

Financing space assets: 6 things you should know

Financing space assets has many of the hallmarks of financing traditional aircraft and related assets. However, it does operate in its own unique environment, with its own significant opportunities and pitfalls.

The NASA / SpaceX Demo-2 mission has signalled a turning point in the development and execution of space assets. It has also sparked a fresh wave of private sector interest in Mainland China and APAC more broadly in what has traditionally been viewed as a highly specialised, but generally *public sector*, industry arena.

Commercial space activities are moving beyond traditional satellites, and into a world of satellite constellations, cargo freighters, reusable launch vehicles and crewed commercial spacecraft such as Crew Dragon. Development is rapid, ambitions are being realised.

All of this requires capital. For financiers, this means opportunities to expand beyond traditional aviation and trade finance, into emerging technologies that will shape a vast industry. Having sound financing structures in place for space activities will be critical. Early movers will have the advantage of building track record and shaping future regulation.

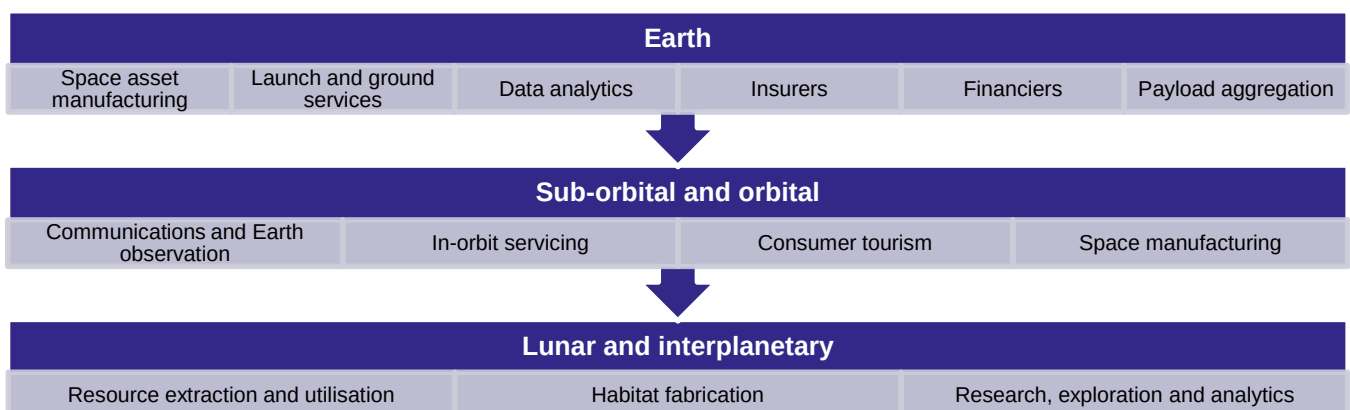
So here we go – 6 things you should know about financing a space asset.

Key point 1: The space sector has multiple players, with a vibrant and growing APAC industry

The space sector is not limited to the United States and Europe. Mainland China is also a key player. The vibrant Chinese space industry includes established state-owned enterprises, such as China Aerospace Science and Technology Corporation, as well as private commercial ventures, such as i-Space. We are also seeing rapid growth across APAC – for example, Hong Kong has a robust satellite sector, the Philippines has just set up its own space agency, Indonesia and Australia are rapidly developing launch sites, and Singapore is awash with space start-ups.

The growing commerciality of space activities – or “NewSpace” – extends well beyond satellites, through to practically any commercially valuable object that can be launched into space – a “space asset”. A key feature of this new space age is that the key players are no longer just governments, credit export agencies, large state-owned enterprises and listed companies. Rather, private companies are looking for financing to help them expand throughout the full space industrial chain.

The following chart provides a snapshot of the key players:

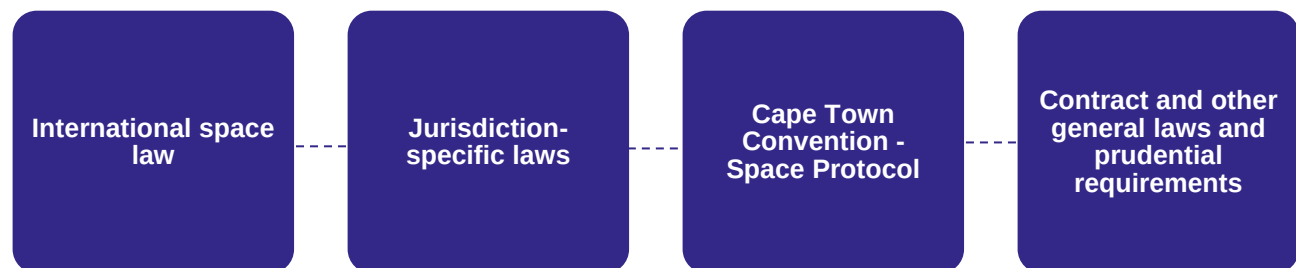


THE GLOBAL SPACE INDUSTRY GENERATES REVENUES OF USD350 BILLION BUT IS ESTIMATED TO REACH MORE THAN USD1 TRILLION BY 2040.

- Morgan Stanley, *Space: Investing in the Final Frontier*, July 2019

Key point 2: The legal framework consists of international and jurisdiction-specific laws

There are four key components relevant to financiers.



We briefly summarise the three space-specific components as follows. **Key point 5** deals with contracts.

International space law

There is a significant body of international space law, essentially in the form of five treaties developed under United Nations auspices. The core principles are established in the first of these treaties, the **1967 Outer Space Treaty**. Of particular relevance to commercial parties is Article VI of this treaty, which requires states to authorise and continually supervise their commercial space activities.

Jurisdiction-specific space law

To meet their Outer Space Treaty obligations, leading space-faring jurisdictions have adopted **jurisdiction-specific space laws**. While these space laws vary significantly across jurisdictions, they typically establish:

- a licensing regime for launches and other space activities;
- a national register for space assets; and
- in some cases, indemnification or insurance requirements for private space actors.

These laws are set out various ways. For example, Australia has a single act – the *Space (Launches and Returns) Act 2018* - with subsidiary legislation. Mainland China's space law is contained in a series of departmental regulations – primarily the *Measures for the Administration of Registration of Objects Launched into Outer Space 2001* and the *Interim Measures on the Administration of Permits for Civil Space Launching Projects 2002*.

The Space Protocol

The Space Protocol to the Cape Town Convention is part of the framework of international space law, although it is **not yet in force**. Unlike other international space laws, the Space Protocol is focused on addressing the concerns of financiers (such as title to space assets, the priority of secured parties and remedies on an event of default, including rights of repossession). The Space Protocol is designed to facilitate the commercialisation of space assets (which includes, for example, space stations, space vehicles and reusable launch vehicles).

Once it enters into force, private parties will be able to protect their financial interests in space assets by registering them on the International Registry and have access to the remedies available under the Cape Town Convention. However, to replicate the success of the Aircraft Protocol to the Cape Town Convention, the key countries with capacity to engage in space activities will need to become party. To date only four states have signed the Space Protocol – at this stage, the small group of signatories does not include Mainland China or any other APAC jurisdiction.

Key point 3: Successful structuring requires considerations of the unique attributes of space assets

Financing models

Space asset projects require substantial financial investment. Financiers may consider using the usual models of equity finance, secured financing and project finance.

However, particular risks and challenges of financing space assets should be considered.

- Using **project finance**, financiers can be repaid through income generated by the space asset, such as income from transponder leases on satellites or revenue generated by space tourism.

However, the challenges with taking effective security over the space asset should be considered when structuring the transaction, including the relevant applicable law and registration of the security.

- Under typical **secured financing**, given the practical difficulties with repossession of a space asset, the parties may agree for security to be taken over other valuable assets of the debtor on land, such as equipment, factories or intellectual property.

Financiers may also consider taking assignments over agreements ancillary to the operation of the space asset (such as transponder leases, service agreements and customer agreements) and requiring the control codes of the space asset to be held in escrow until an event of default.

Unique attributes of space asset financing

Space asset financing arrangements must take the realities of the industry into account. In particular:

- the **design, manufacture and testing** of a space asset is specialised and highly technical, often involving layers of contractors and sub-contractors. And once a space asset is in orbit, repair - and in the case of asset-based financing, **taking possession** - is virtually impossible;
- **delay and lengthy timeframes** are common. It can take two to three years to manufacture a space asset. Launch is then subject to launch range availability, launch vehicle readiness and the vagaries of weather; and
- **political and regulatory sensitivity** is required. Some jurisdictions view space activities primarily through a military or national security lens, and impose restrictions accordingly.

Accordingly, financiers must carefully structure their financing arrangements to account for these unique features.

CHINA'S SPACE
VALUE CHAIN IS
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- Euroconsult, *China Space
Industry Report*, 2018



Key point 4: Regulatory due diligence requires knowing the touchpoints and jurisdictions in play

Typical regulatory touchpoints

In addition to the usual checks that accompany financing, the launch of and operation of a space asset requires regulatory due diligence. This includes thinking about:

Launch and operations
licensing

Payload review and
registration

Orbital debris mitigation
approval

Radio-transmitter
authorisations

Orbital slot and
spectrum coordination

Import / export
compliance

Further complexity arises when space activities involve new technologies, utilise nuclear power sources and/or carry life (human or animal). Besides space-specific laws, these issues can engage, for example, laws restricting the financing of weapons of mass destruction, sanctions or dual-use goods restrictions.

Jurisdictional nexus

A project's jurisdictional nexus impacts its regulatory treatment and requires close examination.

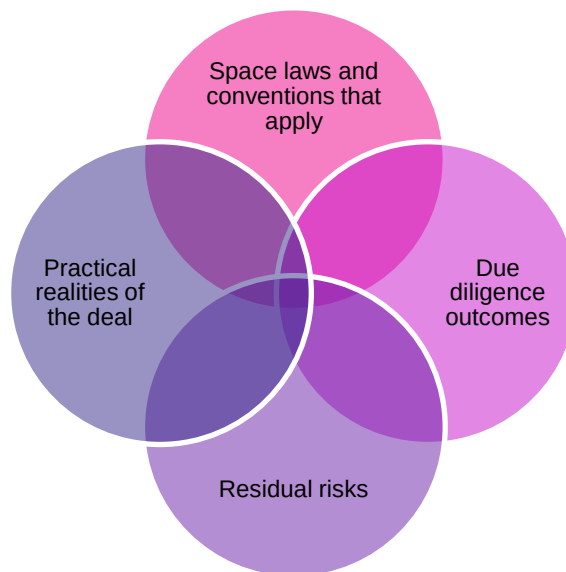
Questions to ask include:

- What is the provenance of the project assets?
- Where are relevant project companies involved?
- What is the nationality of any relevant individuals (eg crew)?
- Where will the launch take place?
- Where are the parties to the operation/service/customer agreements incorporated, and what is the governing law of these agreements?
- From which location will the payload be operated?
- Where are payments made or received?
- Is any international cooperation required? For example, to access technology or expertise, to transit assets or otherwise?

Financing parties should be cognisant of the potential impact of these regulatory issues on any space-related project. Some issues, such as launch licence rejection, mean that the project will (quite literally) be grounded.

Key point 5: Strong (space-specific) contracts are essential to protect financial interests

Contracts must be tailored to the project. This includes ensuring that the financing and security package takes into account:



The practical realities of the deal include the specifics of taking and perfecting appropriate security, appropriate conditions precedent (including realistic long-stop dates for any approvals), and even fundamentals such as time zones. The residual risks include those set out in **Key point 6**.

Transparency for financiers

In addition, a financier will need to ensure that they have access to all other relevant contracts, and (where necessary) that they can be assigned to them, upon the default of the creditor. The exact contracts in play for a space project will vary according to the structure and intended operations, but key documentation typically includes the following:

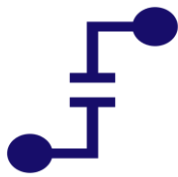
- **Launch services agreement:** Depending on whether delivery of the space asset will take place in space or on the ground, this agreement will be between the launch service provider and either the space asset operator or space asset manufacturer.
- **Space asset procurement agreement:** These agreements between the space asset manufacturer and the space asset operator often feature extensive limitations of liability.
- **Insurance policies:** Multiple policies are often needed to cover the pre-launch manufacturing, launch and in-orbit / operational phases. Domestic legislation may require that the policy include specific named insureds - usually the government licencing the relevant activity – before a licence can be granted.

Depending on the launch jurisdiction, various cross-waivers of liability may also be inserted by operation of law into these agreements. Transponder leases, utilisation agreements and other commercial documents will then fill out the suite.

Key point 6: Address residual risks

The residual risks will differ for each deal. They will generally only be fully scoped as part of due diligence and structuring.

Two common examples residual risk for space asset financing include the following:



Case study 1:

Hidden defects and barriers to recovery

Space is an extremely harsh operating environment. This means that a hidden defect in a space asset or its launch vehicle often has catastrophic affects.

While contractual protections and insurance can cover many eventualities, contractual limitations on liability – and the difficulties of determining liability remotely – can present obstacles to recovery.

This in turn can increase the chances of creditor default, and should be factored into a financier's assessments.



Case study 2:

Difficulty of taking physical possession

If a space asset is used to secure financing, the financier must pay particular attention to how they can take effective possession of that space asset once it is in space.

Similar to repossessing aircraft, this will often involve retention of command codes or similar control devices, but regulatory risk will also arise. For example, in the case of space assets, the national licences for the operation of that space asset will need to be transferred to the party taking effective possession.

This can theoretically be addressed in contract. However, in practice such transfer may not be possible. This may leave the financier without recourse against a creditor whose only valuable asset may be a space asset.

Key risk mitigation strategies

The key strategies for managing residual risks include the following:

- **Risk allocation** – as between the financier and borrower, and as between financiers if there are multiple.
- **Contract** – precisely drafted representations, warranties, undertakings and indemnities;
- **Security package** – a sophisticated approach to the security package to ensure that the right assets and payment flows are selected to support the assessed credit risk, with appropriate levels of third party support.
- **Collateral monitoring** – utilising specialists as necessary.
- **Proactive regulatory engagement** – where appropriate, comfort can be sought from national regulatory authorities regarding specific issues, such as licence transfers.
- **Dispute resolution forum** – evaluating pros and cons of arbitration over litigation, taking into account factors such as confidentiality, cost efficiency and enforcement procedure.

Please contact us if you would like to discuss your project. We would be delighted to help.

Key contacts



Katherine Ke
Registered Foreign Lawyer
(New York)
Hong Kong SAR
T +852 3443 8335
M +852 9198 7678
katherine.ke@hk.kwm.com



Urszula McCormack
Partner
Hong Kong SAR
T +852 3443 1168
M +852 6796 6130
urszula.mccormack@hk.kwm.com



Ma Feng
Partner
Beijing, China
T +86 10 5878 5588
mafeng@cn.kwm.com



Wang Ning
Partner
Beijing, China
T +86 10 5878 5276
wangning@cn.kwm.com



Peter Bullock
Partner
Hong Kong SAR
T +852 3443 1012
M +852 9104 5966
peter.bullock@hk.kwm.com



Neil Carabine
Partner
Hong Kong SAR
T +852 3443 1260
M +852 6656 1831
neil.carabine@hk.kwm.com



John Canning
Partner
Sydney, Australia
T +61 2 9296 2098
M +61 419 721 204
john.canning@au.kwm.com



Dale Rayner
Partner
Sydney, Australia
T +61 2 9296 2139
M +61 408 261 803
dale.rayner@au.kwm.com



Renae Lattey
Managing Partner, Clients and
Mergers & Acquisitions
Melbourne, Australia
T +61 3 9643 4065
M +61 417 214 795
renae.lattey@au.kwm.com



Annabel Griffin
Partner
Canberra, Australia
T +61 2 6217 6075
M +61 408 847 519
annabel.griffin@au.kwm.com

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Office locations

Asia

Beijing

18/F, East Tower World Financial Center
1 Dongsanhuan Zhonglu Chaoyang
Beijing, 100020, PRC
T +86 10 5878 5588

Chengdu

Suite 1603-6, Tower 1, Chengdu IFS
No.1 Section 3 Hong Xing Lu,
Chengdu, Sichuan, 610021, PRC
T +86 28 8620 3818

Guangzhou

25/F Guangzhou CTF Finance Centre
6 Zhujiang East Road, Zhujiang New
Town, Guangzhou,
Guangdong 510623, PRC
T +86 20 3819 1000

Hangzhou

D Region, 12/F Euro America Center,
No.18 Jiaogong Road, Hangzhou,
Zhejiang 310012, PRC
T +86 571 5671 8000

Haikou

34/F Tower A, HNA Internet Finance
Building, No.3 Guoxing Avenue, Meilan
Haikou Hainan 570203, PRC
T +86 898 3156 7233

Hong Kong

13/F Gloucester Tower
The Landmark
15 Queen's Road Central
Hong Kong, PRC
T +852 3443 1000

Jinan

18/F, Enterprise Square (Shangri-La
Office Building), No.102, Luoyuan Street
Jinan, Shandong 250000, PRC
T +86 531 5583 1600

Nanjing

32/F, One ifc, No.347 Jiangdong Middle
Road, Jianye District, Nanjing
Jiangsu, 210019, PRC
T +86 025 5872 0800

Qingdao

10/F, Hisense Building,
17 Donghaixi Rd., Qingdao,
Shandong, 266071, PRC
T +86 532 8579 0008

Sanya

7/F, Office Building, Plaza of CRREC,
165 Yingbin Road, Hedong District,
Sanya, Hainan, 572000, PRC
T +86 898 8820 9061

Shanghai

17/F, One ICC, Shanghai ICC,
999 Middle Huai Hai Road (M),
Xuhui, Shanghai, 200031, PRC
T +86 21 2412 6000

Shenzhen

28/F, China Resources Tower,
2666 Keyuan South Road,
Nanshan, Shenzhen
Guangdong 518052, PRC
T +86 755 2216 3333

Singapore

138 Market Street
#09-03, CapitaGreen
Singapore 048946
T +65 6653 6500

Suzhou

02A, 43/F West Tower, China Overseas
Fortune Center, 9 Suzhou Avenue West,
Suzhou Industrial Park,
Suzhou, Jiangsu 215021, PRC
T +86 512 6292 7100

Tokyo

21F, Marunouchi Nijubashi Building, 3-2-3
Marunouchi, Chiyoda-ku,
Tokyo 100-0005, Japan
T +81 3 5218 6711

Australia

Brisbane

Level 33, Waterfront Place
1 Eagle Street
Brisbane QLD 4000, Australia
T +61 7 3244 8000

Canberra

Level 5, Tower B
7 London Circuit
Canberra ACT 2601, Australia
T +61 2 6217 6000

Melbourne

Level 27, Collins Arch
447 Collins Street
Melbourne VIC 3000, Australia
T +61 3 9643 4000

Perth

Level 30, QV1 Building
250 St Georges Terrace
Perth WA 6000, Australia
T +61 8 9269 7000

Sydney

Level 61, Governor Phillip Tower
1 Farrer Place
Sydney NSW 2000, Australia
T +61 2 9296 2000

Europe

Brussels

Square de Meeûs 1
1000 Brussels, Belgium
T +32 2 511 5340

Frankfurt

KWM Europe Rechtsanwalts-gesellschaft
mbH, Taunusanlage 17
60325 Frankfurt am Main, Germany
T +49 69 505029 300

London

11th Floor
20 Fenchurch Street
London
EC3M 3BY, UK
T +44 20 7550 1500

Madrid

Calle Goya, 6
28001 Madrid, Spain
T +34 91 426 0050

Milan

Milano Largo Augusto 8
20122 Milano, Italy
T +39 02 30 31 751

Middle East

Dubai

401-404,
Gate Village 6,
Dubai International Financial Centre
Dubai, UAE
T +97 14 313 1700

North America

New York

50/F 500 Fifth Ave
New York City
NY 10110, USA
T +1 212 319 4755

Silicon Valley

535 Middlefield Road, Set 245
Menlo Park, CA 94025, USA
T +1 650 858 1285