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Enabling Infrastructure Investment

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Vietnam: Capacity Building Program for Promoting Private Sector Participation

REFERENCE GUIDE ON KEY ISSUES

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EXECUTIVE SUMMARY

Background: The Government of Vietnam seeks to address its growing infrastructure needs by way of Public Private Partnerships (PPP). Currently the Ministry of Planning and Investment (MPI) is close to finalizing a "Decree on PPP Investment" (Draft Decree) on the instruction of the Office of Government, with a goal that the Draft Decree be enacted in July 2014.

On 20 May 2014, MPI circulated to its consultants and development partners a revision to draft number four of the Draft Decree that was expected to reflect continued input from consultants, investors, public sector stakeholders and development partners. **It should be noted that the Draft Decree is not yet finalized, as of the date of this document.**

During the period of 26 May through 6 June 2014, PPIAF in association with JICA sponsored a series of legal and financial trainings for members of central and local government bodies from Vietnam, under the title:

Vietnam: Capacity Building Program for Promoting Private Sector Participation

Purpose of this document: This reference guide addresses some of the key issues discussed during PPIAF and JICA supported trainings for participants from central and local government bodies of Vietnam. Although the Draft Decree remains to be finalized, many of the concepts discussed in this reference guide may be useful to participants in the training regardless of the final outcome of the Draft Decree. This reference guide is structure as follows:

Unit 1 introduces the need for PPPs in Vietnam

Unit 2 sets out the core concepts for PPPs in Vietnam

Unit 3 identifies key success factors for PPPs, building on Unit 2

Unit 4 places the Draft Decree into the larger context of Vietnam's recent legal reforms

Unit 5 introduces the PPP project cycle

Unit 6 illustrates how transaction advisors assist the ASA during the PPP project cycle

Unit 7 compares the roles of the public and private sectors in PPPs

Unit 8 addresses principles of risk allocation between the public and private sectors

Unit 9 addresses project preparation including project screening, project proposals and feasibility studies

Unit 10 discusses the need for project management for PPPs

Annex 1 presents a brief case study on how value for money was achieved on a mine wastewater project

Unit 1: Introduction to the need for PPP in Vietnam

Competition for investor monies is growing amongst countries in similar economic development stages to Vietnam. In recent years, private sector investment in Vietnam has begun to fall behind the country's growth plans. According to the Ministry of Planning and Investment, Vietnam needs US$170 billion in new infrastructure investment from 2010 through 2020 to fuel continued growth of its economy. Private sector investments are anticipated to cover approximately 50 per cent of such investment (about US$8.5 billion per year). Unfortunately, these investment targets are not being fully achieved. In 2012, it is reported that the total amount of foreign direct investment across all investment sectors amounted US$16.3. Of which, US$3 billion was directed to infrastructure investment.

There have been a number of legal and systemic issues that have slowed the development of Vietnam's needed infrastructure including:

- Lack of clarity in key regulations governing private sector infrastructure investment such as Decree 108 and Decision 71
- Unclear decision making pathways delaying resolution of key terms of contract negotiations
- Lack of capacity by Government negotiators on issues raised in complex project development and financing stages
- Over-reliance on direct contracting and the lack of competitive pressure in selecting investors
- Failure of some investors to implement projects that have been awarded to them
- Systemic bankability constraints such as lack of clarity on lender security, unavailability of guarantees and currency conversion issues

These factors lead to extraordinarily long negotiation periods, averaging more than five years to go from selection of investor to signing of the concession contract. Thus the Government of Vietnam has called for dramatic legal reform, including the development of a new legal framework promoting PPPs, to move beyond the above hurdles to investment.

PPP is a proven model across a number of countries that has usually delivered needed infrastructure faster and at a lower price than traditional procurement. The PPP model and methodologies look to optimize the balance between public sector debt and private sector investment. Although many of the concepts are new for Vietnam (and will require Authorized State Agencies (ASAs) to learn and try new methods of procuring projects), they are well tested across a number of markets, including many countries in a similar stage of development as Vietnam.

This reference guide discusses the current status of Vietnam legal framework and introduces main concepts for developing projects under the Draft Decree based on international best practice.

UNIT 2: CORE CONCEPTS FOR PPPS

This unit identifies some of the key PPP concepts that should be commonly understood by public and private sector stakeholders in order to implement a successful PPP program in Vietnam.

PPP definition: Public Private Partnership (PPP) is a method of procurement between the public and private sector to utilize the innovation of the private sector and achieve Value-for-Money in the provision of public services. Under a PPP contract, the private sector shall provide infrastructure and other public services and is permitted to earn profits from the provision of the services.

The Draft Decree provides the following definition for PPP:

> "**Public Private Partnership Investment Form** means the implementation of Projects based on a contract between an Authorized State Agency and an Investor to implement investment, construction, management and operation of infrastructure facilities, and provision of public services." (Article 3.1)

Project Cycle: A predictable step-wise process to develop a project starting from project identification (screening) and leading toward financial close.

The purpose of the PPP project cycle is to:

- Provide a proven and consistent approach to developing infrastructure projects
- Make the development of projects predictable and understood to both public and private sector stakeholders
- Reduce inefficiency and corruption

The Draft Decree does not refer specifically to "project cycle", but rather different steps of the project cycle are provided for in Articles 16 to 19 and Articles 26 to 33. These steps comprise of:

- Project screening (initial selection of project)
- Project Proposal
- Formulation of Project List
- Announcement of Project List
- Formulation of Feasibility Study Report
- Approval of Feasibility Study Report
- Selection of Investor
- Project Contract signing

Value for money (VfM): Although "value for money" is not a recognized legal term in Vietnam, the concept is a central pillar of the PPP model. The principle behind Value-for-Money is to ensure that the users are provided, to the highest possible standard, with the services they requires at the lowest possible costs to the State. According to PPIAF, VfM means the optimal combination of benefits and costs, in delivering services to meet user's requirements.[1]

The Draft Decree does not clearly contemplate VfM. It sets out an investment principle as "encouraging competitiveness, creativity, experience and resources of Investors, thereby enhancing investment efficiency, ensuring that goods and services are provided to the satisfaction of requirements and benefits of users".

Facilities vs. Services: Infrastructures and facilities are designed to provide a service to users. The key outcome of a PPP Project should be conceptualized as the delivery of necessary public services, which encompasses the provision of infrastructure and facilities to achieve the service provision goal.

Competition: Competition is critical to the delivery of value for money and further innovation. The state can benefit from lower costs through competition. In international practice, a solicited project must be procured through competitive bidding. For unsolicited projects competitive bidding is recommended by means of the "Swiss Challenge" or other forms of competitive pressure.

Risk allocation: Another goal of PPPs is efficient and effective risk allocation between the public and private sectors. Risks should be allocated to the party who is best able to manage and mitigate the risks.

Bankability: This refers to the Project's ability to obtain credit support from lenders. Lenders generally require borrowers to put into place various means to mitigate all risks which may result in the borrower being unable to repay its loans. When lenders are willing to lend on the basis that a project is properly structured and risks (to repayment of the loan) are mitigated, then a project is said to be "bankable." Key bankability factors typically sought by lenders include:

- Foreign currency convertibility: revenues of projects are fully convertible to an international hard currency and fully remittable to a foreign country
- Step-in-rights: lenders have the right to take over the Project or replace an operator in the event of a default by the investor/borrower
- Rights to mortgage: the investor may grant to the lenders a mortgage on assets or business rights of the Project

1 World Bank Institute - PPIAF, Public-Private Partnerships, Reference Guide, version 1.0, page 138.

- Governing law: the Project contract and other relevant contracts (such as loan agreements) are governed by neutral but well understood (foreign) law upon agreement by the parties to the contract
- Dispute resolution: The parties may contractually agree to the venue of dispute resolution, including a foreign arbitration process.

Project Proposal: Analogous to a pre-feasibility study, a project proposal assesses whether a project is suitable to be implemented as a PPP, taking into consideration whether it offers a greater benefit-to-cost ratio to the State, when compared to traditional public procurement.

Under the Draft Decree, the criteria for selecting the project ("**Project Selection**") to formulate the Proposal are as follows:[2]

- Conformity with the investment sectors, contract form and investment principles
- Capability of attracting capital resources, technology and adequate managerial experience of the Investors
- Capability of delivering services, which meet quality standards and users' needs
- Enhancement of the efficiency of State capital resources
- Capability of recovering investment capital and reasonable profits for the Investors from the revenue of the Project (including State participating Portion)

According to the Draft Decree, the contents of the Project Proposal must confirm:[3]

- Conformity of the Project with the development master plans and the requirements for Project Selection
- Necessity to implement the Project, outlining the advantages of proceeding under the PPP model
- Estimated Project target, scale, components, implementation location, demand for land use and quality standard requirements
- Estimates of the total investment capital, capital sources and bankability of the Project
- Preliminary estimate of the State Participating Portion and other forms of State supports and guarantees (if any)
- Estimated timeline and schedule for Project implementation (including timeline for construction and operation of the facility)
- Anticipated preliminary financial plan of the Project (including anticipated user fees)
- Preliminary analysis of risks in Project implementation and risk allocation between ASAs and investors
- Preliminary analysis of the Project's efficiency and its impact on the environment, society, security and national defense

2 Clause 2, Article 17 of the Draft Decree
3 Article 23 of the Draft Decree

- Other anticipated contents for Project in specific sectors (such as conditions for implementing auxiliary projects under BT contract)
- Costs for Project implementation and the anticipated revenue sources.

Feasibility Study: The PPP feasibility study differs from the feasibility study traditionally used in Vietnam. The purpose of a PPP feasibility study is to determine the optimal financial and legal structure, desired technical output and the financial viability of the Project. More specifically, a feasibility study comprises the following analysis:

- Determine if the project will deliver Value for Money for the State
- Specify the optimal financial and legal structure necessary for delivering the project, maximizing VfM
- Outline the desired technical outputs
- Quantify the level of State support needed to make the project Financially viable

The Draft Decree contemplates the following requirements for a feasibility study report:[4]

- Detailed analysis and assessment of the Project's necessity and conformity with the investment master plan and conditions for the Project Selection (Please refer to Project Selection above)
- Detailed analysis and determination of the Project's targets, scale, components and implementing location; market demand and affordability; demand for land use, and plan for land clearance and resettlement (if any)
- Analysis of technical specifications and minimum technology solutions to ensure that the quality of Project facilities and services meet users' needs
- Detailed analysis and assessment of the Project's: implementation schedule and term; time-frame for Project construction and exploitation; plan for management and operation; assets status assessment (for O&M contracts)
- Detailed analysis and assessment of risks, as well as the parties' obligations on risk management during implementation
- Determination of Project contract type
- The Project's financial plan, including estimated total investment capital and revenues
- Expected State Participating Portion and other forms of State support as well as investment incentives

Project Approval: Following the feasibility study, the key structural, technical and financial elements of the Project will be defined in the Project Approval phase.

The following items need to be approved before going to investor selection:

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[4] Article 27 of the Draft Decree.

- The expected outputs of the Project
- The proposed contract form
- The financial structure of the Project
- State Participating Portion
- Payment structure
- Land acquisition costs
- State support and guarantees
- Key commercial terms

The Draft Decree does not specify a distinct Project Approval stage. Instead, it contemplates an approval of the feasibility study report. Under the Draft Decree, the following elements should be appraised by the competent authority reviewing the project:

- The need for the Project
- Basic elements including scale, location, design, technical/ technological requirements and plans for operation and management
- The efficiency of the Project
- The financial plans including total investment capital, revenues, capital mobilisation and the State Participating Portion

State Participating Portion: see explanation of Viability Gap Funding.

Payment structure (user fees base vs. availability payment): The Draft Decree specifies two primary payment methods to investors:

User Fees under BOT type contracts, whereby the investors recovers investment capital and profits from a payment stream obtained by users; and

Availability Payments under BTL contracts, which are paid in circumstances where user fees are difficult for the investor to obtain and, instead, the State makes regular payment for the output of the services.

Viability Gap Funding (VGF): VGF is not defined in Vietnamese law. In international practice, it is defined as support from the State to a Project to ensure the Project is financially viable. Normally, VGF may take the form of capital contribution to construction costs or subsidies for the operation stage of the Project. In the Draft Decree, the analogous concept to VGF is referred to as the State Participating Portion.

The following are examples of other countries' applying VGFs for PPP projects.

INDIA

In India, VGF may be granted up to 40% of build-operate-transfer projects. Key conditions related to the eligibility for VGF grant include:[5]

- The Central Government may cover up to 20% of project cost, and the State (where the project is located) may co-finance another 20% of project cost from its own revenue base.
- The project must be 51% owned by the private sector and the grant can only be used during the construction.
- The project is the direct beneficiary of the grant.

Regarding VGF granting procedures: Approval of the grant occurs before the bidding takes place. PPP equity must be disbursed entirely first, before VGF is disbursed. Subsequently, VGF will be disbursed proportionately to the release of debt.[6]

PPP projects must meet certain requirements as follows:[7]

- The viability gap through the use of the tariff (for reasons of affordability) cannot be eliminated; and
- lengthening the project term will not solve the problem.

The Department of Economic Affairs of the Government of India has recently approved a viability gap funding grant for a metro railway project in the city of Hyderabad, Andhra Pradesh, of about $244 million, which constitutes 12.35 per cent of the total cost of the project.[8]

INDONESIA

In 2013, Indonesian Government began developing a VGF scheme to support the involvement of PPP in infrastructure investments. [9] Like the Indian model, projects must meet several conditions in order to receive funding, such as:

- a minimum investment of about $100 million;

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5 Policy Brief: *Government share of PPP costs and risks*, prepared for Philippines PPP Center under ADB's capacity building technical assistance, p.31-32. Link: http://ppp.gov.ph/wp-content/uploads/2013/01/Government-Share-Incorporating-VGF-Final-Draft-as-of-16-Jan-2013.pdf

6 Ibid.

7 See India, Planning Commission, Guidelines: Financial Support to Public Private Partnerships in Infrastructure (New Delhi, Secretariat for the Committee on Infrastructure, 2005). Available from www.infrastructure.gov.in/pdf/Finance.pdf.

8 Major issues in transport: *Innovative financing options for regional infrastructure development and maintenance*, No. E/ESCAP/FAMT(2)/4, UN Economic and Social Council, p.8.

9 Indonesia country report submitted to the third Asia-Pacific Ministerial Conference on Public-Private Partnership for Infrastructure Development, Tehran, 11-14 November 2012.

- projects must be based on the "user pays" principle; and
- all other options have been discounted.[10]

BANGLADESH

In Bangladesh, VGF includes capital grants, annuity payments or both, for up to 30 per cent of a build-operate-transfer project, excluding the cost of land.[11]

KOREA

In the Republic of Korea, construction subsidies, which act as VGF, can reach between 25 and 30 per cent for roads; 30 and 40 per cent for ports; and up to 50 per cent for railways, provided that these subsidies are required to keep user fees at an affordable level.[12]

Minimum Revenue Guarantee (MRG): This is a form of guarantee whereby the State bears the demand risk of the Project. The Minimum Revenue Guarantee ensures that if demand is too low, the investor will receive payment to make up the revenue gap of the project, the purpose of which is to ensure a reasonable rate of return to the investors. MRG is considered where demand is outside the control of the investor and the State agrees to take the risk on demand and promoting greater demand for the service.

From 1999 to 2009, the Korea has implemented a mechanism of minimum revenue guarantee, whereby part of the projected revenue was guaranteed by the State. In the road sector for example, the government of South Korea offered guarantees to the revenues for a minimum number of vehicles at an agreed toll level.

The following terms were considered by the Government while granting guarantees:

- The period for which the guarantee was provided;
- the proportion of the projected revenue that was guaranteed;
- the conditions attached to the guarantee; and
- the application of the mechanism to unsolicited projects as compared to solicited projects.[13]

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[10] See Freddy R. Saragih, "Role of Ministry of Finance to promote PPP infrastructure development". Available from www.jica.go.jp/press/2012/ku57pq000012e8t8-att/20130124_02_04.pdf.

[11] Bangladesh, "Guideline for Viability Gap Financing (VGF) for Public-Private Partnership (PPP) Project". Presentation made at the Indonesia PPP Infrastructure Investment Forum – Issues and Outlook for PPP Infrastructure Development in Indonesia, Tokyo, January 2013. Available from www.pppo.gov.bd/download/ ppp_office/Guideline-for-VGF-PPP-Sep2012.pdf.

[12] Major issues in transport: *Innovative financing options for regional infrastructure development and maintenance,* Op. cit., p.8.

[13] Case Study developed by Foster Infrastructure, November 2013. Source information: Hyeon Park, "Government Support for PPP Projects in Korea", Korea Development Institute (November 2012). Link:

In 2006, minimum revenue guarantees applied only to solicited projects for a period of 10 years (in which the maximum guarantee level is 75% for the first 5 years and 65% for the next 5 years).[14]

However, the mechanism was deemed too generous and caused considerable pressure on the national budget. At the end of 2008, approximately $1.2 billion had been paid by the Government of Korea in the form of minimum revenue guarantee subsidies.[15]

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https://wpqr4.adb.org/LotusQuickr/copmfdr/PageLibrary482571AE005630C2.nsf/0/413E3BDF18727C5E48257C3C001DE055/$file/PPP%20Case%20Study%2013%20%20South%20Korea_s%20Minimum%20Revenue%20Guarantee%20Mechanism_RFoster.pdf

[14] Ibid.

[15] Jay-Hyung Kim and others, *Public-Private Partnership Infrastructure Projects: Case Studies from the Republic of Korea - Volume 1: Institutional Arrangements and Performance* (Mandaluyong City, Philippines, Asian Development Bank, 2011). Available from www.adb.org/sites/default/files/ppp-kor-v1.pdf (Case Studies from Korea - Volume 1).

Building on the issues raised in Unit 1 (the need for PPP) and the concepts presented in Unit 2 (core principles of PPPs) this Unit identifies the key success factors needed for Vietnam's PPP program. Through the Draft Decree and various circulars and efforts to implement it, Vietnam's PPP program fundamentally needs incorporate the following success factors:

Achieving better Value-for-Money

A Value-for-Money (VfM) ethos is core to a successful PPP program. Recall that Value-for-Money is the relationship between the quality and quantity of infrastructure provided by a private partner, and the risks and price to the government and infrastructure users. It is believed that well-structured PPPs can offer better VfM than using traditional procurement or direct public provision. As ASAs look at projects, they should take an objective view on whether the project will actually delivery VfM as a PPP or would be better placed as a traditional public procurement. It is not unusual for authorities (e.g. ASAs) to become more concerned with finalizing a project they have already started than to take an objective assessment of whether the project is actually in the best interest of the State and delivers the desired VfM.

Private participation in infrastructure through the PPP modality can create VfM for Vietnam and the government in a number of ways, including:

- Bringing private innovation, expertise, and management to infrastructure
- Better project management including project delivery on-time and on-budget
- Optimized project design, investment, maintenance, and operations
- Better customer orientation
- Mobilization of private financing
- Better realization of commercial potential of infrastructure
- More efficient and cost-effective management of certain risks (such as construction risks)

To realize Value-for-Money from private participation, the government needs to focus PPP projects on an output basis with appropriate risk transfer, lifecycle contracting, competitive procurement of private partners, and effective post-contract oversight. The government role is crucial in the structure, procurement, and oversight of PPPs, and will put in place specialized support in this regard.

The Government's approach to VfM assessment varies from country to country. For example, Canada and United Kingdom require VfM assessment for all PPP/PFI projects and issued VfM assessment guidance to procuring authorities. The UK HM Treasury's Value for Money Assessment Guidance (2006 version) requires 3 stage assessment for a PPP/PFI project, including:[16]

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[16] UK HM Treasury's Value for Money Assessment Guidance, November 2006, p.5.

- **Stage 1 – Program Level Assessment** to ensure that PFI is only considered for use in those programs where it is appropriate and is likely to represent good VfM;

- **Stage 2 – Project Level Assessment** requiring an upfront procurement appraisal at Outline Business Case (OBC), which replaced the previous Public Sector Comparator (PSC) and identifies the aspects that are key to VfM; and

- **Stage 3 – Procurement Level Assessment** which is an ongoing assessment during the procurement phase of a project to ensure that the desired project can be delivered in view of, for example, the competitive interest and market capacity.

Meanwhile, requirement of VfM analysis in Chile is limited to social sector PPPs that will be paid for by Government availability payments. It is noted that user-fee projects are deemed more politically and socially feasible under a PPP and do not require VfM.[17] Similarly, in France, VfM analysis is only required for "partnership" contracts, user-fee projects are not required VfM analysis.[18]

Risk allocation and management between public and private sectors

PPP arrangements are long-term contracts that commit the government to certain obligations, payments and direct and indirect risks over many years. Some PPP projects will require additional support in the form of subsidies and/or guarantees. Typically, the level of necessary state support is assessed prior to the project going to tender. PPP contracts should be developed on the basis of fair and economically reasonable risk allocation (including government-side fiscal obligations), and such allocation should be reconfirmed prior to the contracts being signed.

As such, the government shall place attention on fiscal affordability, appropriate risk structuring and risk management.

Transparency and fairness in procurement process

To date many projects have been identified and developed by the private sector on an unsolicited or direct contracting basis, in which the private sector has identified projects, conducted project feasibility and structuring work, and negotiated directly with the government.

Under the PPP framework, the government should play a larger role in identifying projects, undertaking feasibility and structuring work, and offering these projects to the market. This will require more capacity in government and specific measures are proposed to provide this. For delivering the best Value-for-Money, greater emphasis must be placed on selecting private partners through open, transparent and competitive procurement procedures meeting international standards.

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17 Value-for-Money Analysis - Practice and Challenges: How Governments Choose When to Use PPP to Deliver Public Infrastructure and Services, May 2013, PPIAF, the World Bank, p.17.

18 Ibid.

Transparent, efficient and predictable procurement processes are critical to give investors confidence in the overall PPP program, which in turn has significant cost and risk implications.

Reducing the cost and risk to bidders broadens investor interest in a country's PPP program and also lowers the risk premium applied by investors (e.g., for country / political risk) resulting in attracting higher quality investors. This increases the competitive forces during the tender process and ultimately reduces the cost of delivering infrastructure / public services.

Greater efficiency may be achieved by providing pre-approved and tested (e.g. tested for bankability) contract forms to bidders as a part of the bid documentation—against which the potential investors bid. To this end, standardized contractual terms and project agreements also benefit the government and government contracting counterparties (ASAs) in monitoring and managing contracts through the implementation of PPP transactions and the delivery of infrastructure and public services by the private contractor.

A typical example is South Korean case where the procurement process is supported by a solid legal framework consisting of the PPP Act, the PPP Enforcement Decree, and the PPP Basic Plan. This structure allows consistency and transparency. The clearly defined procurement processes and roles of related government bodies in the South Korea are advanced distinguished from the procedures in some developing countries.[1]

Beside the PPP Act, PPP Enforcement Decree, and PPP Basic Plan, PIMAC, the Korean PPP Unit, has developed PPP implementation guidelines to improve transparency and objectivity in PPP implementation, such as (i) a guideline for the VfM test, (ii) guideline for request for proposal preparation, (iii) guideline for standard output specification by facility, (iv) guideline for tender evaluation, (v) guideline for a standard concession agreement, and (vi) guidelines for refinancing.

The supreme audit institution of Korea is known as the "Board of Audit and Inspector" (BAI), which ensure that administrative practice and exercise of government and public bodies are fair, reasonable and appropriate. BAI provides independent oversight of the PPP process, auditing practices (specifically in terms of procurement) of the line agency. Normally, reports of supreme audit institution to the Parliament may keep the public informed about the services that they receive and also spread best practice.

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Source:

Public–Private Partnership Infrastructure Projects: Case Studies from the Republic of Korea, volume 1: Institutional Arrangements and Performance. Attachment: Global Country Comparison of Public–Private Partnership Frameworks and Projects, p.71, Edited by: Jay-Hyung Kim, Jungwook Kim.

Organizations enabling Public Private Partnership: An Organization Field Approach, Stephan F. Jooste and W. Richard Scott, October 2009, p.28.

Recommendation of the Council on Principles for Public Governance of Public-Private Partnerships, May 2012, OECD, p.40.

Common institutional characteristics of successful PPP Programs

Among the determining factors of successful PPP projects, public institutional setting is one of the most important factors. Countries with strong public sector institutions have typically performed best. Examples include the United Kingdom, South Africa, Australia, South Korea and Chile.[19] Key common institutional characteristics of successful PPP programs includes, among others, the following:

- *Single Window for Investor Acces*s
  The implementing agency, often a professional PPP unit, is authorized to lead the implementation of the PPP project and make or procure decisions during project selection, tendering and negotiation of the deal

  Examples of PPP unit across the world include:

  - United Kingdom: PPP Policy Team
  - South Africa: National Treasury PPP Unit (unit within the National Treasury)
  - Australia (Victoria): Partnerships
  - South Korea: Public and Private Infrastructure Investment Management Center (PIMAC)

- *Unified political support for the program*
  Ministries, agencies, and other government stakeholders are aligned for a common purpose to achieve implementation of the PPP program and its projects. Implementing agencies are not to compete for projects or to develop "their own PPP program".

  Below is an example of the public institution setting in South Korea:

  - The Ministry of Strategy and Finance (MOSF) is the "control tower" for national PPP programs (large-scale projects) and chairs the PPP Review Committee (PRC), which consists of members from procuring ministries and private sector experts. As the budget authority, the MOSF has been able to induce procuring ministries to utilize the PPP method where appropriate in the budget allocation process.
  - The PRC, chaired by MOSF, convenes whenever needed to make important decisions on PPP policies and major projects.
  - Procuring ministries are in charge of developing sector-specific PPP plans and implementing projects. In other words, individual projects are implemented and administered by each procuring ministry. MOSF exercises control through public expenditures in the implementation stage. Ministries are required to spend within the limits set in the budget implementation plan. When deemed

[19] Vickram Cuttaree, "Key Success Factors for PPP projects: Based on International Experience", World Bank presentation in St. Petersbug, 22 May 2008.

necessary, the MOSF is able to postpone or block part of the expenditures for PPP projects.

- PIMAC (PPP unit) played an important and independent role in the process of PPP project procurement and policy development. By being involved in various stages of PPP procurements, PIMAC has contributed to the success of the PPP program by assisting the public and private sectors and promoting infrastructure projects.

- *Strong public sector transaction management skills*
  Implementing agencies have sufficient staff, resources, and skill sets to select, prepare, negotiate, and monitor a complex, multi-stakeholder PPP project.

Government guarantees and other forms of support

International investors in a developing PPP market, such as Vietnam, will be concerned about risks they cannot control such a counterparty risk (e.g. credit risk) and demand risks. These risks can be mitigated to a large extent through provision of payment guarantees or minimum revenue guarantees, or through the selection of counterparties holding a minimum credit rating. Lenders will typically require that counterparty risk and demand risk be mitigated through government guarantees. Bankability of a project may also depend on the availability of other forms of government support such as the prior acquisition of land rights.

Payments of Government guarantees are generally sourced from State budget as allocations from the Ministry of Finance. An issue is that budgeting allocation is planned for short-term periods. For example, budget planning in Vietnam is for a period of maximum 5 years, while the concession terms typically last for at least 15 or 20 years. On the other hand, contingent liabilities are always difficult to project in State budget planning.

To address the difficulty of planning contingent liability into a State budget, some countries have opted to set up a central contingent liability fund to provide resources for guarantees.

> For example, Korea has established the Korea Infrastructure Credit Guarantee Fund (KICGF), which commenced its operation in 1995 in accordance with Private Participant in Infrastructure (PPI) Act and Korea Credit Guarantee Act.[20] Sources of capital funds for its guarantee program are the central government budget, revenue guarantee fees and independent financial institutions. The Government capital is subject to annual budgetary considerations. The Korea Credit Guarantee Act restricts the amount of guarantees in proportion to the fund's level of capital. A 20:1 ratio is the legal restriction for the infrastructure fund.[21]

On the other hand, the Government may control the public payments by applying a safeguard ceiling for annual PPP payments. In United Kingdom, although there are no specific guidelines or limits of the total amount of annual government payments concerning private finance

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20 Outlook for Infrastructure Finance in South Korea, by Fitch Ratings, April 2006.
21 Ibid.

initiative (PFI) projects, the ratio of annual government payments for PFI have been maintained at about 2% of the total annual government budget.[22] Also, the UK government controls the total amount of PFI projects over the total public investment. For example, PFI takes about 10% - 15% of total public investment. These measures would help to prevent the Government's payments for PFI from impacting its financial soundness.[23]

State's fiscal obligations

While guarantees and other form of State support are often required to ensure PPP projects are financially viable, the State must implement fiscal procedures to ensure the use of State resource achieve the desired VfM. For example, when the State guarantees the obligations of the local government there is a risk of "moral hazard" where the local government is not truly accountable for its decisions or actions. It may act with impunity or disregard to its potential liabilities, or propose and implement projects which are not necessarily financially sound, relying on the comfort of having a central government guarantee in place.

The State should, therefore, place proper measures for evaluating the viability of proposed projects and have some recourse against the guaranteed contracting agency / local government (the so-called "fiscal intercept") to reduce the risk of "moral hazard" especially when a guarantee is being sought from investors.

In implementing PPP, the Government may potentially face large fiscal costs, particularly over the medium to long term. Therefore, it is necessary to promote transparency in fiscal consequences of PPPs, including the known and future fiscal costs such as guarantees. The International Monetary Fund (IMF) recommends applying disclosure requirements for PPPs under which information on PPPs should be disclosed in budget documents and year-end financial reports. The disclosures should include an outline of the objectives of a current or planned PPP program, and a summary description of projects that have been contracted or close to signing. For each PPP project or group of similar projects, the following information, among others, should be provided:

- future payment obligations (for example, for a period of 5 years, 10 years, or 20 years);
- terms of projects that may affect the amount, timing, and certainty of future cash flows (such as contingent liabilities, concession term);
- whether the PPP assets are accounted as Government's assets and appear on its balance sheet, and how the project affect the reported fiscal balance and public debt;
- any preferential financing for PPPs provided (such as government on-lending);

[22] Jay-Hyung Kim and others, Case Studies from Korea - Volume 1, p.139 - 140, based on the information of the HM Treasury, UK in 2006, *PFI: Strengthening Long-Term Partnerships*, London, the Stationery Office.
[23] Ibid.

- expected or contingent government revenues (such as upside sharing); and

- PPP contracts, or summaries of their key terms (i.e. in standardized form), should also be made publicly available.[24]

Rigorous project evaluation and selection process

Bidding for PPP projects usually requires significant investment of time and cost. Bidders must, therefore, be confident that there is a fair chance of their investment paying off.

To facilitate the investment decision, the process for awarding projects must be:

- fair (bidders are not shown preferential treatment or discriminated against)
- transparent (bidders know precisely what is required of them and that the evaluation conducted in an objective manner)
- competently managed (the evaluation team are aware of market norms and are able to respond to bidders' concerns)
- consistent (to enhance the PPP program's reputation for predictability and stability).

Selection and use of qualified transaction advisors

Transaction advisors are selected through a transparent process and on the basis of appropriate qualifications and experience. Fees for transaction advisors should be on-market and selection of such advisors should give sufficient weight to the advisors' technical proposal so as to avoid automatic selection of the lowest bidder who may not have actual competency to perform the role.

The implementing agency should consider proper use of the Transaction Advisors, in light of the unit's stage of development, in order to achieve both the sufficient assistance with the program/project and transfer of knowledge and skills to the implementing agency. Both under-reliance and over-reliance on advisors should be avoided. Transaction advisors for PPP projects typically include financial advisors, legal advisors, and technical advisors.

Further details related to transaction advisors are discussed in Unit 6 of this document.

Example of PPP/PFI key success factors in United Kingdom[25]

Factors	Details

[24] Richard Hemming, Fiscal Affairs Department, IMF, *Public-Private Partnerships*, p.9, paper presented at the seminar: *Realizing the Potential for Profitable Investment in Africa*, organized by the IMF Institute and the Joint Africa Institute, 2006.

[25] Critical Success Factors For PPP/PFI Projects in the UK Construction Industry: A Factor Analysis Approach; Hardcastle, C; Edwards, P.J.; Akintoye, A.; and Li, B., 2005, p.5.

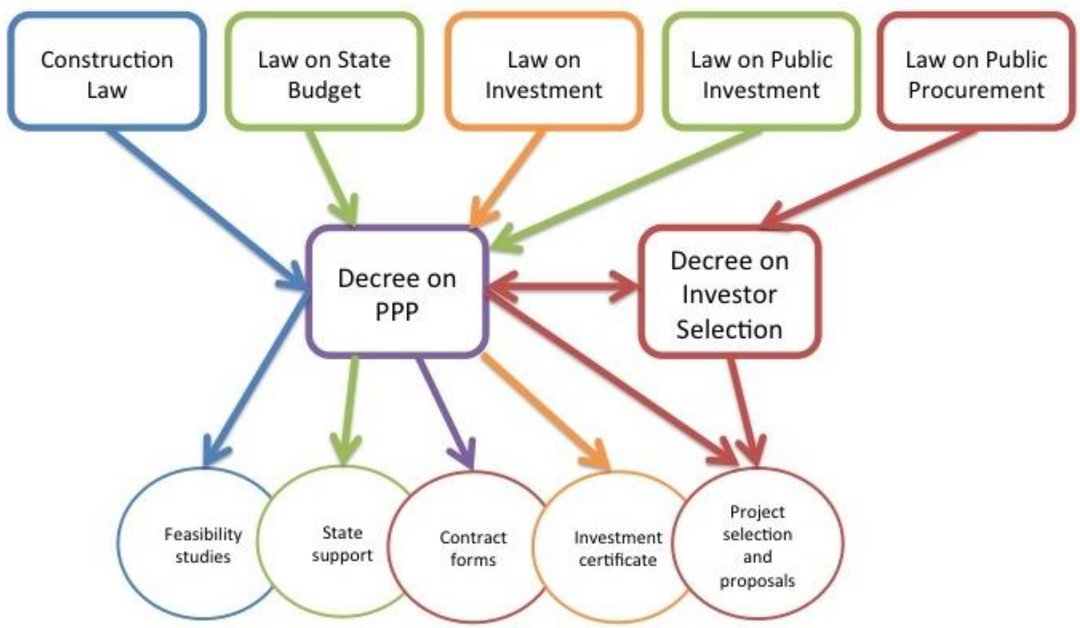
Effective procurement	Transparency in procurement process
	Competitive procurement process
	Good governance
	Well-organized public agency
	Social support
	Shared authority between public and private sectors
	Thorough and realistic assessment of the costs and benefits
Project implement ability	Favorable legal framework
	Project technical feasibility
	Appropriate risk allocation and risk sharing
	Commitment/ responsibility of public/private sectors
	Strong private consortium
Government guarantee	Government involvement by providing guarantees
	Multi-benefit objectives
	Political support
Favorable economic conditions	Stable macro-economic conditions
	Sound economic policy
Available financial market	Available financial market

OVERVIEW OF PPP LEGAL FRAMEWORK (AS OF MAY 2014)

Currently, the Draft Decree is in final drafting stage. The Draft Decree is expected to replace the current legislation on PPP and BOT investments, including Decree 108 and Decision 71. Upon the effective date of the Draft Decree, new projects developed under PPP investment form (including BOT/BTO/BOO/BTL/BT projects) will follow the procedures of the Draft Decree and its implementing guidelines.

The following chart sets out the key elements of Vietnam's legal framework for PPP, in order of legal effectiveness with laws on top, decrees in the center and implementing circulars on bottom. Laws under development should be carefully prepared to permit the PPP Decree to properly operate as drafted. It should be noted that the current development of the PPP framework is dynamic and the chart below may need to be modified from time to time.

Diagram 1: The Draft Decree in relation to laws and circulars related to PPP



The PPP Decree will be subject to and affected by the above laws. Further implications of these laws on PPP Decree are discussed below.

Law on Investment and Law on Public Investment: The PPP Decree will be sitting under the Law on Investment and the Law on Public Investment that are currently under revision and drafting process. These instruments will, for the first time, recognize investment under the PPP form at the level of laws. The Law on Investment sets out general investment procedures for private investment, (including PPP) such as procedures for investors to obtain investment certificates, and investment incentives. Meanwhile, the Law on Public Investment governs the public aspects of PPP investment form, such as the management of public investment and public investment capital.

Law on Public Procurement and Investor Selection Decree: The Law on Public Procurement (issued on 26 November 2013 and effective as of 1 July 2014) provides procurement process for selection of investors, including investors for implementing PPP projects. The Investor Selection Decree, which is currently under drafting, will be issued to provide further guidance on procedures, selection method and criteria for selecting PPP investors. It is important that the PPP Decree and PPP Selection Decree are consistent on circumstances where open tendering or direct contracting will apply to selection of investors for a PPP project.

Construction Law: The Construction Law governs general construction activities and the management of construction activities. PPP projects involving construction of facilities shall be governed by Construction Law. It is necessary that the Construction Law and its implementing Decree be compatible with the provisions of the Draft Decree, particularly, on the requirements for preparation of project proposals and feasibility study report.

Law on State Budget: The Law on State Budget governs principles and activities for management, use and disbursement of the State budget. The estimation, allocation, disbursement, and accounting report of the State Participating Portion and other Government's payments (such as contingent liabilities) in PPP projects are governed by the Law on State Budget. The Law on State Budget is currently being revised and is expected to be issued this year. It is important that the revised Law on State Budget provide a more flexible approach on State budget planning, estimation, and disbursement to be adaptable with PPP projects.

Implementing circulars: To give full effect to the PPP program, a number of circulars will need to be developed to assist ASAs and investors in interpreting the details of concepts set out in the Draft Decree. Currently, there are funding from multilateral agencies to support the Government to develop detailed circulars and guidelines for implementing PPP Decree. These circulars shall includes guidance on key PPP components, including, among others, the following:

- Standardized contract forms;
- Guidance for preparation and standard form of feasibility study;
- Guidance on project selections and preparation of project proposals;
- Guidance on form and calculation of State support;
- Guidance for implementing small sized PPP projects.

In addition, line ministries may develop their own sectorial circulars to provide guidance on their specific sector. For example, detailed guidance on implementing PPP projects in agriculture will be developed by the Ministry of Agriculture and Rural Development, guidance on development of transportation infrastructure under PPP will be issued by the Ministry of Transportation, and so on.

Anticipated key issues under the Draft Decree

As discussed above, the Draft Decree has not yet been finalized and certain issues are still subject to further revisions by the government. The following issues are presented as key concepts of PPP that the consulting team expects to be reflected in the Draft Decree. There remains, however, uncertainty of how these issues are addressed in the final version of the Decree.

Governing scope: the Draft Decree is applicable to investment projects developed under PPP investment form. PPP Investment Form means:

> The implementation of Projects based on a contract between an ASA and the investor to implement investment, construction, management, and operation of infrastructure facilities, and provision of public services that are normally within the scope of facilities and services provided by the public sector.

Investment sectors: the Draft Decree covers the following general sectors (with detailed sub-sectors listed):

- Transport
- Water supply and drainage and sanitation
- Energy
- Healthcare
- Education and training
- Culture and sports
- Information technology and communication
- Civil engineering
- Agriculture
- Other sectors in accordance with the Prime Minister's decision

Roles of institutional organization: the Draft Decree sets roles for institutions, particularly:

- Steering Committee assists the State and the Prime Minister in directing and coordinating PPP investment form
- MPI acts in support of the Steering Committee through its PPP Office
- ASAs - sign and implement project contracts with ability to authorize specialized bodies or people's committee at district level to sign and implement project contracts
- Specialized unit for PPP under each ASA - acts as focal point for managing and organizing the implementation of PPP within ASA
- Project Management Unit - acts as focal point in preparation and implementation of specific PPP projects

State Participating Portion: the Draft Decree introduces as VGF the concept of "state participating portion" which:

- has no cap
- does not include the value of land issued for projects
- is used to support investment in construction of BOT, BTO, BOO projects and to pay for BT, and BTL contracts, to support construction of auxiliary facilities, land clearance and resettlement, etc.

Project selection criteria: the criteria for selecting a project for development as a PPP should:

- conform with sectors, contract types, and investment principles
- be capable of attracting and accessing capital sources, technologies, management experiences of the Investors
- be capable of steadily providing products and services satisfying the quality standards and meeting demands of the users
- be capable to ensure investment capital recovery and profit for Investors
- consider economically efficiency for State investment capital
- compare effectiveness against traditional procurement

Project proposals and unsolicited proposals: project proposals can be prepared and proposed by either ASA or investor. When prepared and proposed by the investor, it is categorized as "unsolicited proposal," which the project proponent may be authorized to prepare feasibility report. An "unsolicited project" is subject to competitive bidding after feasibility stage although the original project proponent may be entitled to certain incentive with regard to the bid.

Feasibility Study (FS) report: the Draft Decree follows similar feasibility study requirements as are familiar under the Law on Construction but a goal is to ensure that in interpreting the Draft Decree the follow international standard core concepts are achieved:

- FS requirements generate output specifications rather than be overly input specific
- FS includes assessment of Value for Money, and proposed contractual and financing structure of the project

Feasibility studies in respect of the State's important project should be approved by the Prime Minister while ASAs can approve projects under Group A, B, and C.

Government guarantees and other forms of support: the Draft Decree provides that forms of guarantee may include guarantee for contractual payments conversion of currency and minimum revenue guarantee.

Bankability issues: The Draft Decree addresses the following bankability issues:
Full guarantee for conversion of foreign currency has to be considered
Lenders' security rights and step-in rights need to be assured

Application of foreign laws: Foreign law may be applied to the following contracts:

- Projects contracts
- Contracts whose performance guarantees are provided by the Authorized State Agency

- Financing and security agreements between the lender(s) and Investor or Project Enterprise
- [Mortgage of assets on land is permissible, and land allocated for a project shall remain with the project for the duration of the term in case lenders have exercised their right to step in or substitute an operator] [CONCEPT IS UNDER REVIEW]
- Other agreements related to the Project as set out in the project contract.

Investor selection process: the Draft Decree defers to the laws on procurement (investor selection regulations) for selection of investors.

Small-size projects: the Draft Decree contemplates that projects below a threshold (currently VND 20 billion) will be subject to accelerated procurement procedures to be developed by the MPI.

Land clearance and resettlement: the acquisition of land, land clearance and resettlement shall be determined when approving the project and specified in the project contract

Governing law: the Parties to the project contract may agree on their choice of governing law.

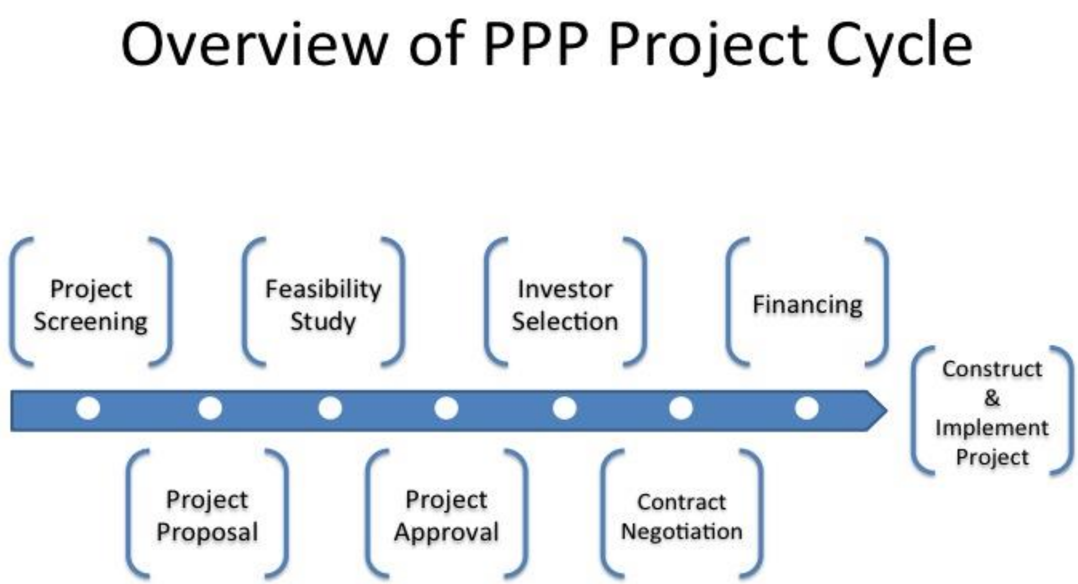
Dispute settlement: The mechanism and venue for the resolution of disputes, including reconciliation, arbitration or litigation, shall be as mutually agreed upon by the parties to the project contract.

Unit 5: Introduction to the PPP project cycle

Vietnam's PPP program is developing in response to a significant and growing investment gap for needed infrastructure, inefficiencies in taking projects from initial screening through to financial close and lack of transparency in investor selection. The PPP program must strike a balance between public sector and private sector interests.

PPP projects are typically developed in a cycle that requires the public sector to screen, assess, approve and prepare the project for competitive bidding prior to private sector involvement. This "PPP project cycle" is designed to minimize the amount of time required for the private sector to bid on the deal, negotiate the project contract(s) and reach financial close—once the investor has been selected. The PPP project cycle promotes consistency and transparency across projects. The PPP project cycle that has been advised to the Government of Vietnam and expected to be reflected in Draft Decree is as follows:

Diagram 2. Overview of PPP Project Cycle



The PPP project cycle contemplated in the Draft Decree is designed to make the process of developing projects more predictable and transparent. Key to implementing the PPP project cycle will be the project approval stage wherein the findings and recommendations of the feasibility study are approved as the basis on which an ASA may negotiate the terms of a project contract with the selected investor. Ideally, the PPP project cycle would run approximately 18 months, which appears to be the average of countries with strong PPP programs.

UNIT 6: UNDERSTANDING THE ROLE OF TRANSACTION ADVISORS IN THE PPP PROJECT CYCLE

OVERVIEW OF TRANSACTION ADVISORS' ROLE

The use of high caliber, credible and experienced international transaction advisers (in particular, financial / commercial, legal and technical advisors) is critical to adequately prepare and structure PPP projects and to develop clear, transparent and efficient procurement processes. Their presence also has an important bearing on investors' confidence in the structure and contractual framework that will be developed for the PPP project.

Many countries that initiate PPP programs start with a relatively heavy reliance on international transaction advisors to develop "pathfinder" transactions and develop standardized transaction structures and contracts. In parallel, the government agencies develop in-house capacity, 'learning-by-doing' alongside international transaction advisors. In time, a growing proportion of the work can be done in-house by the government contracting agencies and coordinating government agencies.

OVERVIEW OF KEY TRANSACTION ADVISORS IN A PPP PROJECT

According to international practice, key transactions advisors in a PPP project include economic advisors, legal advisors, financial advisors, and technical advisors. The following are brief descriptions of key advisors' roles based on guidance from PPIAF's toolkit - "A guide for hiring and managing advisors for private participation for private participation in infrastructure".

Financial advisors

Financial advisors have the skills and experience to ensure that the final transaction represents value for money and an affordable and deliverable deal for the government. The financial advisors shall have a good understanding of the commercial logic and market feasibility of the project, be able to carry out risk analysis and to prepare the financial structure for the type of PPP project being implemented.[26]

Legal advisors

Legal advisors should be involved through out the development of a PPP project. They can develop policy objectives by outlining the possibilities for the project within the existing legal framework, identify legal or regulatory restraints to implement the policy objectives, and provide advice on project structuring. Legal advisors will also provide advice during the pre-qualification processes, evaluation of bids, during stage of appointment of successful bidders, assist in drafting, negotiating, and advising on any variations to the contracts, or disputes arising during the term of the contract.[27]

[26] PPIAF's Toolkit: A guide for hiring and managing advisors for private participation in infrastructure - Volume I - What is PPO and how can advisors help? - page 53.

[27] Ibid, page 57.

Technical advisors

Technical advisors are those with engineering and related specializations who understand the physical aspects of the infrastructure sector under consideration. They should be knowledgeable about the particular sector and be able to advise on operational and investment needs as well as the technical aspects of regulation, legislation and evaluation. It is important that technical advisors have specific and geographically wide-ranging experience of the particular sector they are advising on.[28]

The technical advisors may carry out the following tasks:

- Undertake preliminary analysis to establish the approximate capital costs and the technical specifications or operating standards needed to achieve the government's objectives;
- Analyze the possibility of breaking up various elements of the industry;
- Prepare a schedule covering the construction period, estimated annual operating and maintenance costs, and estimated project lifecycle costs; and
- Review any cost estimates under feasibility study.[29]

WORKING WITH CONSULTANTS DURING FEASIBILITY STUDY PHASE

PPP projects can be complex, both technically and in terms of the procedures to develop the project and attract investors. An ASA is strongly recommended to use experience transaction advisors to assist the development of the project. Advisors should be brought on early in the PPP project cycle, preferably early enough to prepare the Project Proposal. Little savings are gained by bringing in advisors late into the process only to learn the advisors must replicate the work already done due to technical errors in the earlier work.

FUND FOR HIRING CONSULTANTS

Hiring advisors or consultants for PPP projects is important but costly. In preparation of a PPP project, budget for hiring consultants and transaction advisors must be planned. The government State budget is the main source for paying the costs of consultants and transaction advisors. The costs of consultants for advising project preparation of the Government might be reimbursed by the selected investor after signing concession contract.

Many countries set up project development fund managed by an independent agency to prepare funding for costs of preparation of PPP projects, including the costs of consultants, for example P3 Canada Fund, or Philippines' PPP Project Development Fund of PhP550 million (approximately US$12.6 million) set up in 2011 as a revolving fund. The sources of project development fund come from State budget, success fees (paid by the selected investor), and multilateral financial institutions.

In Vietnam, the Project Development Facility (PDF) was set up in 2013 as a revolving fund under a co-financing of ADB (US$20 million) and AFD (EUR8 million). The PDF would be used by Government ministries / project sponsors to fund PPP project preparation activities which

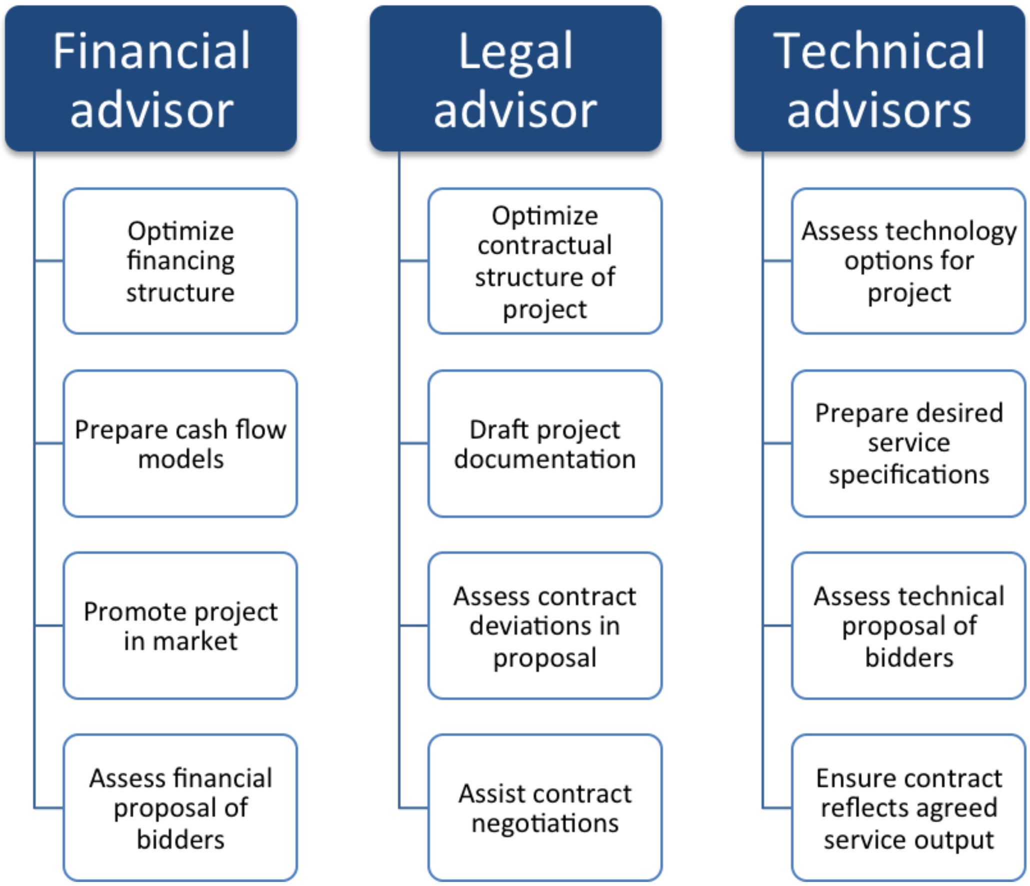
28 Ibid, page 58.

29 Ibid, page 58.

include pre-feasibility studies, full feasibility studies and the engagement of transaction advisors who would structure deals to bring to the private sector for bidding.

The diagram on the following page identifies the key transaction advisors and their respective output.

Diagram 3: Key roles of PPP transaction advisors



Unit 7: Roles and responsibilities of the public authority and the investor in the PPP project cycle

The following table describes main roles and responsibilities of public authority and investor in each stage of the PPP project cycle:

Table 1. Roles of public and private Sectors in implementing the PPP project cycle

Stage of PPP Project Cycle	Public Authority Role	Private Sector Role
Project screening	ASAs are main actors in project screening: • ASA identifies potential PPP projects • ASA prepares project proposal for inclusion into PPP project list For projects using central budget as State participating portion, project proposals shall be sent to MPI, MOF and other Ministries for collecting opinions For unsolicited proposals: ASA evaluates and selects unsolicited proposals prepared by the investor	Investor identifies potential unsolicited projects • projects shall not be in PPP project list • projects might be within projects that are open to proposals • projects must be within the master plan Investor prepares project proposals for submitting to ASAs
Project preparation and feasibility study	ASAs are main actors for preparation of projects listed in PPP project list: • ASA prepares or hire advisors to prepare feasibility study report Appraisal of feasibility study report is carried out by ASA (except for projects of national importance which are to be approved by the Prime Minister)	In case unsolicited project is selected by the ASA, the investor may be assigned to prepare feasibility study for unsolicited projects The investor's project proposal and feasibility studies must comply to the same requirements as those undertaken by ASAs
Project approval	The Prime Minister approves feasibility study reports for projects of national importance	No role for the investor in this phase.

	ASAs may approve the feasibility study reports of projects in groups A, B, and C	
Investor selection	ASAs lead the process for investor selection through competitive bidding for projects to be developed as solicited projects The current Draft Decree is silent on when and how investors are to be selected in respect of unsolicited proposals	Investors attend competitive bidding process in case of competitive bidding
Contract negotiation	The ASA negotiates or assign its specialized unit to negotiate project contract with the selected investor The ASA or its authorized body signs investment agreement with the investor The ASA or its authorized body signs project contract with the investor after issuance of Investment Certificate	The selected investor negotiates and signs investment agreement and project contract with the ASA or authorized body of an ASA
Project implementation and monitoring	The ASA carries out its obligations under the project contract The ASA monitors the implementation of project contract by the investor	The investor complies with the reporting requirements set forth in the project contract that support the monitor program for the project
Hand back	ASA evaluates the infrastructure and receive the infrastructure handed over by the investor	The investor hands back the infrastructure to the ASA at the end of the project contract in accordance with the terms of the contract

UNIT 8: RISK ALLOCATION BETWEEN PUBLIC AND PRIVATE SECTORS

PRINCIPLES OF RISK ALLOCATION

Depending on nature of risks, risks will be allocated amongst different parties in a PPP project. As discussed in Unit 2, the central principle of risk allocation state that:

> "Risk should be allocated to the party best able to manage such risk in an efficient and economical manner."

This concept implies that the total cost of a project will be lower if risk is correctly allocated to the party who can more economically manage the risk, even if that requires the public sector to bear risks it otherwise would prefer not to bear. Ultimately, the public sector benefits from the services (and possible handover) of a PPP project, and therefore it should be willing to assume or share some of the risk of a project.

Generally, risks are allocated according to the following principles:

> Public sector: The government bears the risk for matters within control of the government or which cannot be economically and efficiently managed by the investor (such as through its own resources or the purchase of insurance products).
>
> Private Sector: Risks arising from the construction, operation and management of the project will generally be borne by the project company.
>
> Lenders: Lenders are willing to take credit risk (i.e., the business evaluation they have made that their loan will be repaid in a timely manner) after being satisfied with the results of due diligence on the borrower's ability to repay the loan. Lenders are unwilling to take other risks, which are therefore borne by the borrowers (i.e., project companies).

TYPICAL PPP PROJECT RISKS

There are several categories of risks that may commonly be expected in a PPP project.
The below table describes how risks might be allocated between public sector and private sector:

Table 2: Typical risk allocation

Risk	Description	Public sector	Private sector	Shared
Site risk	Land acquisition and resettlement delay, and cost	✓		
	Unable to acquire entire project land site	✓		
Design risk	Design faults		✓	
	Design fault in tender specification	✓		
Construction risk	Construction cost increase		✓	
	Poor performance of subcontractors		✓	
	Delay in completing construction works		✓	
	Failure to meet performance criteria at completion		✓	
Financial risk	Financial structure risk		✓	
	Interest rate risk (fluctuation of loan interest)		✓	
	Inflation rate risk (increase of inflation rate used for estimating lifecycle costs)		✓	
	Foreign exchange rate risk			✓
Operating risk	Availability of facility		✓	
	Non-performance of services		✓	
	Increase in inputs price		✓	
	Misestimating operating and maintenance costs		✓	
Operating risk	Variation of demand from forecast levels, for reasons beyond control of the government		✓	
	Changes in market prices		✓	
	Incorrect estimation of revenue from income generation model		✓	
	Failure to implement contractual changes in tariffs	✓		
Unexpected event risk	Natural disasters			✓
	Events of war, riots, civil disturbance			✓
	Government acts/omissions causing project cessation	✓		
Political risk	Currency convertibility	✓		
	General change in laws		✓	
	Change in law specific to the project	✓		
	Delay in achieving planning approval	✓		

OVERVIEW OF PROJECT SCREENING

According to the Draft Decree, ASAs carry out project identification and screening based on the following criteria:

- The project conforms with the sectors, contract types and investment principles set out in the Draft Decree;
- The project has capability of attracting and accessing capital sources, technologies, management experiences of investors;
- The project has capability of steadily providing products and services satisfying the quality standards and meeting demands of the users;
- The project has capability to ensure investment capital recovery and profit for Investors (including State Participating Portion);
- The implementation of the project contribute to the supplementation, replacement or enhancement of the efficiency of State investment capital source to construct infrastructure facilities or provide public services.[30]

If a project satisfies the above criteria, it might be select by the ASA to prepare project proposal.

With regard unsolicited project proposed by investors, in addition to the above conditions, the project shall:

- Conform to investment master plan for the industries, localities and investment sectors as provided for in the Draft Decree; and
- Not be implemented under BT or BTL contract type.

OVERVIEW OF PROJECT PROPOSAL

Project proposals act as a pre-feasibility study report of a project which set out preliminary assessment of the project feasibility in term of technical, legal, social, and environmental, and economic viability. Unlike traditional procurement, pre-feasibility study and feasibility study of PPP project should be prepared based on output specifications instead of input specifications. Output specifications define ASA's functional requirements for the facilities and services while offer the private sector flexibility to develop innovation.

Project proposals whether prepared by ASA or unsolicited proponent must satisfy requirements of a pre-feasibility study and then be evaluated by ASA before being approved. For solicited projects, approval of project proposal is the basis for listing project into PPP project list.

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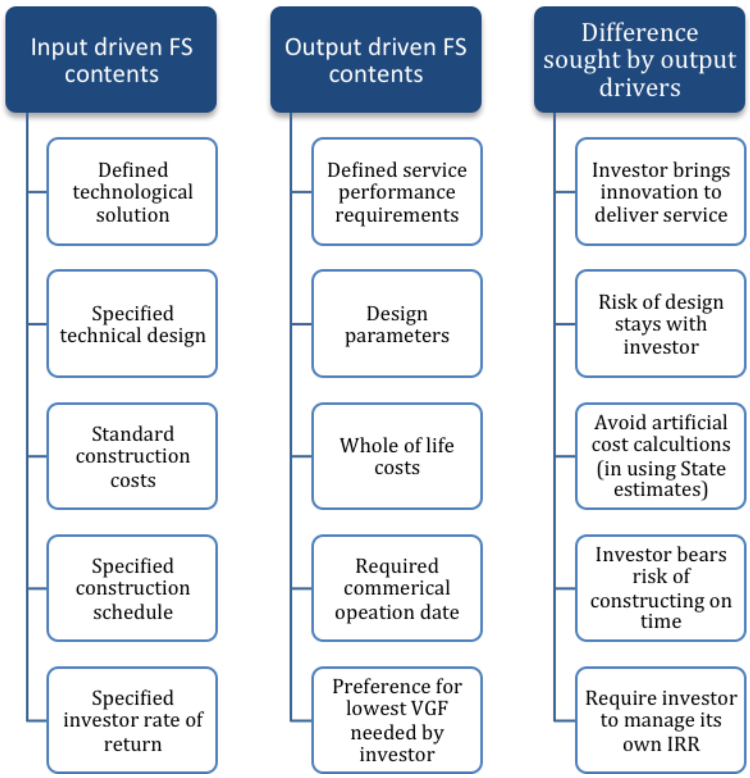
30 Draft Decree dated 20 May 2014, Article 21.

OVERVIEW OF FEASIBILITY STUDIES BASED ON OUTPUT SPECIFICATIONS

A Feasibility Study Report will further develop the Pre-Feasibility Study Report (Project Proposal) with further details and analysis. The Feasibility Study Report should cover the outline scope of the project (output specifications) that is set out earlier in the Pre-Feasibility Study Report. The following diagram compares some key input and output specifications for Feasibility Study Reports.

Diagram 4: Comparing input and output specifications



As discussed above, an output-base feasibility study can encourage a higher level of innovation in PPP project by specifying what is required from a project, including technical and operational requirements as well as payment mechanisms and change mechanisms, etc., rather than how it should be delivered. 31

As a result, output-based feasibility leaves an open space for developing an optimal path to deliver a project as long as the specified requirements are satisfied. In order to compile an output-based feasibility study, the following steps are recommended: 32

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[31] Adapted from draft guidance material prepared under a U.K. DFID grant titled, *Support to the Ministry of Planning and Investment on the development of PPP: Guidelines to support the new Draft Decree* delivered to the Ministry of Planning and Investment by the consulting team of IMC, Rebel Group International, Frontier Law & Advisory, as drafted by Stephen Raggett.

[32] Adapted from *Project Preparation-Feasibility Guidelines for PPP Projects*, p. 12-13. Found at: http://www.ppiaf.org/sites/ppiaf.org/files/documents/toolkits/highwaystoolkit/6/bibliography/pdf/project_preparation_feasibility_guidelines_for_ppp_projects.pdf

Diagram 5: Steps to output based feasibility studies

Step 1	• Description of the service that need to be delivered
Step 2	• Specification of the outputs required to deliver these services
Step 3	• Specification of the minimum standards for the outputs to ensure that the delivered services will meet the expectations.
Step 4	• Assess whether the output specifications can meet on-going service needs
Step 5	• Specify key indicators that will measure performance, allowing for more accurate costing of the output specifications
Step 6	• Identify service interface expectation. This pertains to the interface between the project and the institution's other services
Step 7	• List socio-economic targets to achieve in the project.

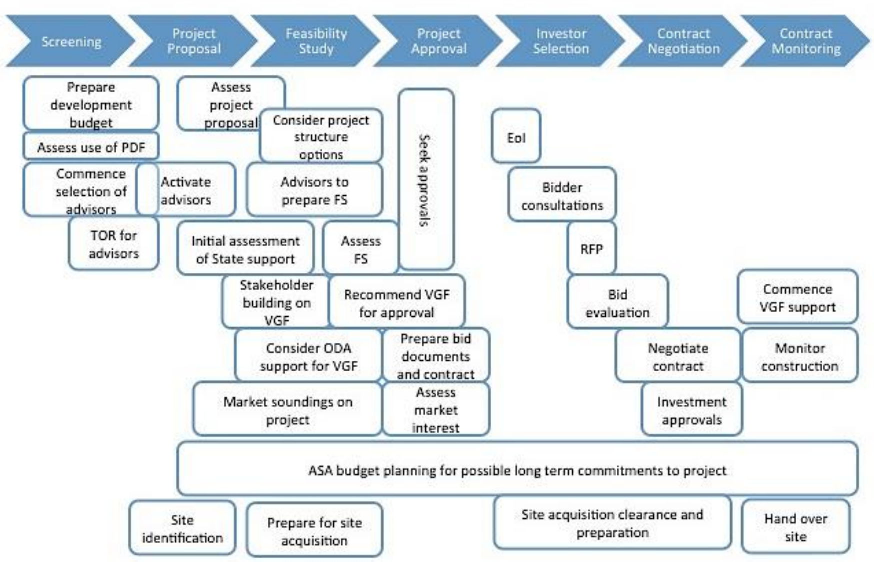
INTRODUCTION TO PROJECT MANAGEMENT OF PPP

Within any PPP program, beyond sector specific technical skills relating to projects, public authorities should develop project management skills to handle each phase of a PPP project. Simply understanding the technical aspects of a project is not enough. The ASA must also develop the skills to manage its internal processes and external interface with investors to ensure a project is identified, developed, tendered and implemented on time and within budget. Managing a project typically requires an ASA to break a project timeline into its components to:

- identify the requirements (both public and private) to implementing the project
- recognize and address the various needs, concerns, and expectations of the stakeholders as the project is planned and carried out
- balance the competing project constrains including, but not limited to:
  - scope of the project
  - quality and output being sought
  - schedule for implementing the project
  - budget available to implement the projects
  - resources to be allocated to the project, and
  - risks inherent in the process of implementing a project

It should be recognized that the program of activities for a PPP project are not likely to be linear or stepwise. There may be several activities running in parallel and delays or failures with one set of activities can soon bring the project to a halt. Taking the PPP project cycle as an example, the following illustrates some of the background activities the project managers within a PPP unit will need to undertake to bring the desired project into operations:

Diagram 6: Example of program of ASA activities to implement PPP project



Within project management lies the need to manage the PPP contract. Contract management involves ensuring that the respective roles and responsibilities set out in the contract are fully understood and met to the standards laid out in the contract, in order to fulfill the government's overall objectives. Part of the contract management process will involve establishing procedures and the institutional units to monitor the contract, and taking appropriate action where contractual obligations are not met.[33]

THE ROLE OF THE TOR AND HOW TO MANAGE DELIVERABLES

The Terms of Reference (TOR) for transaction advisors set out the scope, deliverables, timing and fees for the advisors to perform the tasks they are hired for. A TOR should be factual and concise and specify clearly the deliverables and when they are due. Too often public authorities will try to put too much into a TOR, thinking they are getting a better deal from their consultants. It is the observation of the authors that this typically results in creating impossibilities for the consultants, with the result that the TOR must be varied. Variations lead to project delays, increased costs and often ill will between the parties. They should be avoided by ensuring both parties fully understand and agree on the scope of the TOR and communicate regularly about progress under the TOR. Good and poor TORs can be compared as follows:

Characteristics of a good TOR:

- Factual
- Concise
- Well define deliverables that are realistic and achievable
- Realistic timelines
- Smaller, discreet deliverables connected to milestone payments
- If needed, an ability to assess progress and substitute deliverables

Characteristics of a poor TOR:

- Ambiguity
- Vague and unclear scope
- Overly ambitious work schedule
- Multiple deliverables linked to a single milestone payment
- No ability to substitute a deliverable (for reason)

In the end, it is not in an ASA's interest to create a TOR that cannot be reasonably fulfilled and causes the advisors to fail to achieve the required tasks.

Working with advisors can provide many gains for an ASA's team. Knowledge transfer should be foremost in the team's mind when working with their advisors. Clear communication, responsibility on both sides and open thinking are key to the ASA-advisor relationship in PPPs.

[33] PPIAF's Toolkit: A guide for hiring and managing advisors for private participation in infrastructure - Volume I - What is PPO and how can advisors help? - page 38.

CASE STUDY: ACHIEVING VALUE FOR MONEY ON MINE EFFLUENT WATER TREATMENT

Description

This brief case study examines the Britannia Mine Water Treatment Plant in Britannia Beach in British Columbia. A PPP agreement was approved between the province and a private enterprise, EPCOR, to design, build, finance and operate a mine waste water treatment facility. This case study cites provisions contained in the Request for Expressions of Interest (RFEI) which was issued by the Province in 2003.

Purpose

The report illustrates how Value-for-Money is being achieved throughout the lifecycle of a Public Private Partnership (PPP) project contract entered into between the Ministry of Sustainable Resource Management (MSRM) and EPCOR. It should be noted that, in 2005, the net present value lifecycle cost of the Britannia Mine Water Treatment Plant stood at $27.2 million which was $10 million less than the estimated cost of completing the plant through traditional procurement methods. Environment needs to reduce metals laced water from entering fishing waters drove the public sector's desire to use PPP as a means to more economically achieve environmental safety goals.

Background

The Britannia Mine is located just north of Vancouver at Britannia Beach on the east shore of Howe Sound and was a major producer of copper, which operated during the first half of the 20th century. Approximately 80 kilometers of underground works and five pits were excavated during the operation period of the mine. The raw ore was processed by mills located close by in Britannia Beach. Britannia Beach, itself, is a small town located 55 kilometers north of Vancouver.

An undesirable by-product of the historic operations of the mine has been the generation of acid rock drainage, caused by the exposure of the excavation to air and water. Acid, metal laced water had been flowing into Howe Sound, damaging the marine habitat in the immediate vicinity. If unmitigated, contaminated water from the abandoned mine site would continue to deposit, on average, 600 kilograms of metals into Howe Sound on a daily basis.

The water treatment plant was designed to treat up to 500,000 cubic meters per year of contaminated water before it drains into Howe Sound.

Through an agreement brokered in 2001, the province of British Columbia assumed responsibility for site remediation, which previously belonged to the mine operators, with responsibility for managing the Britannia Mine Remediation Project being assigned to the Ministry of Sustainable Resource Management in 2003, with the Ministry of Water, Land and Air Protection retaining regulatory responsibility under the Environmental Management Act.

EPCOR, who won the bid to finance, design, build and operate the water treatment plant in 2005, is a major company, specialized in the provision of waste water services in British Columbia, with municipalities among their clientele.

Procurement as a Public Private Partnership

The competitive selection stage commenced in January 2004, with requests for Expressions of Interest issued and advertised nationally. Six teams issued expressions of interest and three shortlisted teams were invited to submit proposals with the preferred proponent selected in November 2004. The agreement was signed in January 2005—a procurement period of 12 months.

Competitive Selection Stage	**Process**	**Number of Proponent Teams**	**Timing**
Requests for Expressions of Interest Issued	The request for expressions of interest was advertised nationally. Expressions of interest were received, evaluated and short-listed.	Six	January 2004
Request for Proposals Issued	The short-listed teams were invited to submit proposals.	Three	May 2004
Request for Proposals Closed	Proposals were evaluated		September 2004
Preferred Proponent Selected	The draft concession agreement was produced	One	November 2004
Negotiations	A final project agreement was negotiated with the proponent		November 2004 - January 2005
Agreement signed			January 2005

The Request for Expressions of Interest (RFEI)

Within the RFEI[34], Value-for-Money is very prominent as one of the MSRM's criteria in the evaluation of Expressions of Interest (EOI), with envisaged cost savings achieved through the deployment of **innovative design, technology and operating procedures as well as performance sureties and performance based payments**[35].

The commercial arrangements of the PPP contract specified responsibilities, with the Province transferring '*the financial risks relating to design, construction, operation and maintenance costs of the WTP'*[36] to the Concessionaire.

The public authority sought performance based payments to the project concessionaire. The driving principle was worded as follows:

> *The MSRM is prepared to pay the Concessionaire through a performance based payment mechanism, subject to the Concessionaire meeting the contractual Service Requirements. A proposed payment schedule will be expected from Proponents during the RFP stage*[37].

Obtaining Value-for-Money was a strong motivating factor behind the procurement of the Britannia Mine Water Treatment Plant through the PPP vehicle. The RFEI specified the key objectives to include:

- *The Water Treatment Plant (WTP) will be designed, built and operated in a manner that provides the best overall value to the Province*

- *The WTP should be sufficiently flexible to permit upgrading in an affordable manner*[38]

Value for Money Goals

- The provision of a performance based payment mechanism that will trigger as soon as the plant becomes operational, taking into consideration the volume of processed water and conformance with environmental standards and guidelines;

- The Province's lifecycle investment will be utilized as efficiently and as cost effective as possible, whilst ensuring its execution of water treatment processes are fulfilled to the highest possible standards;

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[34] http://www.partnershipsbc.ca/pdf/bmwt_rfei_final.pdf
[35] http://www.partnershipsbc.ca/pdf/bmwt_rfei_final.pdf pg 9
[36] http://www.partnershipsbc.ca/pdf/bmwt_rfei_final.pdf pg 8
[37] http://www.partnershipsbc.ca/pdf/bmwt_rfei_final.pdf pg 9
[38] http://www.partnershipsbc.ca/pdf/bmwt_rfei_final.pdf pg 5

- Taxpayers will be protected from the financial risks arising from cost overruns, construction and operational delays, and costs related to water treatment technology and plant operation, these will include instances of non-conformance to environmental standards;

- EPCOR's experience in water treatment processes will be harnessed and utilized to maximize cost savings;

- The deployment and effective use of innovative technology will reduce the volume of input materials such as chemical, and utilities such as electricity, required to treat the contaminated water. Technological innovation includes the construction of a hydro generation plant that will produce electricity from the contaminated water as it flows into the water treatment plant;

Valuable lessons can be applied from this early PPP to Vietnam's entry into the PPP market.