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Client Alert

Vietnam: New draft decree tries to boost investment under new PPP Law

The Ministry of Planning and Investment of Vietnam (**MPI**) recently released a draft of the new decree ("**Draft Decree**") guiding and implementing certain provisions of the Public-Private Partnership (PPP) Investment Law ("**PPP Law**").[1]

The Draft Decree provides noteworthy guidelines and options for interpreting the PPP Law, including the following:

- PPP investment eligible sectors and minimum scale
- a definition of "policy" in the context of PPP project development, even if the consequences of addressing the risks of change in laws and policies remain unclear
- additional guidelines on early termination events and termination compensation payments under PPP project contracts
- drafting options to be considered for compensation in cases where the project is terminated/stopped due to the transition from the previous PPP regulations (i.e., Decree No. 63) to the new PPP Law[2]

While the Draft Decree remains a work in progress, investors looking for PPP project opportunities in Vietnam will need to consider certain unresolved risk allocation issues. In addition, some vaguely drafted guidelines might allow for different interpretations and create uncertainties from a developer and financier's perspective.

Recommended actions

PPP project investors looking for opportunities in Vietnam may want to keep track of how this Draft Decree develops in order to grasp key legal implications and take the necessary steps to ensure the best position in their relevant projects.

Please do not hesitate to contact us if you would like to know more about any legal, regulatory and contractual issues, including the following:

- further details on the legal development and interpretations related to PPP projects in Vietnam
- specific opportunities and challenges, as well as legal and practical solutions, for investing in a PPP project in Vietnam
- more specific implications and practical advice for financing, developing, and managing PPP projects in any particular sector, including energy projects, water supply and treatment, transportation infrastructure, or any other PPP projects

In depth

[1] Law No. 64/2020/QH14 adopted by the National Assembly dated 18 June 2020 on PPP investment.
[2] Decree No. 63/2018/ND-CP of the Government dated 4 May 2018 on PPP investment.

PPP investment eligible sectors and scale

The Draft Decree provides a more specific list of investment projects for the eligible sectors under the PPP Law. By providing an exhaustive list of PPP investment eligible sectors, the Draft Decree appears to limit the eligibility scope for PPP investment projects.

In terms of the PPP investment eligible sectors, the PPP Law provides a general list of sectors, including: (i) transportation; (ii) power grids and power plants; (iii) irrigation, water supply, drainage and wastewater treatment, and waste treatment; (iv) healthcare, education, and training infrastructure; and (v) investment technology infrastructure.

To implement the PPP Law, the Draft Decree provides relevant specific sub-sectors of eligible projects as follows:

- ***Transport***: road, railways, domestic waterways, maritime and aviation
- ***Power grids, power plants (except for hydropower plants and the State's monopolies according to the Electricity Law)***: thermal power, wind power, solar power, renewable energy, gas-fired power and liquefied natural gas (LNG), nuclear power and transmission grids for interconnection between power plants of the above power sectors and the national power grid system
- ***Irrigation, water supply, drainage and wastewater treatment, waste treatment***:
  - Irrigation
  - Water supply, drainage and wastewater treatment, and waste treatment in urban areas
  - Water supply, drainage and wastewater treatment, and waste treatment in rural areas
  - Water supply, drainage and wastewater treatment, and waste treatment in areas with difficult socio-economic conditions or special difficult socio-economic conditions under the Investment Law
- ***Healthcare, education and training infrastructure***
- ***Information technology infrastructure***
  - Information technology parks, including internal and external technical infrastructure (e.g., roads, electricity, clean water, water drainage, communication, environmental treatment and other infrastructures)
  - National information systems, important national databases, specialized databases and online information connection systems on the e-Government platform; infrastructure and technology solutions to ensure information security; information technology technical infrastructure; systems applying information technology for citizens and businesses; systems applying information technology within state agencies

The Draft Decree seems to limit PPP investment eligible projects to the list mentioned above. However, certain overlaps in subsectors may result in unnecessary confusion. For example, although the Draft Decree mentions renewable energy in relation to the power sector, it lists out only wind power and solar power. Considering that power generation technology is changing at a fast pace, specifying the types of power generation

technologies may limit PPP investments into developing new power sources not contemplated in the Draft Decree.

In addition, although certain nuclear power projects are monopolized by the State, it is not clear whether the Draft Decree's reference to nuclear power projects means that nuclear power projects are open to private investors in the PPP form.[3]

In terms of the eligible PPP investment scale, instead of specifying a minimum investment capital threshold under the previous draft version, the new Draft Decree assigns specialized ministries to stipulate a minimum investment scale. In addition, the Draft Decree allows a specialized ministry to restrict the PPP investment scope even further by providing a minimum investment threshold for investing in the respective PPP sectors.

The Draft Decree requests relevant specialized ministries to propose the relevant thresholds for their respective sectors. For example, the Ministry of Industry and Trade of Vietnam proposes to study and recommend a minimum threshold in accordance with the PPP Law for power projects, including renewable energy and LNG-to-power projects.

Termination of PPP project contracts

Termination events and compensation payments upon termination, also known as “buyout” amounts, are briefly discussed in the Draft Decree.

As with any contract, a serious breach of a PPP project contract may entitle the other party to terminate the contract. The question is under what circumstances a party should be entitled to terminate a PPP project contract.

For termination events, under the PPP Law, a party may terminate the PPP project contract if the counterparty materially breaches its contractual obligations. The Draft Decree currently proposes two approaches:

- **Option 1**: The provided list of termination events is mandatory and restricted. The Draft Decree expressly allows PPP investors and governmental bodies to terminate PPP Contracts early in cases of investors' default, governmental bodies' default, or an event of force majeure.
- **Option 2**: The provided list of termination events will serve as reference and be included in an appendix to the Draft Decree as guidance for preparing PPP project contracts.

However, termination by the governmental contracting party as an off-taker may leave the project with nowhere to sell its proposed products or services. The private investors will therefore look to limit the rights of the governmental agencies (whether in the capacity of a licensing authority or a PPP contracting party) to terminate against the PPP project contract.

Because termination of the PPP project contract may leave the project without access to the market, private investors will have to also protect themselves financially from the consequences of termination.

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[3] Nuclear power projects that are important to the economy and society are monopolized by the state in accordance with the annex of Decree No. 94/2017/ND-CP of the government dated 10 August 2017 on commercial goods and services, under which monopoly is held by the State and geographical areas.

As for compensation payments upon termination events, the Draft Decree does not specify the method of calculating or formula for determining compensation payments to give sufficient certainty and comfort in terms of such financial protections.

The Draft Decree only states that the parties shall agree on a formula for determining the compensation amount under PPP contracts. As such, in practice, without a clear policy on minimum protections, it can be difficult for private investors to negotiate actual project contracts to agree on a reasonable formula for determining compensation payments with clear and sufficient financial protection. In addition, the Draft Decree includes a provision that if the State has paid a portion of the amount to support the PPP project company, the State's payment must be "put into" the formula to determine the compensation amount. Given the lack of clarification, it is not entirely clear what the wording "put into" means and how it works, resulting in concerns over potential limitation or reduction of compensation amounts.

In this respect, under the PPP Law, the State's capital can be used:

- to support the construction of the PPP works/infrastructure system
- to make payments to the PPP project enterprise supplying products or public services
- to provide the funding for payment of compensation, site clearance, assistance, resettlement, and assistance for building auxiliary works
- to pay any revenue shortfall
- to pay the costs of discharge of duties by the authorized agency, the contracting agency, the PPP project preparatory agency and the party inviting tenders during the PPP project process
- to pay the appraisal costs

The PPP project contracts should clearly set out not only the basis on which each party may terminate the PPP project contracts, but also and more importantly, the consequences that flow from such termination.

For termination compensation payments, the PPP project contract should provide that the termination payment becomes payable if termination occurs. Except if termination is a direct result of an unjustified investor breach, lenders will seek to ensure that the investor/project company receives a termination payment by way of compensation that is at least equal to the full amount of the project company's outstanding senior debt. If the termination is a result of a governmental agency's default or prolonged political force majeure (also known as governmental events), then lenders and investors may also seek compensation for their expected return on equity.

Defining the concept of 'policy' to determine a change in law event

The Draft Decree provides a definition of 'policy' that is used to determine change-in-law events where an investment policy decision must be amended, and an investor must amend the feasibility study report (FS report) of a PPP project. This definition may also be considered to determine whether the PPP Contract needs to be amended.

The Draft Decree proposes two options for the scope of policies to be considered for that purpose, as follows:

- **Option 1**: The policies of the central level authorities (e.g., the Government's resolutions and the ministries' directives)
- **Option 2**: The policies of both the central and local level authorities (e.g., the Provincial-level People's Committees' decisions)

However, the definition only provides the scope of policies. The Draft Decree is unclear about how to apply the defined term "policy" to a particular change-in-law event. Investors may face difficulties with determining what a policy change is and to what extent the change will require an amendment to the PPP project or the PPP contract.

The change in law is an important consideration for PPP investors given that under the PPP Law, it may trigger amendments to the PPP project's approvals and/or contracts, specifically as follows:

- An investor must obtain an amendment to the issued investment policy decision if a change in policies affects the investment objectives, location, scale, or contract type, or increases the total investment amount by 10% or more or increases the State's capital value.[4]
- An investor must obtain re-approval for the feasibility study report (FS report) if a change in policies directly affects the project's objective, location or scale.
- An investor or its counterparty may amend the PPP project contract if a change in policies causes a material impact on the project's technical and financial plans, the prices of products or cost of public services that the PPP project company supplies.[5]
- An investor and its counterparty may amend the contract's term if a change in policies reduces the project revenue to lower than 75% of the level set out in the financial plan stipulated in the contract. [6]
- The State provides a mechanism for sharing a revenue decrease risk with the investor only if the decrease is caused by a change in policies. Accordingly, when the actual revenue is lower than 75% of the level set out in the financial plan, the State may share 50% of such difference with the private parties.[7]

Changes–in-law arrangements for the project can result in net project revenues going up or, more likely, down. For example, an increase in costs due to changes in policies and laws that are payable by the project company/investors may not affect the prices of products that the project company/investors deliver to the governmental counterparty, but it will affect the profits or return that the project company/investors can distribute to their lenders.

From a risk allocation standpoint, the parties to a PPP project contract need to allocate the risk of changes in laws or policies between them. Lenders can be particularly sensitive in projects where a governmental agency or a State-owned enterprise is a contractual counterparty who, by implication if not by fact, may be able to influence laws or policy rules.

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[4] Article 18 of the PPP Law.
[5] Article 50 of the PPP Law.
[6] Article 51 of the PPP Law.
[7] Article 82 of the PPP Law.

Lenders may also be particularly sensitive if the economic viability of a project is contingent on tax or investment incentives (e.g., in the case of renewables projects that are typically eligible for certain incentives).

From a private sector perspective, the PPP contract should ensure that the governmental contractual counterparty bears the risk of the law or policy regime changing after the date of the agreement and diminishing the economic returns of the project for the project company/investors. To ensure that a PPP project contract is "bankable," especially on a project finance basis, most lenders would typically require the public sector contractual counterparty to bear this risk (preferably in a form that is certain and clear, e.g., supplemental tariffs).

In this respect, the Draft Decree does not include a specific provision on changes in law, policies or costs that can be relied upon when negotiating a PPP project contract for sufficient adjustments to the payments for services and products to be provided by the project company/investors to the governmental contracting counterparty.

Options for compensating investors for the transitional process

The transition from the previous PPP regulations to the PPP Law will stop the development of certain projects (e.g., a project investor seeking a Build-Transfer opportunity or a project in an investment sector that is no longer eligible under the PPP Law). As such, those projects' investors may face a risk of losing certain investment costs incurred in relation to those project developments.

The Draft Decree proposes two options for compensating such potential loss. Specifically, if the investor is forced to stop the project, the State's relevant agency may compensate the investor as follows:

- **Option 1**: The investor must bear all the risks and costs, except for cases where there is a written agreement between the competent state agency and the investor stating that the State must reimburse all such costs; or
- **Option 2**: The investor and the governmental agency will negotiate and agree on a monetary amount to be recovered by the investor based on the work performed and the expenses incurred. This does not apply to cases where the written agreement between the relevant state agency and the investor indicates that the State must reimburse all such costs.

In both options, if an investor's project is stopped due to a change by the PPP Law and the Draft Decree, the investor can seek a reimbursement in accordance with the previous agreement with the government's counterparty. However, in practice, it is unlikely or potentially difficult for an investor to reach a compensation agreement in full to cover all costs.

Both options may still contain certain risks and uncertainty from a private investor perspective. While Option 1 allocates all the risks to developers, Option 2 only states that the governmental bodies will negotiate the compensation amount with the developers. Developers might expect a more certain obligation from the government to share those costs incurred due to the transition from the current PPP regulations into the new PPP Law given that these risks are outside the control of private sector investors.