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If a whole or part of a paragraph has been amended, the date of the amending regulation appears in square brackets at the end of the paragraph. If a whole paragraph or sub-paragraph has been deleted, the date of the deletion appears in square brackets beside the deleted paragraph or sub-paragraph.

Republic of Latvia

Cabinet

Regulation No. 1152

Adopted 6 October 2009

Procedure for the Conduct of Financial and Economic Calculations, Determination of the Type of a Public-Private Partnership Agreement and the Provision of an Opinion Regarding Financial and Economic Calculations

*Issued Pursuant to
Section 9, Paragraph four, Section 14, Paragraph two
and Section 15, Paragraph three of the
Public-Private Partnership Law*

I. General Provisions

1. This Regulation prescribes:

1.1. the procedure by which the type of a public-private partnership agreement shall be determined and by which financial and economic calculations shall be conducted, as well as the criteria for the accounting of the assets of a public-private partnership, in order to determine the impact of a public-private partnership contract on the amount of long-term liabilities of the State budget and the government debt;

1.2. the procedure by which the Monitoring Institution shall provide an opinion regarding the assumptions included in the financial and economic calculations and the risk allocation between the public partner and private partner in the public-private partnership agreement, including the deadlines for the provision of opinions, observing the expected contract value in the financial and economic calculations and the risk allocation between the public partner and the private partner; and

1.3. the procedure by which the Ministry of Finance shall provide an opinion on the expected impact of the conditions referred to in the financial and economic calculations on the amount of the long-term liabilities of the State budget and the government debt.

2. A public partner shall be responsible for the conduct of the financial and economic calculations (consequently, also for the correctness and accuracy of the information provided) of a potential public-private partnership project (hereinafter – project) and the type of a public and private partnership agreement and the determination of the expected contract value.

3. When preparing financial and economic calculations, a public partner shall utilise the recommendations developed by the Ministry of Finance regarding the information to be included or to be appended to the financial and economic calculations. The Ministry of Finance shall publish the recommendations regarding the information to be included or

appended to the financial and economic calculations on its Internet home page www.ppp.gov.lv.

II. Conduct of Financial and Economic Calculations and Determination of the Type of a Public-private Partnership Agreement

4. Financial and economic calculations shall consist of:

- 4.1. a characterisation of the current situation and the justification for implementing the project;
- 4.2. a comparison of alternative financing for implementation of the project; and
- 4.3. an assessment of the best alternative for implementing the project.

5. A characterisation of the current situation and the justification for implementing the project shall include the following:

5.1. a description of the current situation in the field of the project implementation and the justification for significance of the project implementation (including the opinion which the responsible institution has provided regarding the formulation of the policy in the sector, where it is planned to implement the project);

5.2. an assessment of the compliance of the project to the development planning documents at the local, regional and national level, as well as the overall impact thereof on regional development and the economy;

5.3. an assessment of the technical feasibility of the project (for example, the requirements in respect of the construction work and services included in the project (including the quality level of the expected construction work or services), objective, fulfilment time and place thereof and, if necessary, the methods and resources to be utilised for carrying out the construction work or provision of the services);

5.4. the legal justification of the admissibility of the project implementation (for example, if the particular public partner or its representative is entitled to assign the project for fulfilment to the private partner and in what manner (institutional or contractual public-private partnership) it can perform this);

5.5. an assessment of the project in accordance with the estimated project costs and the expected project outputs (gains), taking into account not only the financial costs and gains, but also indirect costs and gains associated with the project implementation; and

5.6. an assessment of the feasibility of attracting European Union or other fund co-financing to implementation of the project and, if the attraction of European Union or other fund co-financing is intended, the course of acquisition of the selected co-financing (the schedule for acquisition of the co-financing, the beneficiary of the co-financing, amount and conditions for the utilisation thereof).

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6. In accordance with the characterisation of the current situation and the basis for implementation of the project, all the possible alternatives for implementing the project shall be specified, which comply with the types of a public-private partnership.

7. The comparative analysis of the alternative financing for implementing a project (including an assessment of the repayment period for the project, risk analysis and, if necessary, sensitivity analysis) shall be performed for the best of the alternatives specified in Paragraph 6 of this Regulation from the viewpoint of the most rational and effective utilisation of the financial resources of a public person, as well as for the alternative to the implementation of the project in accordance with the Public Procurement Law and, if possible, for the alternative to the project implementation, when the public partner itself continues ensuring the relevant functions.

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7.¹ If in comparative analysis of the alternative finances for implementing the project such alternative to the project implementation is utilised, when the public partner itself continues ensuring the relevant function, all the possible measures the public partner may perform for improving its activity with similar methods as a private partner shall be evaluated, and the assumptions based on the referred to principle shall be utilised in the comparative analysis of the alternative finances for implementing the project.

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8. The comparison of the alternative finances for implementing a project shall be performed, clearly indicating the assumptions that have been set out, costs, revenue and the impact of these factors on the financial indicators of the project.

9. On commencement of the comparison of the alternative finances for implementing the project, taking into consideration the characterisation of the current situation and the justification for the implementation of the project, all of the project assumptions shall be specified, which are justifiable, including:

9.1. assumptions concerning the possible length of the project implementation and the apportioning thereof (how long the construction and renovation or reconstruction time period, period for provision of services shall be);

9.2. assumptions concerning the project costs (indicating, what are financial investments, maintenance costs, taxes) and revenue (if expected);

9.3. assumptions concerning the project financing and financial source (indicating, how much of the financing required for the project will be available from the resources of the public partner, what amount of financing shall be attracted from the private partner or financial resources or from other sources, when financing shall become available and in what amount, what are the allowable sponsorship acquisition costs and the loan annual interest rate);

9.4. assumptions concerning the guarantee from the resources of the State budget (if such are intended) provided by the public partner;

9.5. assumptions concerning the conditions of making availability payments (if such are required) by the public partner;

9.6. assumptions concerning the requirements necessary in respect of for the length of the activity of the private partner in the field, where the project shall be implemented (if such are required); and

9.7. assumptions concerning the co-financing rate and its impact on the proposed payment (which the public or private partner perform with each other or which are collected from end users during the validity period of the public-private partnership agreement), if it is intended to attract European Union or other fund co-financing for the implementation of the project.

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10. The comparative analysis of the alternative finances of a project implementation shall include an assessment of the impact of each alternative to the project implementation on the local government or State budget, and shall consist of:

10.1. an assessment of the budget amount and long-term liabilities of the public partner;

10.2. an assessment of the impact of the payments of the public partner planned in the project on the local government or State budget in the long-term; and

10.3. an assessment of the impact of the revenue related to the project on the local government or State budget in the long-term.

11. In performing the comparison of the alternative finances for implementing a project, the discounted cash flow principle shall be applied throughout the whole implementation period of the project, utilising the macroeconomic assumptions and forecasts prescribed in the Annex to this Regulation. The Ministry of Finance shall update the numerical values of the macroeconomic assumptions and forecasts once every quarter and publish these on its Internet home page www.ppp.gov.lv.

12. In order to determine the implementation time for the project, an assessment of the repayment period for the project shall be performed – the most economically substantiated time period for the project shall be selected as the length of time for implementing the project, where it shall be possible to gain a financial or economic benefit from the finances invested, resources or generated assets. If it is necessary, the implementation time of the project shall be selected in accordance with the specifics of the relevant national economy sector.

13. In performing the comparison of the alternative finances for implementing a project, the results of the project risk analysis shall be taken into account. If in accordance with the results of the calculations of the comparison of the alternative finances for implementing the project there are several equally good project implementation alternatives (their net discounted cash flow value today does not differ by more than 10 per cent), a sensitivity analysis for the relevant alternative shall be performed, determining the main assumptions for the project, for which the change (positive or negative) of one per cent of the net discounted cash flow value today changes the base value by five percent, and calculation of the variable margins, indicating, with which percentage amount the changes for the discounted cash flow value today for the main assumption is zero.

14. The qualification (determination of the risk priority, assessing the possibility of risk occurrence and the consequences of such occurrence) and quantification (the assessment of the risk event occurring expressed in monetary terms) of the risks identified in the project implementation alternative analysis shall be performed in a project risk analysis, as well as their initial division between the public partner and private partner in the public-private partnership agreement. In performing qualification and quantification of the identified risks, a detailed justification of the assumptions utilised shall be provided and, in performing the initial division of the identified risks, their management mechanisms (for example, the payment exchanges of the public partner, penalty sanctions, if the contract is not fulfilled or is performed poorly) shall be indicated.

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14.¹ The project risk analysis shall be performed on the basis of empirical experience (risk-management experience in at least two projects implemented in the same or similar field) or, if that is impossible, utilising an alternative risk analysis method.

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15. Risk analysis shall be performed on mandatory basis for such risks as:

15.1. construction risk – related to the fulfilment of the construction work for a project (for example, related to the increase in construction costs, the occurrence of additional costs, delays in the supply of building materials, losses or damage, which have occurred as a result of construction work, but detected during exploitation, observance of the prescribed specifications);

15.2. availability risk – related to the services provided within the project (for example, related to ensuring the quality of the service provided in accordance with the prescribed specifications in the planned quantity and time period); and

15.3. demand risk – related to the demand for the services provided within the project (for example, related to a decrease or increase in the number of end users of a service, but this deviation may not have been caused due to insufficient or poor quality service, or by other circumstances that influence the quantity or quality of the provided service).

16. An assessment of the best alternative to the project implementation shall be prepared, taking into account the results of the analysis of the comparison of the alternative finances for the project implementation. The project implementation alternative that shall be considered the best alternative, shall be the one with the highest value of money – the most effective project costs and revenue combination.

17. If the highest value of money is possessed by one of the analysed project implementation alternatives, which complies with public-private partnership, the type of a public-private partnership agreement and the intended contract value shall be specified in the assessment of the best project implementation alternative.

III. Provision of an Opinion Regarding Financial and Economic Calculations

18. The person or institution (hereinafter – applicant) specified in Section 14, Paragraph three of the Public-Private Partnership Law after performing the financial and economic calculations shall submit the referred to calculations to the Ministry of Finance and the Monitoring Institution.

19. Financial and economic calculations shall be submitted to each of the institutions referred to in Paragraph 18 of this Regulation in one hard copy, as well as written to the electronic data storage medium (drawing up the financial models in *Microsoft Office Excel* an equivalent format, which provides transparency of the formulae utilised in the calculations).

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20. If in the financial and economic calculations all the calculations performed are not reflected in detail, if justification for a value or utilisation of an assumption has not been provided or additional information is necessary for evaluation of the assumptions included in these calculations and risks, the Monitoring Institution shall send a letter to the applicant regarding the necessity for additional information or for updating the financial and economic calculations (indicating the specific deficiencies in the calculations). The Monitoring Institution shall also send this letter to the Ministry of Finance for information.

21. An applicant shall submit the information referred to in Paragraph 20 of this Regulation in one hard copy, as well as written to the electronic data storage medium. The information referred to shall be submitted to each of the institutions referred to in Paragraph 18 of this Regulation.

22. In preparing an opinion regarding the assumptions included in the financial and economic calculations and the risk allocation between the public partner and private partner and the intended contract value, a Monitoring Institution shall examine, whether:

22.1. the assumptions utilised in the financial and economic calculations have been justified and all calculations performed present the correct results and comply with logical business practice;

22.2. the risk analysis performed for the financial and economic calculations for project implementation alternatives is correct and the initial risk allocation between the public and private partner is beneficial from the viewpoint of a rational and effective utilisation of public sector resources, as well as examine its compliance with the Public-Private Partnership Law ;

22.3. the type of a public-private partnership agreement and contract value determined by the best alternative for the project implementation complies with the Public-Private Partnership Law and the economic calculations; and

22.4. the amounts of the intended payments (which the public or private partner shall perform between each other or which shall be collected from end users during the validity period of the public-private partnership agreement) are justified.

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23. The Monitoring Institution shall, within a period of 20 working days after receipt of the financial and economic calculations or their amendment, send the prepared opinion to the Ministry of Finance and the applicant.

24. The Ministry of Finance shall evaluate financial and economic calculations, taking into account the opinion of the Monitoring Institution.

25. If additional information is required regarding the conditions referred to in the financial and economic calculations, the Ministry of Finance shall send the applicant a letter regarding the necessity for the additional information, indicating particular conditions, for which the additional information is necessary. The Ministry of Finance shall also send this letter to the Monitoring Institution for information.

26. An applicant shall submit the information referred to in Paragraph 25 of this Regulation in one hard copy, as well as written to the electronic data storage medium. The information referred to shall be submitted to each of the institutions specified in Paragraph 18 of this Regulation.

27. In preparing an opinion regarding the estimated impact of the conditions referred to in the financial and economic calculations on the amount of long-term liabilities of the State budget and the government debt, the Ministry of Finance shall evaluate:

27.1. the estimated impact of the conditions referred to in the financial and economic calculations on the amount of long-term liabilities of the State budget and the total impact on the government debt in accordance with the Law On Budget and Financial Management; and

27.2. the estimated impact of the conditions referred to in the financial and economic calculations on the State budget deficit, the amount of long-term liabilities and government (general government sector) debt in accordance with the conditions of the European System of National and Regional Accounts (ESA-95) of the European Union.

28. In evaluating the estimated impact of the conditions referred to in the financial and economic calculations on the amount of long-term liabilities of the State budget and the total impact on the government debt in accordance with the Law On Budget and Financial Management, the Ministry of Finance shall evaluate:

28.1. the information regarding the necessary finances and the financing sources thereof for the whole of the project implementation period, yearly operation costs and potential revenue during the whole validity period of the public-private partnership agreement;

28.2. the entered into and planned liabilities of the public partner by year (loans, guarantees, other long-term liabilities);

28.3. the financial report of the private partner for the previous year; and

28.4. the possibility of the European Union fund co-financing indicated in the financial and economic calculations for the project.

29. In evaluating the estimated impact of the conditions referred to in the financial and economic calculations on the State budget deficit, the amount of long-term liabilities and government (general government sector) debt in accordance with the conditions of the European System of National and Regional Accounts (ESA-95) of the European Union, the Ministry of Finance shall allocate the public-private partnership assets as private partner assets, if the following criteria are observed:

29.1. the private partner assumes most of the construction risk and most of the availability or demand risk. The conditions of and the total of the risk factors of the public-private partnership agreement shall be considered to be most of the risk assumed, that provide for the relevant partner to cover more than 50 per cent of the possible relevant risks occurrence costs;

29.2. if the conditions of the public-private partnership agreement provide for handing over the created assets into the possession of the public partner, then the amount of the expected payments by the public partner for these assets during the validity period of the public-private partnership agreement shall correspond to the evaluation of the economic value of the assets;

29.3. if the conditions of the public-private partnership agreement provide for co-financing from the public partner for covering the initial project costs, that shall be less than 50 per cent of the construction and renovation or re-construction asset costs;

29.4. if the conditions of the public-private partnership agreement provide for the public partner's guarantee to the sponsor of the project regarding the repayment of financing attracted by the private partner, then there is a negligible probability regarding the guarantee coming into effect;

29.5. the conditions for making public partner payments (if such are made) do not include a direct payment component by the private partner for recovery of an increase in costs;

29.6. [22 March 2011];

29.7. the additionally selected criteria by the Ministry of Economics, if it is a party to the provision of an evaluation in the case referred to in Paragraph 31 of this Regulation.

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30. In evaluating the estimated impact of the conditions referred to in the financial and economic calculations on the State budget deficit, the amount of long-term liabilities and government (general government sector) debt in accordance with the conditions of the European System of National and Regional Accounts (ESA-95) of the European Union, the public-private partnership assets shall be allocated as private partner assets, if at least one of the criteria referred to in Paragraph 29 of this Regulation is not observed.

31. If required, the Ministry of Finance may involve the Ministry of Economics in the provision of the evaluation referred to in Sub-paragraph 27.2 of this Regulation.

32. The Ministry of Finance shall specify the following in a prepared opinion:

32.1. those public-private partnership assets accounting conditions referred to in the financial and economic calculations, which are the basis for a provisional conclusion that the public-private partnership agreement may cause or not cause an undesirable effect on the State budget deficit, the amount of long-term liabilities and government (general government sector) debt in accordance with the conditions of the European System of National and Regional Accounts (ESA-95) of the European Union;

32.2. the total impact of the project on the amount of long-term liabilities of the State (local government and State) budget, its breakdown over years, as well as its total impact on the government debt; and

32.3. regulations, which must be observed, so that the public-private partnership agreement does not cause an unforeseen undesirable impact on the amount of long-term liabilities of the State budget and the government debt.

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33. The Ministry of Finance shall send the prepared opinion to the applicant and the Monitoring Institution within a period of 20 working days after receipt of the opinion submitted by the Monitoring Institution or the additional information referred to in Paragraph 25 of this Regulation. If the Ministry of Finance involves the Ministry of Economics in the provision of the evaluation referred to in Sub-paragraph 27.2 of this Regulation, the Ministry of Finance shall inform the applicant thereof in writing and send the prepared opinion to the Ministry of Economics within a period of 15 working days after receipt of the evaluation by the Ministry of Economics.

Prime Minister

V. Dombrovskis

Acting for the Minister for Finance –
the Minister for the Interior

L. Mūrniece

**Macroeconomic Assumptions and Forecasts for Carrying Out
Financial and Economic Calculations in Latvia**

[22 March 2011]

1. When performing comparison of the alternative costs for implementing a project, the following macroeconomic assumptions shall be utilised for changes in the price index (per year):
 - 1.1. changes in the consumer price index (as a percentage);
 - 1.2. gross domestic product deflator (as a percentage); and
 - 1.3. gross fixed capital formation deflator (as a percentage).

2. When performing comparison of the alternative costs for implementing a project, the following medium-term and long-term macroeconomic forecasts shall be utilised (per year):
 - 2.1. changes in gross domestic product, constant prices (as a percentage);
 - 2.2. changes in gross domestic product per capita, constant prices (as a percentage);
 - 2.3. employment changes (as a percentage); and
 - 2.4. gross wage changes, constant prices (as a percentage).

3. When performing comparison of the alternative costs for implementing a project, the following discount rates shall be utilised:
 - 3.1. the actual discount rate for the alternative to the project implementation in accordance with the Public-Private Partnership Law; and
 - 3.2. the actual discount rate for the alternative to the project implementation in accordance with the Public Procurement Law.

Acting for the Minister for Finance –
the Minister for the Interior

L. Mūrniece