



HM TREASURY

**To Departmental Private Finance Units
05 May 2006**

Use of the Spens clause in PFI Transactions

In “PFI: meeting the investment challenge”, the Government expressed its concern that the Spens clause creates an extra cost of termination for a bond-financed PFI project compared to a project financed by a bank loan in the rare circumstances where it wishes to voluntarily terminate due to major changes in the public sector’s requirements that cannot otherwise be accommodated.

Since the publication of the document consultations have been carried out with issuers/bond lead managers and investors to gather up-to-date market feedback on the operation of the Spens clause and the extent to which a modified Spens clause has been implemented.

The views and feedback received from all parties were broadly consistent and can be summarised as follows:

- The ABI, in its October 2003 paper ‘improving market standards in the Sterling and Euro Fixed Income Credit markets’, had already recognised that in many circumstances Spens was punitive to issuers and stated that it ‘would be willing to see a move away from Spens-call provisions in favour of a less onerous standard’.
- In PFI, a Spens or Spens-like clause is only contemplated for Authority Voluntary (or Default) Termination. It is already widely accepted that no Spens protection is afforded for payments that result from a Force Majeure event, Corrupt Gifts or PFI contractor Default termination.
- PFI bond arrangers have launched several successful issues where the Spens compensation clause was modified to be less punitive for issuers [and this practice has become more common in the market].

In line with this feedback, and as set out in “PFI: strengthening long-term partnerships”, Government wishes to regularise the practice of using the Spens clause. Therefore, the Treasury will now require all PFI contracts funded through the capital markets to contain a modified Spens clause.

Determining the most appropriate form of modified Spens clause will be a decision for each public sector procuring authority in the context of its specific requirements on a project. Further guidance is attached to this letter to assist procuring authorities in their decision making process.

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