

Vietnam Wind - A look ahead to 2019

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Summary

While there are concerns over the support structure and PPA, market interest has been strong and (onshore) wind projects are getting built.

Although projects may not be moving forward on a traditional international project finance basis, ultimately sponsors are attracted to the market by its equity returns. Lenders who can be nimble on funding structures are lining up behind.

Developers of wind projects in Vietnam were granted some good news on 10 September last year – under Decision No. 39/2018 (“Decision 39”) – with the increase of the onshore wind feed in tariff (“FiT”) from 7.8 US cents/KWh to 8.5 US cents/KWh and the launch of an offshore wind FiT at 9.8 US cents/KWh.

Now that the dust has settled, we take a look at some of the key challenges facing wind developers as they weigh up an investment decision in Vietnam:

a. FiT eligibility – Less speed, more haste

The FiT rate – applicable for a term of 20 years - only applies to projects which achieve commercial operations date (“CoD”) before 1 November 2021, 3 years from the date Decision 39 came into force. While slightly longer than the 2 years afforded to solar developers (other than

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in Ninh Thuan, where developers have an extended window), this is still a tight timeframe for new entrants considering the lengthy in-country permitting and planning process, not to mention the lack of a domestic wind energy supply chain and difficult monsoon season.

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It is also a little unclear if a 20 year fixed price PPA is actually envisaged by the Minister of Industry and Trade (“MOIT”). MOIT Circular No. 32 of 2012 (“Circular 32”), for example, provides that - based on the electricity costs and general prices of the electricity system - the General Directorate of Energy may propose (to MOIT) to adjust the preferential purchase price from wind power at the point of delivery and the subsidy, for consideration and approval of the Prime Minister. Quite how this should be reconciled against the PPA obligations of EVN is unclear (more on this below).

b. Wind PPA – Give with one hand, take with the other

The latest updates to the FiT (under Decision 39) – which amended provisions of the original legislation implementing wind energy in Vietnam (Decision 11 of 2011) - have not been accompanied with any new form of PPA. There are legacy concerns relating to the PPA (the original form of which was appended to Circular No. 32) including:

- **Constraint/curtailment:** Notwithstanding the obligations on EVN - the state offtaker and transmission/distribution network operator – to purchase all electrical output generated and exported to grid by the facility (Article 2.1), there are very broad rights allowing EVN to curtail the generator due to, for example, incidents in the EVN grid or where the generator does not operate its power plant in accordance with national requirements (Article 7). As the parameters are not clear – and no payments are made in the event a generator is curtailed - financial models will need to factor in some uncertainty with regard to MWh output / project revenue over the 20 year period. Ordinarily, where a generator is curtailed, energy payments would be calculated on a deemed delivered basis.
- **Termination Payment:** In the event of termination of the PPA by the generator (for EVN default), termination payments are limited to the value of payments received in the immediate 12 months prior to termination. Leaving aside how any amounts would be calculated if the PPA was terminated in year 1, a generator would expect to be paid – given there is no other route to market - full compensation over the unexpired duration of the PPA to include debt repayments, costs of termination and loss of profit.

- Exchange rate: Decision 39 contains a general statement that PPA payments will be “adjusted according to the USD/VND exchange rate”, but there are no mechanics set out in the PPA. While the intention appears to keep the amounts payable to generator equivalent (in VND) to the onshore/offshore FiT price in US\$ (i.e., 8.5 or 9.8 US cents/KWh) throughout the term of the PPA, this is not clear from the documents. The recent weakening in emerging market currencies against the US dollar heightens the importance of making sure this is watertight, especially if the sponsor is procuring US dollar financing.
- Change in law/tax: There is no compensation payable where – due to a change in law or tax– the generator suffers losses. This is a risk which is customarily borne by the state offtaker (with compensation paid to the generator for any increase in tax that it suffers).
- Force Majeure: Provisions relating to force majeure are extremely wide and include decisions of competent authorities affecting EVN’s ability to perform its obligations. It would be customary for political force majeure type risks to be borne by the state offtaker and not transferred to the private sector generator.
- Disputes: A mixture of local electricity industry dispute resolution bodies and, ultimately, the Vietnamese courts decide the outcome of a dispute under the PPA. This could pose a risk as: (i) some terms in the PPA are unclear and commercially significant (e.g., constraint/curtailment); and (ii) EVN is a state offtaker.

Therefore while the purchase obligations in the PPA are set out under a form of “take and pay”, in reality, this position is watered down by a host of other price/output re-opener clauses in the PPA.

c. Counterparty credit risk

There is no government guarantee or sovereign support in respect of EVN’s payment obligations under the PPA. Investors therefore need to analyse EVN’s credit position and historic payment profile and seek alternative forms of payment protection to the extent available (e.g., through multilaterals). In this context: (i) a grace period of 90 days before EVN’s failure to pay under the PPA is much too long; and (ii) EVN’s right to point to “sound reasons” to cure such non-payment to the generator is extremely wide and uncommon in an international context (Art 6(3)).

d. Availability of financing

Dealing with the various in-country / contracting risks (or accepting them) will very much

depend on how the project is to be funded: via equity, corporate loans with recourse to a parent or project bonds. Given the issues with the PPA and lack of offtaker credit support, it's unlikely that traditional non-recourse project finance would be available. Whether the funders are based in Vietnam or abroad will also have an impact on whether certain risks are accepted or how they are mitigated.

e. Local Content

At the moment, there are import duty exemptions in respect of goods imported in order to “construct or form fixed assets” (this should be the wind turbines and balance of plant). However that is not to say that local content requirements in the future will not apply, as Decision 39 requires the MOIT to prepare a mechanism for “promoting internal production of wind turbines” and “raising the localization rate of wind power projects.” As it stands, it is not clear whether increased local content requirements would apply for future auctions only following the expiry of the FiT eligibility period or if it could apply to projects currently in development (seeking to avail of the FiT). Clarification from the Government would be welcome as to when any local content requirements will come into effect.

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