



Indochina notes

LEGAL UPDATES ON INVESTMENT, INFRASTRUCTURE AND FINANCE

Investment
Infrastructure
Banking and finance

Investment

Decrees implementing the investment and enterprise laws

Since the new Investment Law (IL) and Enterprise Law (EL) became effective on 1 July 2006, chaos has reigned in the investment world. No one could answer anything but the simplest questions about what the two laws meant in practice. Now, like high-energy particle physicists who crash molecules together to see what is inside, the Government has been banging heads to force the draftsman to reveal the real contents of these laws. The decrees to implement the IL and EL so far issued consist of:

- Decree 108 dated 22 September 2006 providing detailed guidelines for the implementation of the IL (Decree 108);
- Decree 101 dated 21 September 2006 on re-registration and conversion of foreign-invested enterprises (FIEs) (Decree 101);
- Decree 78 dated 9 August 2006 on overseas investment (Decree 78); and
- Decree 88 dated 29 August 2006 on business registration (Decree 88).

Implementation of IL – Decree 108

Decentralisation of investment licensing

Until now foreign investors with a desire to invest in Vietnam, however rare their money and however poor the recipient, could not do so without permission from a body sitting in Hanoi called the Ministry of Planning and Investment (MPI). The MPI had, over the years, grudgingly

granted limited licensing powers over small and simple projects to the local authorities. But, by and large, the lucrative licensing power lay in Hanoi. This will now change, at least on the surface. One of the major reforms in Decree 108 is the devolution of licensing authority from the central MPI to the provincial people's committee (PCs) and the management committees (MCs) of industrial, export processing, hi-tech and economic zones. The MCs are responsible for licensing investment projects within the zones that they manage. For all other investments, the provincial PCs will now have the right to issue Investment Certificates (ICs) for foreign and local investors.

Prime ministerial approval

Important projects will still depend on instructions from the MPI and higher so Hanoi will not lose all power. The Prime Minister (PM) must approve certain projects in sensitive sectors prior to their being licensed. These include:

- all projects of any size regarding airports, air transportation, national seaports, mineral exploration and mining, petroleum exploration, production and processing, radio and television broadcasting, casinos, cigarette manufacturing, universities, and establishing industrial, export processing and high-tech and economic zones;
- projects with capital over VND1,500bn (approximately US\$100m) in electricity; mineral processing, metallurgy, construction of railways, roads and internal waterway infrastructure, alcohol and beer production, and trading; and

- foreign-invested projects in sea transportation, postal, delivery, telecommunications and internet networks, printing and distributing newspapers and other printed matter, publishing, and independent scientific research establishments.

Investment certificates

Investors may register their investment projects if such projects have investment capital of less than VND300bn (around US\$19m), but – and it is a big qualification – only if such projects are not in a ‘conditional’ sector and are not subject to prime ministerial approval.

If they cannot register their projects, investors have to undergo a more complicated investment evaluation process, which can also lead to a refusal of permission to invest, in order to be issued an IC.

Conditional investment sectors

The IL provides a range of sectors in which investment by domestic or foreign investors is conditional. Under Decree 108, the range of conditional sectors for foreign investors is still wider. Those sectors include 13 broad areas:

- broadcasting and television;
- producing, publishing and distributing cultural products;
- exploration and exploitation of minerals;
- establishing infrastructure for telecommunications networks, and transmitting and providing internet and telecommunications services;
- establishing public postal networks and providing postal and express delivery services;
- constructing and operating river ports, seaports, terminals and airports;
- transporting goods and passengers by railway, air, road, sea and inland waterways;
- aquaculture;
- producing tobacco;
- ‘real estate business’ (the definition of this term in the real estate laws would turn all simple construction projects into conditional projects);
- import, export and distribution business;
- education and training; and
- hospitals and clinics.

Most importantly, conditional sectors for foreign investors also include all ‘investment fields under

international treaties to which Vietnam is a member and where there are commitments to limited market access to foreign investors’. The terms of Vietnam’s accession to the World Trade Organization should be released in November, which will at least enable practitioners to commence the exercise of trying to determine the range of conditional projects.

Projects in conditional sectors must satisfy certain specific conditions to be licensed. Unfortunately, Decree 108 does not set down the conditions applicable to sectors that are declared conditional. Authorities may continue to delay licensing such projects until clear guidance is issued, which the MPI will no doubt provide on an ad hoc basis when it considers it appropriate.

A more detailed analysis on Decree 108 will be published in one of our *Sector Updates* to be issued in the near future.

Re-registration and conversion by FIEs – Decree 101

Until now, FIEs have been limited liability companies governed by the Foreign Investment Law (FIL). The FIL was repealed on 1 July 2006. The EL allows existing FIEs to re-register or convert their corporate form to operate under the EL. Decree 101 provides some guidance on how to do this and also sets out the rights and responsibilities of FIEs that opt not to re-register.

FIE re-registration

Re-registration is defined as the process whereby existing FIEs register for the replacement of their investment licenses by new ICs, but do not change their corporate form.

A wholly foreign-owned enterprise with one owner can re-register as a one-member limited liability company. Foreign-owned enterprises with multiple owners and joint ventures can re-register as multi-member limited liability companies. Existing foreign-invested shareholding companies, of which there are only a handful, can re-register as joint-stock companies.

A re-registered company operates in accordance with its newly-issued IC. It inherits the legal rights and obligations of the old enterprise and may continue to use its registered name, seal, bank accounts, tax and customs codes.

Enterprises that opt not to re-register by 1 July 2008 may continue to operate in accordance with their investment licences and charters, but in other respects they must comply with the new IL and EL. Quite how a charter under the FIL will be reconciled with the new EL remains a mystery. Such companies will be permitted to amend their investment licences in some respects, but as they will not be permitted to change their authorised business or their duration of operation they will slowly ossify and then die out.

FIE conversion

Decree 101 also allows investors to 'convert' between limited liability company and joint stock company forms at the same time as re-registering. Conversion gives investors the flexibility to choose their desired corporate form.

A converted enterprise may only continue to use the investment incentives provided in its investment licence if foreign investors hold more than 30 per cent of the charter capital following conversion.

A more detailed analysis on Decree 101 will be published in one of our *Sector Updates* to be issued in the near future.

Overseas investment by FIEs – Decree 78

Very few FIEs in Vietnam have themselves invested overseas. Although regulations for this existed in the shape of Decree 22 dated 14 April 1999 (Decree 22), only six FIEs were allowed to do so. In part, this is understandable because such companies are all relatively new and often have offshore parents which can themselves invest offshore. But some joint ventures still wish to invest offshore. It will now be easier for them to do so. Decree 78 is more flexible than Decree 22 but it is unlikely to lead to an exodus of funds.

- Under previous regulations, the PM considered FIEs' overseas investment projects on a case-by-case basis. Now the PM's approval only needs to be obtained to undertake overseas investment projects in a limited number of sectors: banking and finance, insurance, telecommunications, media, broadcasting and television projects involving more than VND300bn or using state budget funds of more than VND150bn (around US\$9.4m); and investment projects in other sectors with investment capital of more than

VND600bn (around US\$37.5m) or using state budget funds of more than VND300bn.

- Overseas investment projects valued at less than VND15bn (around US\$937,000) are only required to be registered with the MPI. Projects valued at more than VND15bn must be evaluated by the MPI after consultation with relevant ministries and local PCs where the investors are located. All investment projects must then be issued with ICs by the MPI.
- Overseas investment projects in the oil and gas sector, and certain other industries in particular foreign localities, will be governed by further regulations to be adopted by the Government. These have not been issued yet.
- The PM will also issue a list of investment sectors in which investors are encouraged, restricted or prohibited from making direct overseas investment.

Business registration

The EL and IL were touted as creating a single legal regime applicable to both foreign and domestic investors. At the implementing decree level, however, the reality is rather different. One example of this is Decree 88 on business registration. This deals primarily with registration of domestic businesses, including JSCs with foreign shareholding. This is because under Decree 108, foreign investors will be issued ICs which also serve as business registration certificates. By contrast, domestic investors wishing to invest over VND15bn must first go through the domestic investment registration/evaluation process and then a separate business registration process. Domestic investors did not require any specific investment approval, just business registration certificates, before 1 July 2006.

Decree 88 changes prior law in a limited number of respects:

- the business registration fee will be based on the number of business lines registered, previously there was a fixed fee for each licence issuance or amendment;
- registration requirements for companies established after a merger, reorganisation, split, or transfer of ownership are clearer; and
- Vietnamese must be the language of company charters and will prevail over any translation into a foreign language. Good translators are now in demand by this law firm among others.

Representative offices and branches

The Vietnamese authorities have always wanted to control the activities of the big representative offices that undertook numerous activities on the borderline of legality. In particular they realised that they were losing substantial tax by allowing such operations. But they were pragmatic enough to know that if they did not allow representative offices they would either have to allow the same businesses in as subsidiaries, or not allow them in at all and thereby kill many geese that laid golden eggs. So they chose to tolerate representative office structures. Now, however, the WTO accession process has resulted in the need to allow properly established corporations into Vietnam to do many of the businesses that previously were being operated through representative offices. Having accepted this, the Vietnamese authorities no longer have any need to tolerate the representative offices in sectors where foreign investors are, or soon will be, permitted to establish companies.

As a first step in implementing the tighter approach, the Government issued Decree 72 on 25 July 2006 on representative offices (ROs) and branches of foreign business entities in Vietnam. Decree 72 will make it harder to establish and operate representative offices.

- Existing ROs and branches, except for those related to tourism, established before Decree 72 have to register before 15 February 2007 for a new RO/branch licence. This will allow the authorities to review the operations of each RO/branch.
- It will become harder to open a RO. The foreign company must have operated for at least one year in its home country before making an application to establish a RO, and it must submit audited financial reports or other evidence of such as part of the application. Under prior regulations, there was no such requirement.
- A license for a RO/branch will only be valid for five years.
- Decree 72 also sets stricter conditions relating to the head of a RO or branch. That person cannot either act concurrently as the head of another entity in Vietnam, or act as the legal representative of the foreign company without a written power of attorney from the foreign company.
- Decree 72 does not permit a RO to undertake any sales activities. There is an expectation that the authorities will become stricter in this area.

On the positive side of the ledger, Decree 72:

- no longer restricts the areas in which a branch can trade;
- removes the cap on the number of branches that a foreign investor may establish in Vietnam (previously limited to just one); and
- abolishes the requirement that the licence of ROs and branches be modified every time the number of expatriate staff changes.

Social insurance law (SIL)

Compulsory social insurance

For the last 10 years, social insurance costs for employers have been stable at a high but manageable 15 per cent of salary, with 2 per cent in addition for health. Now, under the new SIL dated 29 June 2006, rates are heading up.

| | 2007-2009 | 2010-2011 | 2012-2013 | 2014 onwards |
|----------|-------------|-------------|-------------|--------------|
| Employee | 5 per cent | 6 per cent | 7 per cent | 8 per cent |
| Employer | 15 per cent | 16 per cent | 17 per cent | 18 per cent |

The maximum salary level for contributions to the social fund will be capped at 20 times the minimum salary (currently VND450,000 per month). Thus, the salary on which insurance contributions must currently be made will be capped at VND9m per month. Employers who use a large number of highly paid workers will be favoured by the SIL (for a while at least).

Voluntary social insurance

Vietnamese people can also now participate in voluntary social insurance by contributing to the insurance fund. The voluntary social insurance regime will become applicable from 1 January 2008.

Unemployment insurance

A new unemployment insurance regime will become effective on 1 January 2009. This will result in further costs for businesses.

Law on civil aviation

Vietnam has had three airlines for years, but the average traveller knows only Vietnam Airlines. The new Law on Civil Aviation that passed on 29 June 2006 (the new law) makes some changes possible. For instance, an FIE is

allowed to provide air transportation service in Vietnam, provided that the FIE complies with certain eligibility requirements: its capital can be no greater than the percentage allowed by the Government; the legal representative of the FIE must be a Vietnamese citizen; and the number of foreigners on the board of the FIE must not exceed one-third of the total.

The new law also simplifies the conditions under which foreign airlines can open ticketing offices. An air ticket agent of a foreign airline no longer needs to obtain a certificate of satisfaction of conditions for the sale of air tickets as required previously.

A lease of aircraft conducted between Vietnamese and foreign entities has to be approved by the Ministry of Transport. The lessee is prohibited from allowing the lessor any economic benefit or use of the lessee's air transport rights during the lease period.

State-owned enterprises (SOEs)

Ownership of SOEs

The state sector of the economy has been restructured with some regularity over the last 15 years. Decree 86 of the Government dated 21 August 2006 shuffles the cards again. All 19 of the state's most important enterprises will come under the direct control of the PM. These consist of:

- Electricity of Vietnam (EVN), Vietnam Oil and Gas Group, Vietnam Coal and Mineral Group, Vietnam Post and Telecom Group, Vietnam Ship Building Group (Vinashin), and Vietnam Garment and Textile Group; and
- the SOEs operating in shipping, airlines, railway, rubber, cement, chemicals, food, coffee, paper and tobacco.

The above-mentioned SOEs will have to seek the PM's approval for:

- restructuring, dissolution or transfer of ownership;
- determination of targets, strategy, long-term planning, and business lines;
- formulation and amendment of charter;
- adjustment of the charter capital; and
- appointment, suspension or dismissal of members of the management board.

The State Capital Investment Corporation (SCIC) will own the state's interest in the remaining SOEs. Its goal is to become a latter-day Temasek.

Auctions of SOEs

One way of restructuring a loss-making SOE is to sell the whole thing to a gullible punter. For obvious reasons, not many SOEs have been successfully auctioned in this way. However, for the adventurous, the procedures for such an acquisition have at least now become clearer since the Ministry of Finance (MOF) issued Circular 51 on 12 June 2006.

To participate in an SOE auction, foreign investors are required to: open accounts at banks operating in Vietnam (such accounts will need to be registered with the State Bank of Vietnam, a bureaucratic process, so bidders should allow plenty of time); and make a deposit equal to 10 per cent of the starting bid price at least five working days before the auction.

The contract for the purchase of the SOE must be executed within two working days after the auction of the SOE.

The purchaser must make payment for the SOE within the time specified in such contract, which cannot exceed six months after the date of the signing the contract. The payment can be made in instalments, provided that the first instalment is equal to at least 70 per cent of the contract value. A discount of 10 per cent to the contract value is available in some circumstances if the buyer pays the total amount due within 10 days after signing the contract.

The handover of the SOE to the new owners must be carried out as stipulated in the purchase contract, provided that the buyers have paid 70 per cent of the contract price and have provided sufficient security for unpaid amounts.

Hotel investment in Hanoi

The hotel industry has gone from famine to feast in the last three years. Even without SARS, Hanoi hotels were giving away rooms three years ago. Now businessmen cannot find a room for any price. To attract investors in this area, the Hanoi PC issued Decision 78 on 25 May 2006 to encourage investment in four and five star hotels in Hanoi. More investment will be needed to have a material effect on investors as land prices are so high that few incumbents will release quality land at a developable price except in the suburbs. For what it is worth:

- investors will be assigned land as needed (not necessarily where needed);

- investors do not have to be involved directly in site clearance and land compensation procedures. The site clearance will be carried out by Hanoi's site clearance service (no doubt at the investors' expense);
- investors will be granted land use rights certificates with an extendable lease term of 50 years (nothing new here); and
- Hanoi will improve its infrastructure, such as road, electricity, water supply and drainage systems, up to the proposed hotel's location at its own expense (some investors in the mid 1990s are still trying to make good on similar promises).

Domestically produced equipment and materials

The MPI issued Decision 827 on 15 August 2006 promulgating the list of domestically made products in the following areas:

- equipment, machinery, replacement spare parts and special-use transport means;
- construction materials;
- essential supplies in service of the oil and gas sector; and
- materials, means and semi-finished products in the shipbuilding industry.

This list will be the basis for the calculation of import duty and value-added tax reductions and exemptions upon import of products for investment projects.

Infrastructure

Oil and gas

Vietnam Oil and Gas Corporation used to be an SOE managing the state's assets in the oil and gas sector. Under Decision 198 dated 29 August 2006, it will be reorganised to try to create a structure with greater accountability. It will consist of:

- the parent company which will have the same name as the whole group – Vietnam Oil and Gas Group (PetroVietnam). Its function will be to enter into and supervise the implementation of oil and gas contracts with foreign partners, to implement important national oil and gas projects and to invest in other enterprises;
- four operating subsidiaries in which PetroVietnam will hold 100 per cent of the charter capital: (i) Oil and Gas Exploration and Exploitation Corporation

- (to be established on the basis of the restructuring of certain SOEs currently operating in the oil and gas exploration and exploitation sectors), (ii) Gas Corporation (to be established based on the restructuring of PetroVietnam Gas Company), (iii) Power Production and Trading Corporation (to be established when PetroVietnam's power plants come into operation), and (iv) Oil Refinery and Petrochemical Corporation (to be established when PetroVietnam's oil refineries come into operation);
- four one-member limited companies wholly-owned by PetroVietnam, including PetroVietnam Finance Company (PVFC), PetroVietnam Trading Company (PETECHIM), PetroVietnam Oil Processing and Distribution Company (PDC), and PetroVietnam Labour Export and Supply Company (newly established);
- 14 companies in which PetroVietnam will hold more than 50 per cent of the charter capital, including: (i) six already-equitised companies (Petroleum Technical Services JSC (PTSC), PetroVietnam Tourism and Service JSC, PetroVietnam Drilling and Well Services JSC (PV Drilling), PetroVietnam Investment Consultancy and Engineering JSC, PetroVietnam Construction JSC, and Drilling Mud JSC); (ii) three companies to be equitised in 2006-2007 (PetroVietnam Insurance Company (PVIC), PetroVietnam Transportation Company and PetroVietnam Fertilizer and Chemicals Company); (iii) two joint-ventures; and (iv) three newly-established companies (PetroVietnam Real Estate JSC; PetroVietnam Securities JSC; and PetroVietnam Joint Stock Commercial Bank); and
- companies in which PetroVietnam holds less than 50 per cent of the charter capital, including two LPG companies to be equitised in 2006-2007.

Independent power projects (IPPs)

Many smaller IPPs have not been built as originally promised or predicted. To reduce the number of half-built or delayed projects in an era of looming power shortages, the Ministry of Industry (MOI) set some stricter standards on management of construction investment in IPPs in Decision 30 dated 31 August 2006.

Smaller would-be investors in projects with investment capital of more than VND600bn, around US\$37.5m, are handled under different rules. They must have at least 30

per cent of the total capital required for the project before proceeding (20 per cent in special cases). These power projects are also required to have an acceptance letter from EVN or an electricity retailer/wholesaler to purchase electricity. They must also show a credible schedule for the mobilisation of investment capital and loan commitments from credit institutions.

Power master plan

The MOI has recently issued power master plan number VI, which the PM is expected to approve in the next month or so, and a master plan for small and medium-sized hydro electricity plants. Provincial PCs will issue master plans for provincial power development and for provincial small and medium-sized hydro electricity plants. Investment into IPPs must be in accordance with these master plans. Master plans, of course, have a habit of changing, but for the immediate future IPP developers should consult these plans. Power master plan number VI contains a larger number of projects open for foreign investment than its predecessor.

Registration of sea-going ships

The shipbuilding industry in Vietnam is shaping up as one where Vietnam can rapidly compete with more established Asian countries. The Government is putting resources into the sector and skill levels are reportedly good. The legal infrastructure to support this is also being improved. The Maritime Code was recently overhauled. Most recently, the Government issued Decree 49 dated 18 May 2006 to implement the Maritime Code on registration, purchase and sale of sea-going ships.

Banking and finance

Mortgage of land use rights and assets attached to land

It has long been unclear how to mortgage buildings without mortgaging land. The Ministry of Justice and the Ministry of Natural Resources and Environment have resolved this by issuing Circular 3 dated 13 June 2006 on the registration of mortgages of assets attached to land. It allows registration of mortgage of assets, both current and future ones, attached to land of a third party.

Taxation – securities investments

Circular 100 dated 20 October 2004 contained the regulations on the tax applicable to investment in securities in Vietnam. These regulations were not conducive to the development of the bond market. The MOF has now issued Circular 72 on 10 August 2006 revising these regulations. This is a welcome move for foreign organisations investing in Vietnamese securities.

- The capital gains tax on the transfer of securities, including shares, fund certificates and bonds, by foreign organisations that open securities investment accounts in Vietnam will be equal to 0.1 per cent of the total cost of the securities transferred. Under Circular 100, there was no capital gains tax on the transfer of bonds. Now, the tax treatment on the sale of both debt and equity is the same.
- Interest from bonds, except for tax-exempt bonds, is subject to tax at 0.1 per cent of the face value of the bond plus interest, not simply the interest coupons. Under prior regulations, foreign organisations investing in Vietnamese bonds were liable to tax on interest ranging up to 20 per cent.
- Securities companies and commercial banks where foreign investors open securities investment accounts must deduct income tax and make tax payments for their clients. Previously, the investee companies had to declare and deduct tax on behalf of foreign investors.

Securities investment funds

The first local investment fund in Vietnam was only launched a couple of years ago. A booming market has put pressure on such funds to expand. The MOF responded with Decision 30 dated 12 May 2006. This sets out the conditions under which public funds can increase their capital:

- the business operations of the fund in the two preceding years must have been profitable;
- fund certificates must be offered first to existing members of the fund at a price decided by the general meeting of investors on the basis of the net asset value of the fund;
- the plan for issuance of additional fund certificate must be approved by the general meeting of investors; and
- the capital increase plan must be approved in writing by the State Securities Committee.

Government bonds

Many investment banks expect a good run of bond offerings by the Government now that the first one has been successfully bedded down. Their hopes will be further underpinned by the PM's issuance on 24 July 2006 of Decision 171 on the issue and use of capital from the Government bonds in the period of 2003-2010.

According to the decision, Government bonds totalling VND110,000bn (around US\$6.9bn) will be issued from 2003 to 2010. The capital received will be allocated to important national projects.

The Government will determine the amount and timing of bonds to be issued annually based on its need and the progress of relevant projects.

By happy coincidence, the MOF issued Decision 36 dated 7 July 2006 on the usage of the capital received from the issuance of the Government's international bonds in 2005. Decision 36 allocated such capital to the shipbuilding industry. We acted for the Vietnamese Government on that first international bond issuance in 2005.

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