

# Ex-post Management and Renegotiation of PPPs in Korea

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**OECD Second Annual Meeting on Public Private Partnerships,  
5-6 March 2009, OECD Conference Center, Paris**

# C O N T E N T S



1. Performance
2. Renegotiation of Concession Contracts
3. Challenges for Better Ex-post Management and Renegotiation



# Number of PPP Projects by Procurement Scheme

(unit: number (Trill. KRW))

Step \ Type	BTO*		BTL*	Total
	National Projects**	Competent Authority Projects		
Under Operation	19(9.6)	66(3.1)	33	118
Under Construction	32(27.5)	17(1.2)	101	150
Preparing to Construct	10(4.6)	7(0.2)	42	59
Under Negotiation	16(12.7)	1(0.05)	112	129
Under Review	2(0.9)	-	-	2
Subtotal	79(55.3)	91(4.6)	288	458
Total	170(59.9)		(16.5)	(76.4)

\*: as of Dec. 2007

\*\*\* Large-scale projects whose total costs are 200bill. or more are monitored by the PPP Committee organized by the Ministry of Strategy and Finance.

# Trends of Private Investment in PPP

## Public & Private Investment Trends

(unit: trillion KRW, %)

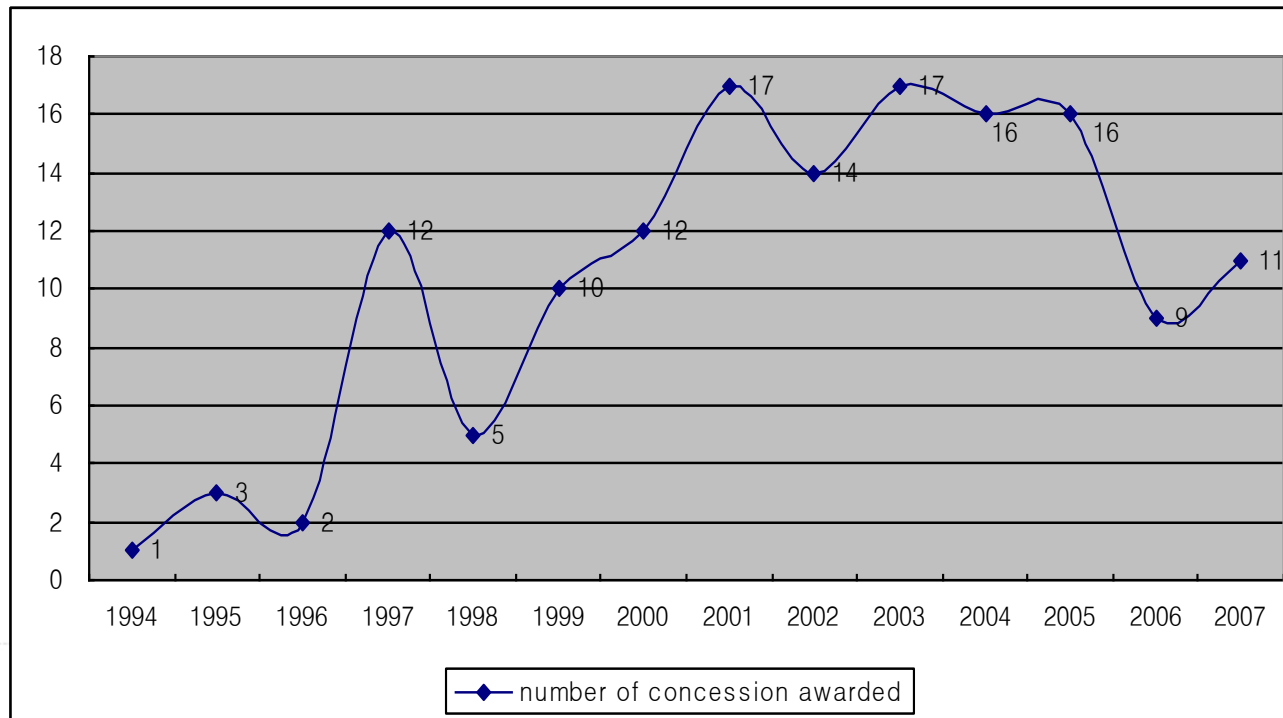
	'98	'00	'01	'02	'03	'04	'05	'06	'07
<b>Private Investment (A)</b>	0.5	1.0	0.6	1.2	1.2	1.7	2.6	3.0	3.0
<b>Gov't Investment (B)</b>	12.7	15.2	16.0	16.0	18.4	17.4	18.3	18.4	18.4
<b>A / B (%)</b>	3.9	6.6	3.4	7.5	6.6	9.8	14.2	16.3	16.3

A : Public works completed

B : Annual budget in transportation and regional development sector, *The Five-year National Fiscal Management Plan*

# BTO Concession Agreements

- ✓ 145 BTO projects of 46.5 trillion Korean KRW are concession awarded.
- ✓ Annual number of concession agreement increases since the amendment of PPP Act in 1999. With MRG support abolished for unsolicited proposals in 2006, it decreases sharply.



# BTL Projects Since 2005

- ✓ 288 BTL projects are under progress, of which the total project cost is KRW 16.5 trillion.

## Number of BTL Projects and Total Cost

(unit: number, trill. KRW)

	Schools	Univ. Dorms	Vocational Colleges	Sewage systems	Servicemen apartment Complexes & Military quarters	Cultural Facilities	Medicare and Welfares	Railroads	Science Museums	Total
<b>Number</b>	136	14	3	61	37	24	9	1	3	<b>288</b>
<b>Amount</b>	5.3	0.9	0.1	4.3	2.9	0.6	0.1	2.3	0.07	<b>16.5</b>





# Number of Renegotiation Changes

- ✓ Among 145 BTO projects awarded, 117 projects are formally supervised and reviewed. 28 projects are missed as : very small parking-lot projects in earlier stage (18 projects), very small environment projects (5 projects), and others (5 projects).
- ✓ Among 117 projects, 65 projects have clause(s) of renegotiation changes in concession agreements.

	Number of projects supervised	Number of projects with renegotiations	(%)
Road	37	22	57.8
Rail	6	2	33.3
Port	16	8	50.0
Environment	46	22	48.8
Others	13	11	84.6
<b>Total</b>	<b>117</b>	<b>65</b>	<b>55.5</b>

# Timing of Renegotiation Changes

- ✓ Among 65 projects with changes, 26 have been initiated within 2 years after the contract: average time to change is 2.6 years.
- ✓ For the earlier projects, the amendment of PPP Act in 1999 activates change of clauses.

	Within 1yr	1~2yrs	2~3yrs	3~4yrs	4~5yrs	Beyond 5yrs	Not-available	Total
Road	4	5	3	5	1	4		22
Rail	1			1				2
Port	2	1		1	1		3	8
Environment	5	5	7	4	1			22
Others	3		2		1	1	4	12
<b>Total</b>	<b>15</b>	<b>11</b>	<b>12</b>	<b>11</b>	<b>4</b>	<b>5</b>	<b>7</b>	<b>65</b>

# Why Changes?

- ✓ In 65 projects with Renegotiation changes, 116 clauses have been initiated, implying 1.8 clauses per project.
- ✓ Among 116 clauses initiated, 19 (16%) are initiated with Act change, 40 (34%) with design change, and 53 (46%) with refinancing.

	Act change	design change	refinancing	others	total
Road	11	11	21	2	45
Rail			2	1	3
Port	2		10	1	13
Environment		24	13		37
Others	6	5	7		18
<b>Total</b>	<b>19 (16%)</b>	<b>40 (34%)</b>	<b>53 (46%)</b>	<b>4</b>	<b>116 (100%)</b>

# Who Initiates?

- ✓ Among 116 clauses, 36 (31%) are initiated by the government and 54 (47%) are initiated by the concessionaire.

	change of Act	government	concessionaire	total
Road	12	10	23	45
Rail	-	1	2	3
Port	2	1	10	13
Environment	6	19	12	37
Others	6	5	7	18
<b>Total</b>	<b>26</b>	<b>36</b>	<b>54</b>	<b>116</b>

# Completed or Under Process

- ✓ Among 116 clauses initiated, 64 (55%) clauses are completed while the remaining 52 (45%) are under process.
- ✓ In case of refinancing, completion ratio is extremely low. Just 6 cases out of 53 (11%) are completed. However, refinancing negotiation is rising now.

	Act change	design change*	refinancing	others	total
Completed	19 (100%)	37 (90%)	6 (11%)	3	<b>64 (55%)</b>
Under process	-	4 (10%)	47 (89%)	1	<b>52 (45%)</b>
<b>Total</b>	<b>19 (100%)</b>	<b>40 (100%)</b>	<b>53 (100%)</b>	<b>4</b>	<b>116 (100%)</b>

\* Number of design change includes changes in total cost and government support.

Part-03

Challenges for Better Ex-post  
Management and Renegotiation



# (1) Upgrade Procurement Schemes

## Current Issues

- ✓ Weaknesses of concession agreement result from their deficient design
  - They are the result of a hurried process, questionable advice, and all combined with the limited experience
- ✓ Importance of regulation with the strongest possible legal grounding cannot be emphasized enough



## Challenges Ahead

- ✓ Upgrade PPP selection criteria : PPP versus traditional public project ; solicited versus unsolicited project ; etc.
- ✓ Provide detailed guidelines for initial concession design
- ✓ Evaluate optimal government support

## (2) Strengthen Ex-post Monitoring and Supervision

### Current Issues

- ✓ After the construction period, each supervising agency (line ministry of central or local government) manages the project separately
- ✓ In the operation and maintenance period, supervising agency pays less attention
- ✓ Ministry of Strategy and Finance request PIMAC to consult about the controversial issues with concessionaire



### Challenges Ahead

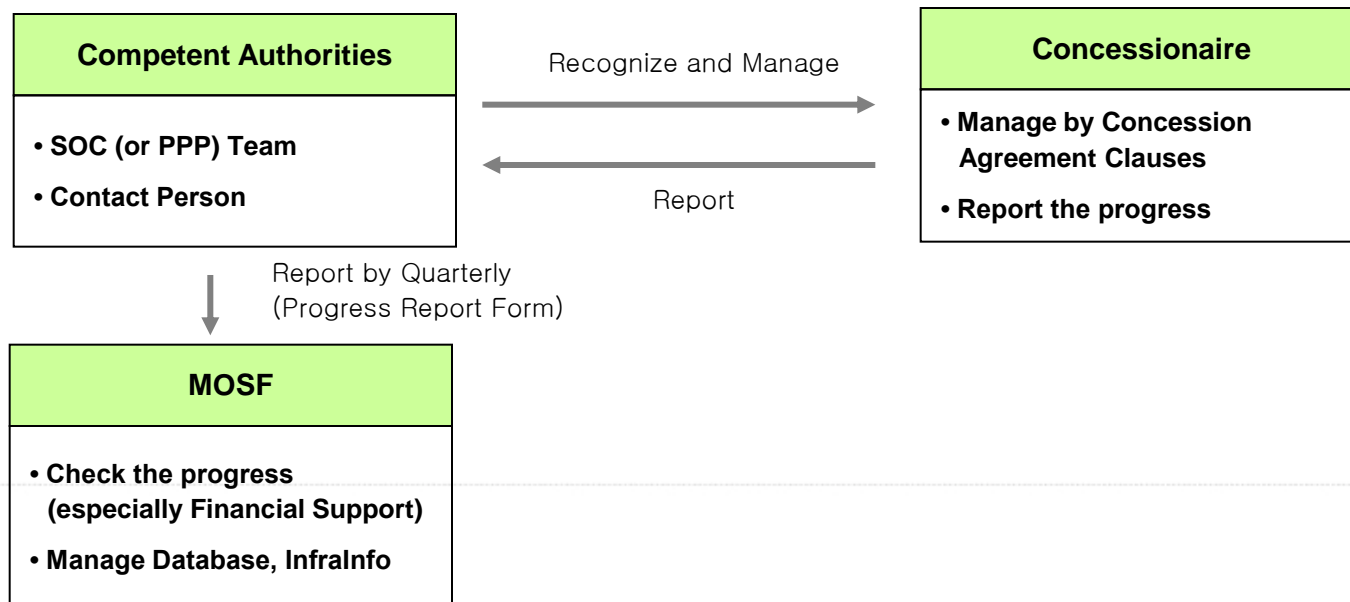
- ✓ Develop centralized information and management system
- ✓ Provide standard guidelines for ex-post operation and management
- ✓ Create full-time PPP portfolio management body in the government



## <Monitoring Scheme>

- ✓ PPP projects are managed by each competent authority (central and local governments).
- ✓ Each competent authority manages projects by (a) controlling guidelines for concession agreements and (b) receiving project progress reports quarterly. The competent authority submits the results to MOSF and also separately inputs status data for each project in the InfracInfo system (<http://InfracInfo.kdi.re.kr>). MOSF and PIMAC administer the system.

### System for PPP Project Management



## (3) Develop Clear Guidelines for Refinancing

### Current Issues

- ✓ Guidelines for refinancing are not clearly defined in an earlier stage
  - Change of investors 5% or more shall be approved in advance
  - Profit from refinancing shall be 50% shared by the government
- ✓ Among changes in concession contracts, design change is initiated by the government while refinancing change by the concessionaire only
- ✓ Too expensive advisory fee



### Challenges Ahead

- ✓ Provide a clear guideline for financing and refinancing
  - Timing of concession contract, financing and refinancing
  - Minimum equity ratio : 5% for BTL / 20% for BTO?
  - Definition of basic versus new financing model
- ✓ Who initiates and measures the profit?
- ✓ Logic of profit-sharing and 50%
- ✓ Should refinancing profit mostly used for reducing user fee?

# <Refinancing Rules>

## Definition

- **Modifying the project consortium's equity structure, investment share, debt financing conditions, etc. by comparing the recent financial conditions following the concession agreement.**

## Sharing Gain

- **Calculation: an increase in the expected profit.**
  - expected IRR for Post-refinancing financial model minus that of Pre-refinancing financial model.
- **The competent authority : the concessionaire = 50 : 50**
- **Utilization: improving the implementation conditions of PPP project .**
  - lowering the user fee (as a priority), reducing the amount of guarantee of operational revenue, concession period, etc.

## Cases

- **Switch from equity to subordinated debts (minimum capital structure requirement: 20% equity during construction period, 10% equity during operation period).**
- **Refinancing on 6 projects have been completed, and that on many projects are going on.**

## (4) Refine Rules for Renegotiation and Termination

### Current Issues

- ✓ Renegotiation is often requested by the concessionaire for:
  - Making up too aggressive bidding
  - Adjusting to macroeconomic shocks
  - Compensating losses from changes in government priorities or from competing government projects
- ✓ Recognition of buyout right in inevitable circumstances / Disposition for public interest
- ✓ Termination payment too generous in case of default by concessionaire



### Challenges Ahead

- ✓ Revise Standard Concession Contract including the details of renegotiation determinants
  - Regulatory framework
  - Macroeconomic shocks
  - Government priorities
  - Competing government/public projects or other PPP projects
- ✓ Clarify what the inevitable circumstances and public interest are
- ✓ Change of standard rule for calculating termination payment

# <Early Termination Rules>

## Buyout Right

- The concessionaire may request the government to buyout the project in the event that facilities is impossible to maintain due to inevitable circumstances such as natural disaster.

## Calculation of BTO

- During the construction period: already incorporated private investment amount, and the opportunity cost if applicable.
- During the operating period: weighted average of 1) depreciated value of the already incorporated private investment amount and 2) the present value of the project (weight varies depending upon the cause of default).

Category	BTO	
	Construction Period	Operating Period
<b>Default by Concessionaire</b>	Incorporated private investment amount	Depreciated value of the amount on the left
<b>Default by Government</b>	Incorporated private investment amount x [1 + current IRR (B)]	Weighted average of 1) the sum of the depreciated value of the amount on the left & 2) present value of the project for the remaining operating period
<b>Non-political force majeure</b>	Incurred private investment amount x [1 + Standard debt interest rate (A)]	Same as above
<b>Political force majeure</b>	Incorporated private investment amount x [1 + (A+B/2)]	Same as above

## Cases

- Up to 2008, there are 3 events of Early Termination.

*Thank you*

Korea's Leading Think Tank

