation, discount rates, and assumptions about plant availability are highly debatable elements; even small differences can change claims by significant amount.

Modern arbitration procedures, such as experts appointed by the tribunal and hot-tubbing,²⁹ are essential to reconcile conflicting technical narratives. The most successful cases combine precise technical evidence with rigorous financial modelling and translate complex engineering and operational realities into coherent, tribunal-ready arguments that protect both legal rights and the project's economic viability.

Damages Model · Sensitivity Drivers

Small shifts in any one variable can change a claim by a significant amount.

±

Tariff assumptions

Revenue forecasts hinge on regulated and merchant pricing.

±

Inflation indices

Compound effects over long concession horizons.

±

Discount rates

Present-value calculations turn on WACC selection.

±

Plant availability

Uptime assumptions drive lost-revenue calculations.

Preserving the Project:

Dispute Resolution Mechanisms that Keep the Deal Alive

Multi-tier dispute clauses in infrastructure deals:

Project agreements usually require ADR in stages before arbitration. Typical steps include good-faith negotiation, referral to a technical expert or engineer, and (in FIDIC-style contracts) a Dispute Adjudication Board (DAB) decision.³⁰ This step-by-step approach allows parties to pause, reassess, and resolve smaller issues early, helping to preserve commercial relationships. Courts now uphold such multi-level dispute resolution clauses as a matter of policy; for example, *Cable & Wireless v IBM*³¹ confirmed the enforceability of a mandatory ADR clause.³² Requiring negotiation or expert determination first helps keep stakeholders engaged and the project running, avoiding an immediate final award.³³

In arbitration for instance, well-drafted clauses spell out scope, seat, law, and tribunal composition. Most of the highly complex project disputes use international arbitration rules: ICC³⁴ or LCIA.³⁵ The clause will often list essential issues (“any dispute arising out of or relating to this contract”) and specify a seat in an enforcing jurisdiction. If one party is a state, BITs³⁶/ICSID³⁷ treaties supplement or replace commercial rules.³⁸ Overall, the clause is structured to minimise challenges and maximise enforceability.

Project continuity focus:

The net effect and objective of these dispute resolution mechanisms is to keep the deal alive. Arbitration’s confidentiality and flexibility mean core stakeholders (lenders, sponsors, authorities) can stay involved rather than withdrawing. The structured escalation (negotiation, expert/DAB, and arbitration) provides multiple chances to fix problems. Experts in project deals have also emphasised that staged and structured dispute resolution “saves time and costs, as well as helping (parties) preserve their commercial relationship”.³⁹

“*Staged and structured dispute resolution saves time and costs — as well as helping parties preserve their commercial relationship.*”

Key Takeaways

01

Progressive resolution

Adopt a progressive dispute resolution process to address issues promptly and protect relationships.

03

Quantify accurately

Use technical and financial analysis to measure delays, performance, and losses accurately.

05

Anticipate external risk

Anticipate regulatory and external risks to reduce uncertainty.

02

Balanced contracts

Draft contracts to protect both lenders' rights and keep the project running smoothly.

04

Engage early

Engage stakeholders proactively to address problems before escalation.

06

Arbitrate to preserve value

Use arbitration as a tool to resolve disputes while safeguarding the value and finances of the project.

Conclusion

When major deals stumble, the problems are usually not limited to a sole issue in contract terms; it often involves the whole financial and operational network being put under pressure.

Late payment, non-payment, force majeure events, regulatory changes, or failure to meet technical requirements will each test whether the agreed allocation of risk between the parties is sound and effective.

That is why arbitration is no longer a place for just apportioning blame, but rather it is a tool for restoring the financial balance.

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