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Key Vietnam project finance considerations in relation to the draft Law on Public-Private Partnerships

In March 2020, the Ministry of Planning and Investment (**MPI**) released a new draft of the Law on Public Private Partnerships (**Draft Law**) for public consultation.

The Draft Law aims to develop an improved enabling legal framework for public private partnerships (**PPP**) to promote private sector investments in large-scale energy and infrastructure projects in Vietnam, and it proposes numerous changes compared to the existing provisions of Decree 63/2018/ND-CP (**Decree 63**) issued by the Government of Vietnam in 2018. If passed by the National Assembly of Vietnam in May 2020, the long-awaited legislative instrument will become Vietnam's first-ever PPP law.

In this publication, we outline certain fundamental changes and key Vietnam law issues in the Draft Law.

1. General requirements

1.1. Eligible infrastructure sectors

The Draft Law specifically contemplates certain infrastructure sectors for PPP projects, including:

- transport;
- power plants, power grids;
- water supply systems, drainage and wastewater systems, waste treatment;
- office buildings for the State agencies;
- infrastructure for healthcare, education and training; and
- information technology infrastructure.

Compared to Decree 63, the Draft Law removes agriculture and rural developments from the eligible infrastructure sectors for PPP projects.

However, the Draft Law also makes it clear that this is not an exhaustive list, and infrastructure relating to other purposes which fall outside the list of those prescribed infrastructure sectors may also be covered subject to specific approval of the Prime Minister if it satisfies all of the following criteria:[1]

- the project falls within sectors prescribed in the Law on Public Investment;
- ability to be balanced in the State capital when delivered under PPP model; and
- being more commercially viable than public investment.

1.2. Authority to issue an in-principle investment approval

One of the first steps for the development of a PPP project is for project sponsors to obtain an in-principle investment approval. Depending on the size and sectors of the projects, one of the following authorities may issue an in-principle investment approval:[2]

- the National Assembly;
- the Prime Minister;
- the Ministries and/or central and local bodies; and
- the provincial-level People's Council.

Please see Appendix 1 to this publication for more details.

2. Contract structures for PPP concession

2.1. Types of Project Agreement

Unlike Decree 63, the Draft Law broadly contemplates three (3) distinct groups of concession afforded to project sponsors in the structuring and development of PPP projects in Vietnam:

- user pays: Build-Operate-Transfer (**BOT**), Build-Transfer-Operate (**BTO**), Build-Own-Operate (**BOO**) and Operate-Manage (**O&M**);
- Government pays in return for the use of infrastructure facilities: Build-Transfer-Lease (**BTL**), Build-Lease-Transfer (**BLT**);[3] and
- resources exchange for infrastructure: Build-Transfer (**BT**).

This is a welcome move from the Government, recognising the importance of availability payments over the life of the project subject to compliance with agreed performance criteria and standards to address demand risks. However, it appears that such fee structure of availability

[1] Article 5.2 of the Draft Law.
[2] Article 13 of the Draft Law.
[3] Article 46 of the Draft Law.

payments is intended for BTL/BLT delivery models for projects such as airports, toll roads and social infrastructure assets, and it will not be made available for IPP power projects, which are traditionally considered by the Government as a user-pays model.

The Draft Law also contemplates that the Government will issue model forms of project agreement for each group above.[4] However, it is not clear if the application of such model forms is mandatory for PPP projects.

2.2. Payment for Build-Transfer Contract

The Draft Law expands the type of public assets that can be used as payment for BT Contracts.[5] In particular, investors of BT Contracts may be paid in one of those forms:[6]

- by public assets in accordance with the Law on Management and Use of Public Assets;
- by the right to commercially operate and exploit other facilities and services; or
- by sales proceeds from the auction of public assets.

3. Selection of investors

3.1. Eligibility of investors

The Draft Law provides additional conditions to be satisfied by an eligible investor of a PPP project, including: [7]

- the investor is not debarred from PPP investment activities;
- the investor must associate with investors of private sectors to participate in bidding, if it is a wholly State-owned enterprise; and
- investors established according to foreign laws must meet market accessibility conditions when participating in bidding for projects of conditional market accessibility sectors and fields subject to laws and regulations of investment.

3.2. Investors selection

The Draft Law provides for three (03) methods for selection of investors of PPP projects, including:

[4] Article 48.2 of the Draft Law.
[5] Pursuant to Article 34 of Decree 63, the State may only use (i) land use right, right over buildings or (ii) commercial rights, operation rights to pay for BT projects.
[6] Article 46.3 of the Draft Law.
[7] Article 31 of the Draft Law.

- direct appointment.[8]
- competitive negotiation: This is a new selection method under the Draft PPP Law. Accordingly, the competent authority will only invite certain qualified investors to participate in the selection. Competitive negation is applied to (i) projects related to the national defense and security[9] or (ii) projects having high-level technology.
- public tender: This method is applied to all PPP projects which do not fall within the scope of direct appointment or competitive negotiation.

We note that in case a project with specific conditions is not likely apply any of the above methods, the competent authority may report to the Prime Minister to consider and decide a method of investor selection.

Unfortunately, the Draft Law does not clearly set out the competent authority for the investor selection in each applicable case.

4. Project Company

4.1. Restriction on conducting alternative businesses

The Draft Law prohibits a project company, typically structured as a thinly capitalised special purpose vehicle (**SPV**) on a limited or non-recourse basis, from entering into alternative business activities that fall outside of a PPP project. On a strict interpretation, it may not introduce any change from the present definition of a special purpose entity duly established to enter into a project agreement with authorised State agency (**ASA**).

4.2. Statutory minimum equity funding requirements

Successful development and commercialisation of major PPP infrastructure projects in Vietnam are primarily funded by a mix of equity finance and multi-source financings.

The Draft Law expressly requires that the equity component of a PPP project must be at least 15% of the total investment capital expenditure of the project (excluding State capital on construction of support facilities or site clearance).[10] As a practical matter, we would typically see debt to equity ratios of 80/20 or 70/30 in the Vietnam project finance context.

Other sources of funding are typically mobilised through shareholders loans from sponsors and multi-tranche syndicated senior secured debt facilities from domestic and international lenders. Determination of viability gap funding and Government participation are key issues to note.

[8] This method is for (i) projects serving the national defense and security, state secrets; or (ii) projects with urgent needs to ensure the continuity in providing public products or services.
[9] In this case, the selection must have the opinion of the Ministry of National Defense or the Ministry of Public Security.
[10] Article 78 of the Draft Law.

The Draft Law requires that a PPP project must have a total investment capital of no less than VND200 billion (approximately USD8.5 million). However, this limitation will not apply to Operate-Manage (O&M) projects.[11]

4.3. Statutory timeline to achieve financial close

The Draft Law imposes a particular requirement for sponsors and the project company to achieve financial close within 12 months (or 18 months for projects which an in-principle investment approval was approved by the National Assembly or the Prime Minister) following the execution of a project agreement.

This is likely to be a risk area for lenders and sponsors as they will be effectively under time pressure to negotiate and execute financing documents and then achieve financial close within such tight statutory timelines, particularly in light of protracted commercial negotiations by parties over the years in previous power projects in Vietnam.

4.4. Project bond offerings [12]

In terms of types of debt instruments, the Draft Law contemplates the possibility of the project company to mobilise debt funding by way of bond private placement offerings to qualified securities investors. It is note-worthy that the debt finance raised through the private placement offerings must not be higher than the debt component of the PPP project provided under the PPP contract.

The project company may also conduct public placement if it has completed the construction stage or has moved to the operation stage (if the project does not include the construction stage).

We note that:

- the bonds in question are exclusive of convertible bonds or bonds with warrants; and
- the bond proceeds will only be used for funding the development of the PPP projects.

4.5. Governing law of project documents

English law has been the most common foreign law typically selected by parties for financing documents, including facility agreements and intercreditor agreements, and certain Government-guaranteed project documents, including a project agreement, long-term supply and offtake agreements, in previous Vietnam IPP power projects.

Unlike the previous approach of Decree 63, the Draft PPP Law contemplates the mandatory application of Vietnamese law as the governing law of a project agreement and certain key project documents.[13]

[11] Article 5.3 of the Draft Law.
[12] Article 79 of the Draft Law.
[13] Article 57 of the Draft Law.

The taking of security over Vietnam-based assets will generally be governed by Vietnamese law.

4.6. Investment incentives and guarantees

In addition to incentives listed under respective laws and regulations on investment, law on tax, law on land, some of preferences that the project company may enjoy include:

- priority right to provide public services: in special cases, the project company may have the priority to provide public services or to use public construction to implement the project;[14]
- right to grant mortgage over assets or commercial rights.[15]

5. Government support

5.1. Guarantees on foreign currency availability [16]

The Draft Law now formally recognises the requirements of the Prime Minister's Official Correspondence 1604/TTg-KTN issued in 2011 for coal-fired IPP power projects to the effect that the Government guarantees on foreign currency availability for the development of large-scale energy and infrastructure projects in Vietnam will be no more than 30% of project revenue in the local currency Vietnam Dong after subtracting expenditures.

Such cap on foreign currency risks has been one of key bankability issues from lenders' perspective, and it remains to be seen how international lenders will price this risk exposure for upcoming PPP projects in Vietnam.

5.2. Risk sharing mechanism for minimum revenue [17]

Of particular note, the Draft Law contemplates a risk sharing mechanism between sponsors/project company and the Government, particularly:

- If actual revenue is lower than contracted revenue which is contractually agreed by the parties in the project agreement, the Government agrees to bear 50% of the shortfall provided that numerous requirements are met.

  However, this risk allocation will only apply for the State-proposed BOT, BTO and BOO projects. In other words, O&M, BLT, BTL and BT projects are not entitled to enjoy the risk allocation.
- In contrast, if actual revenue is higher than contracted revenue, investors will share 50% of increased revenue with the Government.

[14] Article 81.2 of the Draft Law.
[15] Article 81.3 of the Draft Law.
[16] Article 82 of the Draft Law.
[17] Article 83 of the Draft Law.

6. Restriction on the transfer of project

A new challenge is presented in the Draft Law by attempts of the Government to place a statutory restriction on the right of sponsors to transfer its equity interest in a PPP project to a third party, and such transfer is not possible until completion of construction.

This move is seen as attempts of the Government to avoid any sale of equity to unqualified investors and minimise construction delays following prolonged project delays that occurred recently in other large-scale power projects.

Key contacts

If you have any questions or would like to know how this might affect your business, please contact these key contacts.

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Legal notice

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Appendix 1

The authority to decide and issue an in-principle investment approval

Competent authority	Scale of the project
National Assembly	• Projects have the public investment capital over VND 10,000 billion. • Projects have substantial impact or posing potential risks to the environment. • Projects require land use purpose conversion of more than 500 hectares of land for growing rice. • Projects require the resettling of 20,000 inhabitants in mountainous areas or at least 50,000 inhabitants in other regions; or • Projects require special legal frameworks or policies under the National Assembly's resolutions.
Prime Minister	• Projects require the resettling of 10,000 inhabitants in mountainous areas or at least 20,000 inhabitants in other regions. • The projects use the central budget capital, ODA, etc. • The projects for construction of international airport or airport with the capacity over 1 million ton per year. • The projects for construction of special seaports, seaports with the total investment capital equivalent to Group A project under the Law on Public Investment. • The projects have the total investment capital over VND 10,000 billion. • The BT projects with the total investment capital of Group A project.
Ministries or equivalent authorities	Other projects under the authority/ management of the Ministries.
The Provincial People’s Council.	Other projects located in the province.

Appendix 2

PPP Project Development