



Indochina notes

LEGAL UPDATES ON INVESTMENT, INFRASTRUCTURE AND FINANCE

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Investment

Distribution

Vietnam has made various World Trade Organization (WTO) commitments in respect of the import and distribution of goods. The Ministry of Trade has now issued Decision 10 dated 21 May 2007 setting out a roadmap for the implementation of these commitments. Under Decision 10, foreign investors can:

- establish import and export businesses that are foreign-invested enterprises (FIEs) (either wholly foreign owned enterprises (WFOEs) or joint ventures);
- establish joint venture FIEs in the distribution sector as long as the foreigner's share of the capital is less than 49 per cent. As of 1 January 2008, this capital contribution cap is removed. As of 1 January 2009, foreign investors will be able to establish WFOEs in the distribution sector; and
- establish joint ventures or business co-operation contracts with domestic advertising companies to carry out commercial advertising services. Foreign investors' capital contributions in such joint ventures are capped at 51 per cent. From 1 January 2009, this cap will be removed.

Decision 10 also lists goods that cannot be imported, exported or distributed, as well as goods subject to phase-in periods.

Beer and other alcohol

Along with increasing wealth, it seems, comes increasing beer consumption. On 8 May 2007, the Minister of

Industry issued Decision 18 amending the Master Plan for the beer and alcohol industry of Vietnam (Decision 18). The expected production of beer has more than doubled since the 2003 Master Plan.

Decision 18, unlike Decision 58 of 2003, explicitly encourages foreign investment in the brewing and alcohol industry, especially factories having a capacity of more than 100m litres per year. Factories will be located across six different geographical areas, with a total expected investment capital (in the 2005-2010 period) of VND34,690bn (just over US\$2bn), of which VND31,809bn is for the production of beer.

Decision 18 also refers to the equitisation of HABECO and SABECO, the two leading state-owned enterprise (SOE) brewers, as one of the steps to enhance the efficiency of the industry.

Software industry

Vietnam is not India, nor does it want to be, except in respect of its software business. On 12 April 2007, the Prime Minister (PM) issued Decision 51 approving a programme for the development of the software industry of Vietnam until 2010 (Decision 51). This Decision suggests that the Government will grant all necessary favourable conditions for investment in the software industry to develop it as a significant part of the country's economy.

Among several targets set out in Decision 51 (targets were beloved of central planners well before Tony Blair got to them):

- the industry should have total revenues of \$800m by 2010, of which 40 per cent will be generated from exports;
- Vietnam will be one of the leading countries in the world in terms of foreign direct investment attracted into the software sector; and
- Vietnam will be one of the top 15 software processing countries in the world.

The policies that will enable the software industry to reach these targets include:

- introducing better laws and enforcement in respect of intellectual property rights – a policy that is now being promoted in the press;
- introducing better laws on the import and export of software, where over the years taxes in particular have not helped industry development;
- improving the infrastructure for the software industry, another major obstacle;
- encouraging foreign investment, especially in (i) information technology (IT) training establishments (including private training schools and universities); (ii) establishments for developing software products and providing software services in Vietnam; and (iii) venture capital investment funds aimed at the IT sector (the last is curious, as there are currently more funds than investments); and
- increasing the number of foreign employees working in foreign owned software enterprises.

Aviation

Vietnam Airlines is essentially only one airline operating domestically in Vietnam. For a monopoly it is not bad. Planes are more or less on time except when leaders take them off to Cuba. Service is acceptable even if somewhat unexceptional. The deal announced by Qantas to buy a minority stake in Pacific Airlines may provide a little further spark to Vietnam Airlines. But neither this, nor the recent issuance of Decree 76 of the Government dated 9 May 2007 (Decree 76), is likely to result in a free-for-all in the Vietnamese aviation sector. The Government is far too control oriented to allow any such thing to happen in such a sensitive sector.

Decree 76 sets out some conditions that must be satisfied for investors to apply to establish an airline. In particular, the minimum required legal capital for an airline providing domestic commercial service and

operating 1 to 10 airplanes is VND200bn (approximately \$12.5m). The required minimum legal capital increases to VND400bn if an airline operates 11 to 30 aircraft and VND500bn if it operates more than 30 aircraft. If the airline were to provide international commercial aviation service, the minimum required legal capital would be substantially higher.

Of some comfort to safety-conscious passengers, the maximum age of a second-hand airplane at the time of initial import into Vietnam to transport passengers is 10 years and it can be no more than 20 years old at the time of termination of the lease agreement.

Decree 76 caps foreign ownership in a foreign-invested airline at 49 per cent of the charter capital. The maximum permitted shareholding by a single foreign entity is 30 per cent. One-third of the managers of a foreign-invested airline, including the director, vice director, chief accountant and chief operating officer, may be foreign nationals.

The PM would have to approve the establishment of a new foreign-invested airline before the Ministry of Transport and Communications could license it.

SOE reform

Unlike the airplanes in Vietnam, which are generally quite new – the last Tupolev was taken out of active service in 1997 – the railways take one back to a different age. It takes all night to get from Hanoi to Lao Cai, a mere 200km to the north. The trip from Hanoi to HCMC, while quicker than it used to be, is still best measured in days rather than hours. So the PM's approval in Decision 621 dated 16 May 2007 of the plan for renovation of the Vietnam Railway Corporation (VRC) in the period 2007-2010 is welcome news. The railways will not be the only focus. The management consultants look as if they have had a hand: the railways will use their assets to participate in the finance, securities, telecoms, real estate and insurance sectors.

The PM also approved the plan for renovation of certain SOEs under the control of the Ministry of Culture and Information for the period 2007-2010 in Decision 620 dated 16 May 2007. Under Decision 620, the following companies will be equitised:

- in 2007 – Tran Phu Printing Company, Printing and Cultural Products Company, Printing Equipment

- Import and Export Company, Urban and Cultural Work Construction Consultancy Company, Cultural Equipment Import and Export Company, Television Technology Development Company, Central Art Company, Culture Development and Import and Export Company, and Book Distribution Company Region II; and
- in 2008 – Vietnam Film Company, Film Company No. I, Giai Phong (Liberated) Film Company, Cartoon Company, Dong Mo Tourism Services and Aquaculture Company.

Infrastructure

BOT regulations

There is a growing need for the development of Vietnam's poor physical infrastructure. As the American Chamber of Commerce stated at the Vietnam Business Forum in May 2007:

'Infrastructure, especially seaports and electric power, is the most important factor now for firms considering investment in Vietnam. Infrastructure constraints threaten foreign direct investment in manufacturing and exports. Private sector participation in infrastructure development, finance, and management is needed urgently, especially in electric power and deep-water seaports.'

Over the 13 years that this firm has had offices in Vietnam, there have been only two successful foreign-invested build, operate, transfer (BOT) projects in the power sector and one (arguably irrelevant) small foreign-invested BOT project in water. No foreign-invested BOT contracts have been signed since 2001. Since 1995, numerous foreign-invested BOT projects have been tried; some have been licensed before failing at the financing stage; and others have failed completely to get off the ground.

The Government has now issued a new decree relating to BOT projects. The important question for Vietnam is whether this will make any difference or whether, like second marriages, this will prove to be a triumph of hope over experience.

The decree in question, Decree 78 of the Government dated 11 May 2007 on investment in the form of BOT, BTO and BT contracts (the New BOT Decree), replaces the

previous BOT regulations applicable to foreign investors, Decree 62 of the Government dated 15 August 1998, as amended, and regulations applicable to domestic investors, Decree 77 of the Government dated 18 June 1997. These replaced even earlier BOT decrees that dated back to 1993. Our view is that the New BOT Decree is insufficient to make large-scale foreign investment in BOT projects more likely to succeed and to reverse the rather sorry record of the last decade. A truly common and clearly defined legal framework has not yet been achieved. The New BOT Decree in particular takes some steps forwards and some steps back. It fiddles at the edges without making any quantum leaps.

See our briefing *Infrastructure development in Vietnam: a new BOT decree*, July 2007, for further information.

Administrative fines – mineral law

On 10 May 2007, the Government issued Decree 77 (Decree 77) to amend a number of articles of Decree 150 dated 29 April 2004 on the administrative fines applicable in respect of mineral law violations (Decree 150).

To prevent the exploitation of minerals without a permit, Decree 77 increases fines from VND50m to up to VND80m. To facilitate the fair application of fines, Decree 77 provides for a clear range of fines for each kind of mineral illegally exploited, instead of providing a general range of fines for all kind of minerals as before.

Actions such as not registering basic geological mineral resource survey plans with the competent authority or not notifying such authority of exploration plans and exploitation plans previously could have drawn a fine up to VND2m. Under Decree 77, the maximum fine for such violations has been reduced to VND500,000.

Decommissioning – oil and gas

While (smaller) investors are flocking into Vietnam for their share of the oil and gas pie, the Government is turning its thoughts to what these same investors would leave behind when it is time for them to leave. Decision 40 of the Government dated 21 March 2007 goes some way to resolving this issue by providing detailed regulations on the decommissioning of fixed installations, equipment and facilities used in the oil and gas industry.

Companies are required to decommission rigs and equipment in a safe and ecologically sound way. Within

the first year of operation, companies have to set up a fund to ensure that decommissioning obligations are met.

Financial and capital markets

Foreign exchange

On 13 December 2005, the Vietnamese Government passed Ordinance 28 on foreign exchange, with the stated aim of liberalising Vietnam's foreign exchange regime. This marked the beginning of a confusing period in the annals of Vietnamese foreign exchange. The new 'liberal' Ordinance 28 proclaimed that all current transactions were to be conducted freely, but the only implementing regulations available were to be found in Decree 63 on foreign exchange controls and Circular 01 on foreign exchange controls, originally passed in 1998 and 1999, respectively. As a result there was a general lack of guidance as to what the liberalisation of Vietnam's foreign exchange regime actually entailed in practice.

One year after the issuance of Ordinance 28, the passage of Decree 160 clarified the issue somewhat. However, the fog of confusion was not completely lifted. Decree 160 repealed Decree 63 and did give a clearer idea of what the liberalisation of Vietnam's foreign exchange regime means. In contrast to Decree 63, residents and non-residents are no longer required to present source documents certifying the discharge of tax obligations when purchasing, remitting or carrying foreign currency overseas in the fulfilment of current transactions.

Decree 160 also gave a tantalising glimpse of freedoms that had previously been denied. Vietnamese individuals were to be allowed to borrow from foreign entities and to conduct indirect investments offshore. This liberalisation still remains theoretical, as it awaits implementing regulations. These are due to be issued by the State Bank of Vietnam (SBV) in the indeterminate future. The regulations on offshore indirect investment are particularly eagerly awaited by Vietnam's financial community, as they will cover offshore investment by both individuals and entities. Under the old foreign exchange regime, the only guidance as to offshore indirect investment by Vietnamese entities was a statement in Circular 01 that residents could invest in offshore valuable paper 'upon approval of the State Bank' – there were no guidelines as to how such approval could be obtained. Until the regulations are issued, the position remains the same.

There is also a move towards reducing the dollarisation of the Vietnamese economy. Ordinance 28 caused some alarm bells with an article that appeared to severely circumscribe the transactions that could be performed in foreign exchange without the permission of the PM, to the extent that it was questionable whether foreign nationals could receive salaries otherwise than in Vietnamese dong. Decision 160 has a more reasonable list of exceptions to the general prohibition on the use of foreign exchange within the territory of Vietnam, and it is now clear that foreign nationals may receive their salary in foreign currency from both resident and non-resident organisations.

Nevertheless, confusion remains about Vietnam's foreign exchange regime. Circular 01 has not been explicitly repealed, and the vagaries of Vietnamese legislative interpretation mean that, depending on whom you talk to, it is considered repealed, still in force or repealed but nevertheless still applicable to the extent that it is not inconsistent with Decree 160. Parties with transactions involving foreign exchange in Vietnam would do well to remember that Circular 01 may not yet have been repealed and to seek specialist advice on the extent to which it might still apply.

Another point to watch is offshore bank accounts. According to one possible reading of the relevant provision of Decree 160, it is illegal for most foreigners who have resided in Vietnam for more than 12 months to open an offshore bank account – which will come as a surprise to expatriates who regularly remit their US\$-denominated salary back home.

Vietnamese joint stock commercial banks – foreign ownership

There has been a run on the banks in Vietnam over the last couple of years, but the run has been by foreign investors to invest in local Vietnamese banks. Foreign investors were restricted, though, to ownership of 10 per cent, which was hardly enough to give them much cause to add their know-how to their money. The SBV therefore drew up plans to increase the ownership interest to foreign investors. Unfortunately, between draft and issuance, a stock market bubble – led by local banks – intervened. The Government then scaled back the SBV's intentions.

Thus Decree 69 of the Government dated 20 April 2007 on the purchase of shares by foreign investors in Vietnamese joint stock commercial banks delivered less than expected:

- the total of all shares owned by all foreign investors (including existing foreign shareholders) and affiliated persons remains at 30 per cent;
- the cap on the shareholding by a foreign strategic investor and affiliated persons has been raised from 10 to 15 per cent;
- there is scope for an increase (up to 20 per cent) in the shareholding by a foreign strategic investor if permission is obtained from the PM;
- foreign strategic investors are defined as reputable foreign credit institutions with financial capacity and the ability to provide assistance to a Vietnamese bank; and
- shareholdings of other foreign credit institutions and foreign investors (not being foreign credit institutions), meanwhile, have been capped at 5 per cent and 10 per cent, respectively.

The Vietnamese bank must satisfy various conditions to be allowed to sell shares to foreigners. Conditions also apply to foreign credit institutions purchasing shares in the bank, including minimum total assets of \$20bn in the year before it registers to buy bank shares, international operating experience and provision of an undertaking to provide assistance to the Vietnamese bank.

Vietnamese joint stock commercial banks – increase in charter capital

The joint stock banks were taking advantage of the stock market bubble to raise capital that they did not need. The SBV responded with new regulations providing for stricter and more detailed examination and approval of requests from joint stock banks to increase their charter capital. Tighter regulations are supposed to maintain sustainable growth in this fast developing sector.

The Official Correspondence 3103 dated 6 April 2007 lists the minimum information a bank must provide in its plan to increase its charter capital, including information on (i) the particular need to increase charter capital and the capital required for each project; (ii) the projected business effect of the new charter capital; (iii) the capability of management and their capacity to manage on the basis of the increased capital;

and (iv) the plan for implementing the capital increase during the financial year.

This official correspondence goes hand in hand with the Government's Decree 141 dated 22 November 2006, which specified that all commercial and joint venture banks must have at least VND1 trillion in chartered capital by 2008 (to be increased to VND3 trillion by 2010).

Insurance

There is still significant potential in the insurance industry even though it is facing strong competition from the stock market and the banking sector. This was recently evidenced by the interest shown in the equitisation of Bao Viet, the state insurance company (which ultimately fell flat as the result of defective equitisation regulations). But the industry is not growing as fast as it once was. So in a move to facilitate foreign investment in the insurance industry and the operation of insurance companies, the Government issued Decree 45 and Decree 46, both dated 27 March 2007.

To establish a wholly foreign owned or a joint venture insurance company, the foreign investor must (i) be an insurance company that has operated for at least 10 years; (ii) have minimum total assets of \$2bn; (iii) be allowed by the regulator in the country where its head office is located to conduct the proposed insurance business in Vietnam; and (iv) not have committed any material regulatory breach for three years before making the application to invest in Vietnam. A foreign insurance brokerage company is subject to similar conditions (other than the minimum assets requirement, which is replaced by a profitability requirement) if it wants to set up a wholly foreign owned or a joint venture insurance brokerage company.

Decree 45 no longer requires the Vietnamese party to a joint venture insurance company to hold at least 30 per cent of the charter capital.

To facilitate insurance companies' operations, Decree 45 allows life insurance companies to sell investment-linked policies to make life insurance more attractive to investors.

Decree 46 for the first time allows an insurance company to use its equity capital in excess of the minimum charter capital to invest overseas. Decree 46, however, fails to clarify that insurance companies have the right to invest

by way of direct lending. The Law on Insurance Business allows insurance companies to lend, subject to the Law on Credit Institutions. Unfortunately, no one knows how the Law on Credit Institutions (applicable mainly to bank lending) applies to insurance companies.

Decree 46 also sets out stricter capital requirements for insurance companies. A non-life insurance company must have minimum charter capital of VND300bn (previously VND70bn). A life insurance company must have a minimum charter capital of VND600bn (previously VND140bn). Although it is not clear, Decree 46 suggests that the minimum charter capital may be increased depending on the scope and areas of operation of the company. Decree 46 also sets out higher requirements regarding compulsory deposit and minimum solvency margins.

State Securities Commission (SSC)

The stock market boom appears to have taken the regulators by surprise. The PM's Decision 63 of 10 May 2007 grants the SSC additional powers to inspect, supervise and deal with securities violations. These powers have yet to strike fear into the punters.

Stock exchanges

Decision 63 also allows the Ho Chi Minh City Securities Trading Centre, the Hanoi City Securities Trading Centre and the Securities Depository Centre to be converted into independent entities.

The following day, the Ho Chi Minh City Securities Trading Centre was converted into the Ho Chi Minh Stock Exchange (HOSE) by virtue of Decision 599 of the PM dated 11 May 2007. HOSE will operate as a limited liability company in accordance with the Law on Securities, the Enterprise Law and the company's charter.

Public disclosure rules

A new Ministry of Finance (MOF) circular, Circular 38 dated 18 April 2007, regulates public disclosure requirements of publicly traded enterprises, institutions issuing and selling bonds, listed enterprises, securities companies, securities trading centres and related institutions. The new regulations require information to be adequate, exact and timely. General directors, directors and authorised representatives, among others, could be held liable (including criminally liable)

for failure to make the required disclosures or for inaccuracy.

Reports submitted to the SSC or to stock exchanges would also have to be made public under the new circular.

Securities companies

There has been an explosion in the number of securities companies being established, partly because of the low capital required for entry. The original securities companies, all of seven years old, are now immensely valuable. On 24 April 2007, the MOF issued Decision 27 promulgating regulations on the organisation and operation of securities companies (the Regulations).

Securities companies have to obtain an Establishment and Operation Licence (Licence) to conduct securities operations in Vietnam. No further licence is required, even for securities companies involved in underwriting operations (under prior regulations, a separate licence was required). Securities companies established under the previous regulations and satisfying the requirements of these regulations are not required to apply for a new Licence, except for those engaging in investment portfolio management.

To be eligible for a Licence, securities companies will have to meet stricter requirements. The trading floor will have to be at least 150 square metres. Individuals contributing more than 5 per cent of the charter capital will need to prove their financial capability. The legal capital is now substantially higher (three to eight times the former figures) and existing securities companies established under the previous law will have two years to increase their legal capital to meet the new requirement.

Any change in the charter capital or the legal representative of a securities company will require an amendment of the Licence. Similarly, transactions involving more than 10 per cent of the charter capital of a securities company will require SSC approval, unless such company is listed on a stock exchange. These new regulations will obviously provide the SSC with more power to exercise its managerial function over the organisation and operation of securities companies.

Foreign securities companies are nominally no longer required to establish joint ventures with local parties. They will be entitled to establish 100 per cent subsidiaries

in Vietnam. This flexibility is unlikely to manifest itself in practice until the WTO requires it in about five years' time.

Funds and fund management companies

A growing number of fund management companies is being established. Official reports suggest that there are currently 18 fund management companies, both local and foreign, running investment funds with a total value of more than \$12bn, though it is difficult to confirm the origin of this figure. Under Decision 35 of the MOF dated 15 May 2007 on fund management companies, only fund management companies are now permitted to manage portfolios for investors: securities companies are no longer allowed to offer such a service. The minimum legal capital for establishment of a fund management company is VND25bn (five times higher than the legal capital requirement under the old regulations). Numerous new obligations have also been imposed on fund management companies.

A regulation on foreign participation in the Vietnamese securities markets is being drafted by the MOF and is due to be released soon. This will set out the conditions for the establishment of representative offices and branches of foreign fund management companies, which are not regulated in Decision 35.

The MOF also issued Decision 45 dated 5 June 2007. Decision 45 regulates the establishment and operation of closed-end securities investment funds, member funds, and operations relating to fund management by fund management companies. It is not entirely clear whether Decision 45 permits a fund management company to manage offshore funds unless such funds are registered abroad.

New securities trading regulation

HOSE issued Decision 25 on 17 April 2007 to limit the price of shares on a company's first day of trading to 20 per cent of the issue price.

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