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Overview and Recent Developments in the Malaysian PPP Framework

I. Infrastructure Developments in Malaysia

In Malaysia, privatization of public projects and Public Private Partnership ("PPP") projects has been ongoing since the 1980s and the country has been ranked second after Singapore among the ASEAN member states on its infrastructure development[1]. However, in Malaysia, which is aiming to become a developed country by 2020, under its national plan called "Vision 2020," the development of infrastructure, including social infrastructure such as urban transportation and medical facilities, is still highly demanded and PPP is expected to be one of the drivers of such development. In this regard, the Tenth Malaysia Plan (2011 - 2015), the current mid-term development plan of Malaysia, includes strategic PPP-related targets. According to the plan, MYR230 billion have been allocated for development purposes, including the PPP and the Facilitation Fund (described in detail below), which was established with approximately MYR20 billion. This tendency to put high value on infrastructure development that utilizes PPP is expected to continue under the Eleventh Malaysia Plan (2016-2020), which will be tabled in Parliament soon.

II. Legal Framework in Relation to PPP

Laws and Guidelines

In Malaysia, there is no fundamental PPP law. PPP projects are implemented under various guidelines, including the guidelines set out below, in addition to the individual laws for each sector (e.g., Communications and Multimedia Act, Port Authorities Act, Electricity Supply Act, Construction Industry Development Board Act, Railways Act and Federal Roads Act). These guidelines present the PPP framework, as well as the requirements and the selection procedures with respect to PPP projects and project companies, but neither of these guidelines and laws have detailed provisions[2], and UKAS (3PU), the core agency to lead PPP under the Prime Minister's Department, and relevant agencies have broad discretion with regard to the contents and the operation of PPP projects.

Many of the guidelines can be obtained from the UKAS[3] website, however, at present, only the Privatization Master Plan and the PPP Guidelines are available in English.

Below is a summary of the key guidelines:

[1] Malaysia was ranked #29 in the Global Competitiveness Report 2013-2014 issued by the World Economic Forum positions. This rank positions the country at #2 among the ASEAN countries, following Singapore (#2).

[2] There is no standard agreement for PPP officially published in Malaysia.

[3] http://www.ukas.gov.my/en/home

(i) Privatization Master Plan

The Privatization Master Plan was developed in 1991 as a privatization policy for government-owned companies and government-initiated projects[4]. It seems to relate more to privatization compared to PPP, but this Plan, together with the PPP Guidelines (to be described further below), which complement this Plan, will also apply to PPP projects, provided however, that not all of the provisions under this Plan will apply directly to PPP projects.

For example, although foreign participation is limited to a maximum of 25% under this Plan, unless UKAS specifically refers to this Plan, the foreign participation allowed would largely depend on the requirements under the bid proposal of a specific PPP project, regardless of the requirements under this Plan. In many PPP projects, often up to 49% of participation is allowed for the foreign investors. For example, a Japanese consortium and Tenaga National Berhad entered into an IPP agreement in 2014 for an IPP project, in which up to 49% foreign participation was allowed.

(ii) PPP Guidelines (*Guidelines on Public Private Partnership*)[5]

The PPP Guidelines were established under the Ninth Malaysia Plan (2006 - 2010) to complement the Privatization Master Plan. The PPP Guidelines set out the outline of PPP in Malaysia, such as the principles in adopting the PPP approach, definition of PPP (both the standalone model and the service payment model); difference between public projects and privatization; submission of PPP proposal (in case of solicited proposal); general criteria for PPP project (e.g., the sponsor of a project must be financially strong with a paid-up capital of the project company to be at least 10% of the project value[6]); roles and responsibilities of the private and public sectors in PPP, and the overall process flow of the PPP project. Since the PPP Guidelines are very simple and concise, the details of each project defer to the decisions to be made by UKAS and other governmental agencies, and bid documents for such project.

(iii) Facilitation Fund Guidelines

As previously mentioned, the Government has introduced the Facilitation Fund worth MYR20 billion under the Tenth Malaysia Plan. It is a form of support to be provided by the Government for public projects. The purpose of the Facilitation Fund is to bridge the viability gap and stimulate private investments in PPP projects in priority areas, such as infrastructure, education, tourism and health.

The Facilitation Fund Guidelines ("FF Guidelines") were first issued in 2011 to set out the scope of the operations of the Facilitation Fund. According to the FF Guidelines, issued in 2011, any financing provided by the Facilitation Fund was to be provided in the form of a grant, and such grant was to be used only for the development of the basic infrastructure of a project, such as access roads, bridges and utilities. However, there were no provisions regarding the amount of the grant to be provided or the criteria for the eligibility of projects. When the amendments to the FF Guidelines were made in 2014, these were aligned to the points above, as described below.

✧ Key Amendments made to the FF Guidelines in 2014

4 The Privatization Master Plan supersedes the Privatization Guideline established in 1985.
5 http://www.ukas.gov.my/c/document_library/get_file?uuid=02f1ea81-8075-4387-8b69-ebb2120292f1&groupId=15223
6 However, in many cases, debt-to-equity ratio of PPP projects in Malaysia is 8:2 or 7:3.

- Deletion of limitation on the use and maximum amount of the grant

The limitation on the use of a grant from the Facilitation Fund was removed from the FF Guidelines and the Facilitation Fund can be used, among others, to fund up to 10% of the project cost or MYR200 million, whichever is lower. The grant from the Facilitation Fund will be disbursed directly to the accounts of the project companies subject to prior approval from UKAS when requested upon the completion of the project.

- Criteria of eligible projects

A section detailing the minimum criteria that a project company has to follow to apply for a grant from the Facilitation Fund was created. Below are the key criteria:

a) It must be a new investment, which will provide a strategic impact or a significant contribution to the national economy, including projects in the priority sectors identified in the National Key Economic Areas[7], where "physical development" does not exceed 10% of the overall project development (further described below).

b) It must be commercially viable and sustainable in the long term without need for additional help from the Facilitation Fund and the Government.

c) Project cost excluding the cost of land must be MYR100 million or more (MYR50 million or more for the health service sector and the logistics sector);

d) The project company must:

    - be incorporated in Malaysia under the Companies Act 1965 and have a paid-up capital of at least MYR3 million;

    - have ownership of or rights over the land used (i.e., lease) for the development of the project; and

    - have the capacity, capability, skills and expertise to implement the proposed project; and have solid financial standing, as well as the capability to obtain commercial funding for the implementation of the project.

As to the requirement (a) above, "physical development" means the progress of physical development work on a project land that has not been developed, including site clearance, such as clearing of trees on a piece of land, and piling works. As the purpose of the Facilitation Fund is to provide a grant to a new investment project, if the site clearance activities and the piling of the land have commenced and have exceeded 10% of the overall development process, then the project that would commence after the completion of "physical development" shall not be considered a new project and, as such, it would not be eligible for

[7] National Key Economic Areas are specified in the Tenth Malaysia Plan, and they are as follows: (1) oil and gas; (2) palm oil and related products; (3) financial services; (4) wholesale and retail; (5) tourism; (6) information and communications technology; (7) education; (8) electrical and electronic; (9) business services; (10) private healthcare; (11) agriculture; and (12) greater Kuala Lumpur.

consideration for the Facilitation Fund[8]. The requirement of this 10% threshold will, in general, be determined based on the progress report with respect to the development to be submitted by the project company, however, for large-scale projects, UKAS will conduct an onsite inspection and confirm whether the project satisfies the requirements, although it seems that there are no objective criteria, which will be commonly applied to every project[9].

III. Summary of PPP

1. Applicable Projects

The laws and guidelines for PPP do not limit the scope of applicable projects, which can be conducted as PPP projects. Until now, projects related to transport, highways, communication, health, energy and utilities, and education, etc., have been implemented in Malaysia, but the scope of a project will be flexibly determined based on the country's needs.

The following are several key projects that will be undertaken in Malaysia in the next several years:

- Mass Rapid Transit (MRT) project
- Tun Razak Exchange (Kuala Lumpur International Financial District)
- Privatization of the Penang Port
- 300-megawatt Combined-Cycle Gas Power Plant in Kimanis, Sabah

2. Selection of Project/Project Company

In the PPP Guidelines, there is a flow chart that summarizes the selection process of projects and project companies for PPP projects[10]. According to this flow chart, a PPP project should be proposed by ministries and agencies but does not intend to prohibit the proposals from the private sector (unsolicited proposals will be described further below).

In the case of a project proposed by the public sector, in principle, it must go through a bidding process. The time requirement will largely depend on the contents of the PPP bid documents to be provided by the ministries and agencies. However, it is typically the case that the winning project company will be announced within 9 to 12 months after the issuance of the PPP bid documents. There are no absolute rules as to whether the applicant is required to submit a support letter or a commitment letter issued by financial institutions or concerning the content of those letters, and such requirement will be described in each bidding proposal for each project. Note that in some cases, the applicant may be required to submit a term sheet agreed with the financial institutions.

8 This is only to be determined based on the progress of the development, and it will not be determined based on the amount of costs required for the "physical development."

9 According to the responses B&M Kuala Lumpur office obtained from UKAS.

10 http://www.ukas.gov.my/c/document_library/get_file?uuid=02f1ea81-8075-4387-8b69-ebb2120292f1&groupId=15223

For further information please contact

Yasuhisa Takatori
Partner
Tokyo
+81 3 6271 9702
yasuhisa.takatori@bakermckenzie.com

Mark Lim
Partner
Kuala Lumpur
+60 3 2298 7960
mark.lim@bakermckenzie.com

Erik Begin
Partner
Singapore
+65 6434 2598
erik.begin@bakermckenzie.com

Maki Kawamura
Partner
Tokyo
+81 3 6271 9518
maki.kawamura@bakermckenzie.com

Faez Abdul Razak
Associate
Kuala Lumpur
+60 3 2299 6839
faez.abdulrazak@bakermckenzie.com

3. Unsolicited Proposals

As mentioned above, the proposal of a PPP project can be made not only by the Government, but also by companies in the private sector, and if a proposal by the private sector is approved by UKAS and the other relevant agencies, such a project can be implemented as a PPP project. Large-scale projects which involve significant public interest are usually proposed by the public sector and projects that are proposed by the private sector tends to be on a smaller scale, but at present, projects to build incinerators and IPP projects have been proposed through unsolicited proposals.

Unsolicited proposed projects are not required to undergo a bidding process to select a project company, and such a proposer shall negotiate with the Government and/or the relevant agency regarding the project and then implement the project as a PPP project if an agreement is reached. Should the negotiations fail, the project will be privatized through competitive bidding as if it was a solicited proposed project.

4. The PPP Model and Business Structure

PPP projects in Malaysia can be classified into two main models: one being the service payment model and the other the stand-alone model. The PPP Guidelines are prepared based on the service payment model, but the definition of PPP under the PPP Guidelines clearly states that the standalone model can also be selected.

The service payment model is a model in which the public sector pays for the services delivered by the private sector based on a pre-agreed key performance indicator (KPI), and is often used for social infrastructure development, such as hospitals and universities. The business structure for this model is customarily BLMT (Build-Lease-Maintenance-Transfer). On the other hand, the standalone model is the model in which the private sector will be allowed to collect charges and fees directly from end users and it is often adopted for infrastructure development mainly for the transportation sector. BOT (Build-Operate-Transfer) or BOO (Build-Own-Operate) tend to be selected as a business structure.

Market risks will be assumed by the public in the case of the service payment model and by the private sector in the case of the stand-alone model. The availability payment model used for offtake-type IPP projects is similar to the service payment model in terms of market risk profile[11].

5. Government Support

As mentioned above, a grant may be provided by the Facilitation Fund as a monetary Government support to be given to PPP projects in Malaysia. The Government is not expected to provide other monetary support such as guaranties or loans to PPP projects or project companies, provided however, that for the development of renewable energy, the Government introduced a special financing scheme of up to MYR50 million per company called the Green Technology Financing Scheme ("GTFS"). In the GTFS, the

11 According to a research paper issued by the Economic Research Institute for ASEAN and East Asia in March 2013, PPP models are classified into four categories: (a) concession model; (b) accommodation model; (c) process plan model; and (d) usage model (http://www.eria.org/projects/PPP_in_Malyasia_ERIAsummary_March_2013.pdf). (a) and (d) are similar to the standalone model, and (b) and (c) are similar to the service payment model.

Government will guarantee up to 60% of the financing amount and bear 2% of the total interest rate charged on the loan.

In some other cases, tax incentives may be given to private investments. For example, in 2013, the Government announced a 100% tax exemption of statutory income for a period of 10 years, and an exemption from withholding tax and exemption of stamp duty to be given to PPP projects in the oil and gas industry.

www.bakermckenzie.co.jp

Baker & McKenzie
(Gaikokuho Joint Enterprise)

Ark Hills Sengokuyama
Mori Tower 28F
1-9-10, Roppongi, Minato-ku
Tokyo 106-0032, Japan
Tel + 81 3 6271 9900
Fax + 81 3 5549 7720
www.bakermckenzie.co.jp