

POSITION PAPER OF INFRASTRUCTURE WORKING GROUP

ISSUES IN INFRASTRUCTURE DEVELOPMENT

Prepared by
Infrastructure Working Group
Vietnam Business Forum

This paper looks at some of the main difficulties that have emerged in the implementation of infrastructure projects in Vietnam.

1. Tax on loan interest

For many years, the government, sponsors and financing parties in BOT power projects have followed Letter 1604/TTg-KTN (**Letter 1604**) dated 12 September 2011 of the Prime Minister. Letter 1604 allows the exemption of withholding tax on loan interest payable to lenders in respect of BOT power projects for the entire term of the project. Despite that, in recent negotiations, the government has denied the availability of this exemption. This has a substantial impact on project economics, as it necessarily increases the price that the BOT Company has to charge EVN for the power it produces.

Recommendation

While Letter 1604 is not consistent with law and was not consistent with law at the time it was issued, there is a value to consistency in policy on matters such as this. High cost power producers are at greater risk of non-dispatch than low-cost producers. If a change in policy is warranted, as it may well be in this case, it should be brought in clearly and publicly, and applied to all projects that have not begun the project development process. It should not be brought in on an ad hoc basis in negotiations with individual project developers, none of whom know whether others are more favoured.

2. Financially unviable service price in PPP waste treatment projects

Waste treatment is a priority sector for PPP due to the urgent need to clean up urban environments in major provinces in Vietnam. Waste treatment projects are expected to set an example for the PPP program as a whole as projects in this sector are of manageable size. However, to date there is no customized guidance on development of PPP projects in this sector. Particularly, Circular 07/2017/TT-BXD (**Circular 07**) on waste treatment service fees does not set out a pricing mechanism that is workable for PPP projects. Circular 07 limits the profit earned by the sponsors in solid waste treatment projects to 5%, adversely affecting the financial viability of the projects.

Recommendation

We suggest that the authorised State agencies (**ASA**) in PPP projects should be allowed to decide on appropriate service fees which will be finalised subject to the market and tender results instead of setting a cap on the fees, which, if is not in line with the market, would make projects unattractive to investors.

3. Need for more options for sponsors to raise capital for projects

Other than traditional project financing, sponsors of infrastructure projects in Vietnam have hardly any other options to raise capital for projects. The regulations on project bonds or trading

equity are either not accommodating to the nature of an infrastructure project company (e.g. the law requires that the bond issuer must be profitable in the preceding year to be eligible to issue bonds), or not available at all (e.g. strict requirements on transfer of project equity preventing project companies from raising funds on the capital market).

Recommendation

Being able to raise funds on the capital market would provide the sponsors with alternative financing options, especially given the unresolved financing challenges of on-going projects. The government should consider and put into place a legal framework to support such alternatives.

4. Airport policies

A decision on lease terms between Airport Cooperation of Vietnam (ACV) and the state to allow ACV to continue to generate revenue from aircraft movements remains pending. It is not clear what ACV's ongoing role in the airports network will be, or the extent to which private investment in terminals or operations of airports will be welcome.

Recommendation

As there are vast investment needs, and they are increasing quickly (Long Thanh, Tan Son Nhat expansion, Noi Bai expansion, Phan Thiet etc.), a clear policy that covers the roles of ACV and the private sector should be elaborated.

5. New PPP Decree

On 4 May 2018, the Government promulgated Decree 63/2018/ND-CP on investment in public-private partnership (**PPP**) investment form (**Decree 63**). Decree 63 will be effective on 19 June 2018, replacing Decree 15/2015/ND-CP (**Decree 15**). This is the third edition of the PPP law that has been adopted since the pilot program under Decision 71/2010/QD-TTg of the Prime Minister effective in 2011.

Decree 63 includes a number of welcome changes that would help both the Authorised State agencies (ASAs) and the sponsors in preparing and developing PPP projects. Decree 63 provides more clarity on the process for approval of pre-feasibility study reports of projects. It has tightened the conditions and process for investing in build-transfer projects. It also sets out the framework for transforming a public investment project into the PPP form although more detailed guidance would be needed for future implementation. Notably, Decree 63 has removed the requirement for the Investment Registration Certificate, which helps sponsors avoid "double licensing" situation.

Despite the positive developments, we discuss below key outstanding issues that would need to be addressed either in future revisions to Decree 63 or in its implementing regulations. The discussion below focuses on areas that could be resolved within the scope of a governmental Decree and its implementing regulations. It does not discuss the very important issues relating to risk allocation mechanism and bankability challenges which have been thoroughly explored in our previous position papers over many years.

5.1. State support

State support can be in three forms:

- a. contribution of capital by the State to fund construction costs in projects that are not financially viable for investors;

- b. payment to project companies in build-lease-transfer, build-transfer-lease or similar projects for services provided by the project companies; and
- c. capital support by the State for constructing ancillary infrastructure facilities or land clearance.

Although viability gap funding (**VGF**) has been contemplated since Decree 15, translating the concept into reality has not been successful for two main reasons. Apparently, Decree 63 has not resolved either of them.

One is the lack of a clear mechanism for the authorised State agencies to agree with the sponsors and lenders on the gap amount and the disbursement mechanism. Decree 63 just defers to the laws on public investment for guidance, while the laws on public investment do not contemplate a situation where the State invests in a PPP project for the purpose of viability gap funding without investment cost recovery.

The other reason for the difficulty in realizing VGF is that funding for construction cost may not be the suitable form of support to PPP projects. The financial viability of a project should be assessed from the start of construction until the end of the operational period. It is not possible to estimate the amount of VGF required at the construction stage.

Recommendation

The government should consider putting into place a specific fund and disbursement mechanism to provide financial viability gap fillers to PPP projects in high risk sectors where there is often no off-take agreement to guarantee the revenue stream of the project, such as transport. The more common form of VGF in other jurisdictions is availability payment when the government authorities agree to top up the revenue of the project company up to a guaranteed amount if there is a deficit in the actual revenue.

5.2. Publication of contracts

Decree 63 requires that authorized State agencies must publish key contents of the executed concession contracts on the national procurement portal. These contents include, amongst others:

- name and address of the sponsors and the project company;
- location and site area of the project;
- basic specifications to supervise the quality of the services or the facilities;
- total investment capital, the equity and debt of the sponsors, and the State participation;
- contract form, term of the contract, the proposed timing for transfer of the project facility to the State;
- prices and fees, and form and location for collecting of prices and fees.

While transparency should be promoted, it does not necessarily serve its purpose in some cases. For example, if the government agrees to give a good price to a project of national strategic interest, it would not wish to publish such information. The same would be true of sponsors that agree to less favourable terms for reasons other than purely financial interests.

Recommendation:

The government should consider allowing certain exceptions to this publication requirements.

5.3. Transition provision

Decree 63 will be effective on 19 June 2018. Decree 63 will replace Decree 15 and will technically render all the implementing regulations under Decree 15 no longer applicable. Amongst these are Circular 23/2015/TT-BCT of the Ministry of Industry and Trade on thermal power projects in build-operate-transfer form, and Circular 02/2016/TT-BKHDT of Ministry of Planning and Investment on Pre-FS and FS of PPP projects. These are important pieces of regulations that affect ongoing PPP projects.

Recommendation:

Further guidance by the government on the effect of these implementing regulations should be issued in due course to avoid delay to ongoing negotiations.

ANNEX:**Green growth sector committee – European Chamber of Commerce in Vietnam****1. Development of green buildings in Vietnam and standards**

Buildings are, and will remain, the largest consumers of electricity. The rapid growth of urbanization and its associated life and working style, which includes intensive air-conditioning use, accounts for a considerable proportion of the energy consumption growth in the major cities of Vietnam. Proper building design can reduce this growth for the next 25 years of a building's lifetime. However, the development of green buildings is still in its infancy in Vietnam; just around 40 buildings have certification, the majority of these being in the industrial sector.

EuroCham GGSC would like to suggest that the use of Green Building (GB) standards should be promoted. Many building owners have been introduced to the concept of GB, and organisations such as the Vietnam Green Building Council (VGBC) report a significant uptick in interest over the past couple of years. Over 100 buildings are now GB-certified or are undergoing GB certification in Vietnam.

We recommend the Government provides effective encouragement for building owners to certify their buildings. In addition to international green building certifications already being used in Vietnam, such as the United States Green Building Council (USGBC) Leadership in Energy and Environmental Design (LEED) and International Finance Corporation (IFC) Edge, VGBC has developed the LOTUS certificate. We would support a move to recognise multiple systems for use in Vietnam, letting the market determine which are practical and useful. These systems could be licensed for operation based on a set of simple criteria such as transparency, reliability and coherence according to recognised norms.

The application of NFB solutions should be enforced and promoted through the Vietnam Association of Building Materials (VABM), since compliance may reduce carbon emissions from 70% to 40%.

Buildings should become more energy efficient. Making buildings more energy efficient does not mean higher investment costs. This process can be applied from the architecture phase, with passive design and the use of environmentally-friendly construction materials, to the implementation of energy-efficient devices during construction. We would encourage all buildings to achieve the minimum standards of the VEEBC code (or a simplified version) in order to receive the Building license at Basic Design Stage. Furthermore, Electricity of Vietnam (EVN) could impose a tariff scheme that rewards low energy consumption buildings with lower prices and impose higher prices to high consumption buildings.

There are a lot of individual sustainable building solutions and best practice case studies available in the market. However, we believe that a clear urban planning showcase should be produced, including not just green buildings but also water, waste, traffic and environmental livelihood improvement solutions. This macro-level program of incentives and policies could help Vietnam move towards its vision of a Smart City.