



Indochina notes

LEGAL UPDATES ON INVESTMENT, INFRASTRUCTURE AND FINANCE

Highlights of 2007

Investment

Infrastructure

Banking and capital markets

Highlights of 2007

February

The Government updated the Corporate Income Tax laws in Decree 24 dated 14 February 2007. This Decree abolished tax preferences formerly available to shareholding companies after equitisation and to businesses using domestic materials.

March

The Ministry of Finance (MOF) issued a number of regulations on the securities market: (i) Circular 17 detailed the files required for registration of public offerings; (ii) Circular 18 covered the purchase by a public company of its own shares, the sale of treasury shares and the issuance of shares to employees; (iii) Decision 15 provided a model charter for listed companies; (iv) Decision 13 provided a model prospectus; and (v) Decision 12 set some useful standards for corporate governance of listed companies. To bolster the message, the Government provided new penalties for violators of the securities rules but the maximum fine stipulated under Decree 36 is VND70m (US\$4,400), which is unlikely to deter too many would-be Jérôme Kerviels.

April

New securities companies proliferated in 2007. The MOF's Decision 27 dated 24 April 2007 now regulates the establishment and operation of these companies in Vietnam. However, many investment professionals (foreign and local alike) still await a decree on foreign

investment in the securities market. The draft decree is being discussed internally by the MOF and the State Securities Commission.

May

Securities companies were not the only ones in vogue: asset management companies also had another good year and again the regulator's eye lit upon them. The establishment and operation of domestic asset management companies was regulated by virtue of Decision 35 of the MOF dated 15 May 2007. The funds they manage were regulated a month later under Decision 45 of the MOF dated 5 June 2007.

In stark contrast to the development of the capital markets have been the wayward attempts to involve the private sector in infrastructure. After a long and fruitless gestation period, the Government did eventually issue Decree 78 on 11 May 2007 to update the legal basis for build, operate, transfer (BOT) projects. Although the new BOT Decree theoretically introduces some new ways for the private sector to invest in infrastructure, it has failed to address adequately many of the issues that rendered the law ill-equipped to support foreign involvement in sizable infrastructure projects. While the BOT framework is now marginally more developed, there are still too many gaps, uncertainties and potential conflicts in the law.

June

Another area troubling the think tanks is the increasing realisation that the legal framework for equitisations of large-scale companies is defective and that this could

severely retard the state-owned sector reform. New Decree 109 of the Government dated 26 June 2007 was the umpteenth tweak to the equitisation regulations aimed at boosting the conversion of state-owned enterprises (SOEs) into joint stock companies. Decree 109 requires the price at which shares are sold to a strategic investor to be not lower than the average successful auction price (previously, a 20 per cent reduction from the auction price was allowed). It allows a foreign investor to be a strategic investor. And it does not contain the restriction on the number of shares sold to strategic investors that existed before.

July

July was an important month for the Government of Vietnam: the National Assembly approved a reshuffle of its cabinet structure. But despite being busy with the reorganisation, the Government issued Decree 119 dated 18 July 2007 on tobacco manufacturing and trading. This continues the limitations on the participation of foreign investors in tobacco production and trading.

September

The 2005 Enterprise Law (the EL) and the 2005 Investment Law (the IL) left open numerous issues. On 5 September 2007, the government issued Decree 139, which provides some guidelines on the establishment, management, operation, restructuring and liquidation of enterprises operating in Vietnam. Notably, Decree 139 officially lifted the 30 per cent cap on foreign ownership in domestic unlisted companies (except for banking and other service sectors specifically excluded by Vietnam's World Trade Organization commitments). Procedural issues remain.

October

With cooling stock markets, the real estate market took off again. The Government issued Decree 153 dated 15 October 2007 providing detailed regulations and implementing guidelines on the Law on Real Estate Business, such as rules applicable to the sales of property 'off plan', the financial requirements applicable to those wishing to engage in real estate business, the conditions for licensing property brokers and valuers, and the limitations applicable to the transfer of real estate projects under construction.

November

In November, the National Assembly issued a number of laws, including:

- the Law on Personal Income Tax, under which Vietnamese and foreigners will be subject to the same tax rates from 2009;
- the Law on Quality of Products and Commodities;
- the Law on Chemical Substances; and
- the Law on Judicial Assistance.

Also in November, reflecting the spectre of inflation hanging over the country, the Government increased the minimum salary for employees in domestic and foreign-invested enterprises (FIEs).

Investment

New Law on Personal Income Tax

The new Law on Personal Income Tax (PIT Law) was adopted by the National Assembly on 21 November 2007. From 1 January 2009, the PIT Law will replace the current Ordinance on Personal Income Tax adopted by the National Assembly on 19 May 2001 (PIT Ordinance) and its implementing regulations. The key changes are outlined below.

Equal tax rates for Vietnamese and foreigners

Vietnamese and foreigners will be subject to the same tax rates as follows.

Tax level	Portion of taxable income per month (VND million)	Tax rate (per cent)
1	Up to 5	5
2	Over 5 to 10	10
3	Over 10 to 18	15
4	Over 18 to 32	20
5	Over 32 to 52	25
6	Over 52 to 80	30
7	Over 80	35

This compares with the following tax rates that currently apply to foreigners.

Grade	Average monthly income/person (VND million)	Tax rate (per cent)
1	Up to 8	0
2	Above 8 up to 20	10
3	Above 20 up to 50	20
4	Above 50 up to 80	30
5	Above 80	40

Lower maximum rate

The maximum tax rate has been reduced to 35 per cent from 40 per cent.

Foreigners to pay more

Despite the lower maximum rate, as there are more progressive tax levels some foreigners may have to pay more tax than now, whereas most Vietnamese will have to pay less. For example, from 1 January 2009, a foreigner with a monthly gross income of \$5,000 will have to pay approximately VND16.95m, whereas currently he has to pay VND16.2m. On the other hand, a Vietnamese employee with a monthly gross income of \$5,000 will have to pay VND16.95m under the new PIT Law, as compared with the current VND23.5m.

Deductions

For the first time, certain deductions will be allowed against income: VND4m per month for the taxpayer himself, plus VND1.6m for each of his dependants. A person whose income is VND10m a month and who has two dependants will have to pay PIT as follows.

- Under the current PIT regulations: VND10m minus VND5m (the minimum taxable income) x 10 per cent = VND500,000.
- Under the PIT Law: VND10m minus VND4m (the deduction applied to the taxpayer himself) minus VND1.6m x 2 (the deduction applied to the two dependants) = VND2.8m. At this level, the tax rate applied is 5 per cent and, therefore, the payable amount will be VND2.8m x 5 per cent = VND140,000.

More categories of taxable income

- Individuals owning private businesses currently pay corporate income tax at the rate of 28 per cent. After 1 January 2009, income from private businesses will be subject to PIT.
- Income received from real property transfer is subject to a land use rights transfer tax or dwelling registration tax. After 1 January 2009, income from real property transfers will be taxable at 25 per cent of the profit made.
- Income from securities trading, which has up until now been 'temporarily' exempt from tax, will, from 1 January 2009, be taxable under the PIT Law.

Lower tax rates for visiting foreigners

For foreigners staying in Vietnam for fewer than 183 days in a 12-month period, a more favourable tax rate of 20 per cent will be applied to Vietnam-source income, irrespective of where the income is paid (currently, the rate is 25 per cent). A non-resident's income from Vietnamese securities will be subject to tax at 5 per cent, except that income from the transfer of capital in a Vietnamese organisation will be taxed at 0.1 per cent of the value of the transaction.

Minimum salary levels

On 16 November, the Government issued a number of documents increasing the minimum salary in domestic enterprises and FIEs.

- Decree 166 increased the minimum monthly salary of workers in normal working conditions in domestic companies to VND540,000 from VND450,000.
- Decree 167 specified the minimum monthly salary of workers in normal working conditions in domestic companies located in (i) urban districts of Hanoi and Ho Chi Minh City (VND620,000) and (ii) rural districts of Hanoi and Ho Chi Minh City and some other urban districts in other major cities (VND580,000).
- Decree 168 increased the minimum monthly salary of workers in FIEs to VND1m for enterprises operating in urban districts of Hanoi and Ho Chi Minh City (up from VND870,000); VND900,000 for enterprises operating in rural districts of Hanoi and Ho Chi Minh cities, urban districts of Hai Phong City, Ha Long City, Bien Hoa, Long Khanh, rural districts

of Nhon Trach, Long Thanh, Vinh Cuu and Trang Bom in Dong Nai province, Thu Dau Mot town, rural districts of Thuan An, Di An, Ben Cat and Tan Uyen in Binh Duong province and Vung Tau (up from VND790,000); and VND 800,000 for enterprises operating in other localities (up from VND710,000).

Equitisation

The equitisation regulations change with the predictability of the monsoons in Saigon. Decree 109 of the Government dated 26 June 2007 (see our December 2007 edition) provides the latest platform. There are numerous financial issues that are not addressed in that document. The MOF has seen fit to address some of them in Circular 146 dated 6 December 2007, but sadly they are not the most important ones.

- One useful clarification is that legal entities within the same business group as the company being equitised will not be considered as strategic investors. Perhaps slightly less relevantly, the same is true of trade unions in the equitised enterprise.
- Circular 146 lists the persons and organisations who are not allowed to purchase shares of equitised SOEs during the initial public offering process, including members of the Committee for Enterprise Equitisation (CEE) (except representatives of the enterprise), financial institutions providing valuation consultancy services to the enterprise and individuals employed by such institutions, plus underwriters and individuals employed by them.
- One of the problems with the current auctions of SOEs is that many shares that are subscribed are not in fact purchased when bidders realise they have overbid and prefer to give up their 10 per cent deposit instead. If the number of unsold shares is less than 30 per cent of the shares sold, the CEE can now offer these unsold shares directly to any investor who participated in the bidding at a price not less than the average successful bid price in the auction. If the number of unsold shares is higher than 30 per cent, the CEE can sell them at another auction, with the starting price being not lower than the lowest successful bidding price. If the shares are still not sold out after the second round of bidding, the CEE can engage an underwriter.
- Strategic investors must pay a deposit of 10 per cent, calculated on the starting bid price. If they do not conclude the purchase, they will lose the deposit.

Infrastructure

Energy development strategy

There is an obvious need for greater development of energy projects, though most people would say there is a greater need for implementation than strategy planning. But Vietnam has strong central planning roots, so on 27 December 2007, the Prime Minister signed Decision 1855 approving the national energy development strategy to 2020, with a vision to 2050. The strategy sets out development plans for specific energy sectors, including electricity, coal, oil and gas, and new energy sources. It also contains policies for national energy security and energy prices and priorities for the development of new energy sources and environmental protection. All this allows for plenty more detailed planning.

Electricity sector

Ownership of both electricity production and distribution will apparently be diversified. There will be pilot equitisations of hydroelectric power plants and electricity distribution companies, which, if successful, will be expanded. Competitive electricity retail markets will be set up after 2022. The first nuclear power station will be put into operation in 2020. By 2050, nuclear power will account for 15-20 per cent of the total national commercial power output.

Oil and gas sector

The good news here is that the regulator will be separated from business. PetroVietnam will eventually no longer be able to enjoy the double game. The legal framework for oil and gas activities will be enhanced, which will not be hard in midstream and downstream activities, for example gas transportation and distribution, where such framework hardly exists despite numerous efforts by multilateral donors. Foreign investors will be encouraged to contribute capital to oil refining joint ventures and to participate in the distribution market (up to a certain market share). An oil and gas trading market will be created by 2015.

Coal sector

All economic sectors are encouraged to invest in coal production, sorting and distribution. Coal production companies will be equitised over time, with a view to gradually creating a coal market by 2015. The strategy

encourages exploration outside the main Quang Ninh coal-producing area, particularly in the Red River delta area.

Government guarantee of foreign exchange availability

Government guarantees of foreign exchange availability have been rare in the private sector. A mechanical framework for such conversion exists in Decision 218. But there is no published policy on when to grant such guarantees. This may change. On 19 January 2008, the Government Office issued Official Correspondence 457 approving the State Bank of Vietnam's (SBV's) proposal to amend the regulations on government guarantees in foreign currency. The Prime Minister also requested (i) the Ministry of Planning and Investment to report on key national BOT investment projects in energy, transport and waste treatment that need to have foreign currency guarantees and (ii) the SBV and MOF to prepare an annual foreign currency government guarantee limit for approval of the Prime Minister.

Environmental fees applicable to solid waste

Under Decree 174 of the Government dated 29 November 2007, organisations discharging solid wastes must now pay environmental fees (except for those disposing of solid waste by themselves or signing a solid waste disposal contract that complies with environmental standards). The maximum environmental fee for (i) ordinary solid waste is VND40,000 per tonne and (ii) hazardous solid waste is VND6m per tonne.

Public Telecoms Service Fund

Under the Prime Minister's Decision 186 dated 3 December 2007, telecoms companies operating in Vietnam are required to make contributions to the Public Telecoms Service Fund. Such contributions are calculated based on turnover:

- 3 per cent of turnover for mobile telecom services;
- 2 per cent of turnover for international telephone calls and international channel leasing services; and
- 1 per cent of turnover for local long distance calls and local channel leasing services.

Coal industry

The Ministry of Trade and Industry issued two circulars dated 22 October 2007 on the coal industry: (i) Circular 4 on the conditions for engaging in the coal business (entrepreneurs have to satisfy certain conditions regarding business location, transportation vehicles and warehousing); and (ii) Circular 5 on the coal export business. Entrepreneurs wishing to enter into the latter have to satisfy the conditions for Circular 4, plus other conditions such as having valid coal exploitation and coal processing licences or having a valid coal sale and purchase contract.

Banking and capital markets

Joint stock commercial banks (JSCBs)

The SBV issued Decision 24 dated 7 June 2007 on the establishment and operation of JSCBs. Six months later, Decision 46 dated 25 December 2007 created stricter conditions for the establishment of new banks:

- capital contributed to a JSCB must not be entrusted to or loaned by a third party;
- credit institutions contributing capital to establish a new JSCB must ensure their compliance with prudential regulations after they have fully contributed the committed capital; and
- non-credit organisations contributing capital to establish a new JSCB must themselves satisfy certain minimum capital requirements.

Non-bank credit institutions

Non-bank joint stock credit institutions

Although certain non-bank credit institutions (NBCIs) have been set up, a general regulatory framework for the establishment of JSC NBCIs did not exist. Decision 40 dated 2 November 2007 filled this gap.

- Shareholders in a non-bank joint stock credit institution must be Vietnamese.
- A non-bank joint stock credit institution must have at least 50 shareholders. There must be at least three corporate founding shareholders, which have equity capital of at least VND200bn and total assets of VND500bn and were profitable in the preceding year. If the shareholders are credit institutions, their total assets must be at least VND3 trillion and their bad debt rate must be less than 3 per cent.

- Founding shareholders must jointly hold at least 50 per cent of the charter capital, and of this at least 50 per cent must be owned by corporate founding shareholders.
- A shareholder and its related persons can hold a maximum of 10 per cent (for an individual) or 20 per cent (for a corporation) of the charter capital. However, a corporation with charter capital of more than 1 trillion can own up to 40 per cent of the charter capital if approval is given by the Prime Minister.

Branches and representative offices (ROs)

On 9 January 2008, the SBV issued Decision 1 on opening and closing branches and ROs of NBCIs. Decision 1 supersedes and replaces Decision 24 of the SBV dated 7 January 2003. It (i) sets out different capital requirements applicable to NBCIs that have either opened or intend to open a branch, (ii) provides a more precise definition of the management and activities of transaction offices of NBCIs and (iii) creates the requirement that NBCIs must issue internal regulations before opening an RO, branch or transaction office.

An NBCI may be permitted to open a branch or RO after the first year of operation, provided it meets other requirements. Under Decision 24, an NBCI was permitted to open a branch or RO if it had operated for at least two years, its previous two years of operations were profitable and its ratio of overdue debts in the previous quarter was below 5 per cent.

The maximum number of branches that an NBCI may open is determined by the following formula:

$$n = \frac{C - Co}{VND50bn}$$

in which:

n is the number of branches permitted to be opened;
 C is the existing charter capital (in VNDbn); and
 Co is the required minimum level of legal capital that an NBCI must have at the time of making a request to open a branch (in VNDbn).

To open an RO, an NBCI must:

- have operated for at least one year;
- have a need to open a representative office to promote its operations or to seek and manage clients;

- be of sound financial condition and strictly comply with the regulations on ensuring safety in operations;
- not have breached regulations on management, operational apparatus, internal inspection and control systems; and
- have internal regulations on the management and operations of the RO.

Under Decision 24, the requirements and regulations applicable to an NBCI's application to open a branch applied equally to an application to open an RO.

Decision 1 defines a transaction office as 'a body directly under the head office or a branch office of an NBCI, with its own seal and dependent accounting'. Under the previous Decision 24, transaction offices of NBCIs lacked an express definition or regulatory guidelines. A transaction office may be established only in the city or province where the NBCI has a head office or branch office. An NBCI has to meet certain requirements to open a transaction office.

Micro finance organisations

Under Decree 28 of the Government dated 9 March 2005, small-scale finance organisations could be established by Vietnamese socio-political organisations, social organisations, socio-professional organisations, charitable and social funds and nongovernmental organisations. Other domestic and foreign organisations and individuals were permitted to contribute capital to such organisations, the objective of which was to provide micro finance activities for low income people and households. Decree 28 has now been amended by Decree 165 of the Government dated 15 November 2007, which sets stricter conditions on the establishment of micro finance organisations.

- Micro finance organisations have to be established in the form of a limited liability company under the Enterprise Law. The SBV will issue regulations on members, capital contributions and the assignment of capital.
- All micro finance organisations must have a minimum legal capital of VND5bn. Previously, micro finance organisations were only required to have minimum capital of VND500m if they did not receive voluntary savings.
- Micro finance organisations established in the form of multi-member limited liability companies must

have at least one owner who has direct experience in running a programme that offers a compulsory saving service and provides micro finance service. This owner also has to have demonstrated its ability to run a micro finance operation safely and stably during the past year. The capital contribution amount of this owner has to reach a certain level stipulated by the SBV.

Trading of unlisted shares of public companies

The MOF plans to tighten the rules on the trading of shares on the informal over the counter market. Decision 3567 dated 8 November 2007 indicates that the first step will involve the trading of the shares of a number of unlisted public companies on an experimental basis on a formal market. In phase two, shares of all unlisted public companies will be traded on the formal market. However, Decision 3567 does not provide an exact time frame for implementation.

For further information please contact

HANOI
Tony Foster
T +84 4 8247 422
F +84 4 8268 300
E tony.foster@freshfields.com

HO CHI MINH CITY
Milton Lawson
T +84 8 8226 680
F +84 8 8226 690
E milton.lawson@freshfields.com