



Indochina notes

LEGAL UPDATES ON INVESTMENT, INFRASTRUCTURE AND FINANCE

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Highlights of 2006

January

The commercial laws began a complete overhaul in January that should end in 2009 with full rights for foreigners to enter into distribution and retail in Vietnam. On 1 January 2006, the Commercial Law came into force. About three weeks later, Decree 12 was issued to provide guidance on the international purchase and sale of goods. It took another year, until 12 February 2007, for a decree on purchase and sale activities of foreign-invested enterprises (FIEs) to be issued. The decree regulating the trading rights of enterprises without a physical presence in Vietnam is still awaited.

The Prime Minister (PM) also set his sights on the overhaul of the wonderfully inefficient electricity sector that results in this author, for one, not keeping much in his refrigerator. Decision 26 of 26 January 2006 set out a roadmap for the development of the electricity market in Vietnam in three stages: (i) a competitive electricity production market (2005-2014), (ii) a competitive electricity wholesale market (2015-2022), and (iii) a competitive electricity retail market (after 2022).

February

The establishment of a wholly foreign-owned bank (WFOB) in Vietnam was made theoretically possible under the issuance of Decree 22 on 28 February 2006 governing the organisation and operation of foreign bank branches, joint venture banks, banks with wholly

foreign-invested capital and representative offices of foreign credit institutions in Vietnam. The World Trade Organization (WTO) contemplates such WFOBs becoming possible as of 1 April 2007. Several banks have applied. The capital required for such a bank by 2010 will be VND3,000bn (approximately US\$200m).

April

A number of corruption cases have been reported in Vietnam related to tendering activities of state-owned enterprises (SOEs). Some innocent souls hope that the Tendering Law, which came into effect on 1 April 2006, may help to address the problem.

May

Vietnam and the US signed the long-awaited bilateral market access agreement, which paved the way for WTO accession, on 31 May 2006.

June

The National Assembly (NA) issued: (i) the first-ever Securities Law – just in time for a booming stock market (up about 150 per cent in 2006) – which covers public offerings of securities, listings, trading and investment, securities services, and the establishment and regulation of securities companies and investment funds; (ii) the first ever Law on Real Estate Business, which governs transactions in real estate such as the leasing, sale and transfer of real estate, and real estate brokerage, appraisal and consultancy business; and (iii) a resolution on nationally important investment projects that doubled the threshold (to over US\$1.5bn) at which big projects

need approval from the NA. Foreign-invested projects in which less than 30 per cent of the capital comes from the state would not need NA approval even if in excess of this size.

July

The Investment Law (the IL) and the Enterprise Law (EL) came into effect, but without the required implementing Decrees, which began to dribble out by the end of the year. There are still a multitude of questions without answers, making the practice of law in this area even more of an art than it always has been.

The government's Decree 72 issued on 25 July 2006 on representative offices and branches of foreign business entities in Vietnam tightened the admittedly relaxed regime that used to exist with respect to the opening and operation of representative offices in Vietnam.

August

Another reshuffling of SOEs – almost a hobby of the government – took place in August. Decree 86 on 21 August 2006 put all 19 of the state's most important enterprises under the direct control of the PM. The new PM, though, is actually showing signs of really wanting to equitise much of the rest. The success of the stock market is encouraging many of the vested interests that had formerly resisted equitisation to spot the possibility that this may not be such a bad thing after all.

September

Two eagerly awaited documents implementing the new investment regime were issued in September. Decree 101 dated 21 September 2006 dealt with how to re-register and convert FIEs into companies recognisable under the new EL. It is not compulsory, but most will opt to do so in the two-year window available.

Decree 108 dated 22 September 2006 provided detailed guidelines for the implementation of the IL. Most importantly, it devolved licensing authority from the central Ministry of Planning and Investment (MPI) to the provincial people's committees and the management committees of industrial zones. Investors may simply register their investment projects (ie no approval is technically required) if such projects have investment capital of less than VND300bn (around US\$19m), but only if such projects are not in a 'conditional' sector and

are not subject to prime ministerial approval. Important projects will still depend on instructions from the MPI and the government.

November

The NA issued some new laws in November: (i) a Law on Notarisation, which governs the activities of notaries and notarisation procedures; (ii) a Law on Amendment and Supplement to the Labour Code, governing labour disputes and strikes; and (iii) a Law on Technology Transfer, which might help to revive this moribund activity.

Also in November, the NA approved the Protocol on Vietnam's Accession into the WTO, which allowed Vietnam to become the 150th member of the WTO on 11 January 2007.

December

The government issued Decree 163 on 29 December 2006 to implement the new framework for secured transactions in Vietnam that was introduced by the Civil Code in 2005. Most annoyingly, mortgages and pledges are now completely different from before.

Also in December, Decree 160 on foreign exchange dated 28 December 2006 was issued to implement the Ordinance on Foreign Exchange dated 13 December 2005.

Investment

Trading and distribution services

Many foreign investors wish to participate in distribution in Vietnam. Under its WTO accession commitments, Vietnam committed to:

- grant trading rights (the right to import and export goods) for all goods to foreign investors no later than 1 January 2007, except for: (i) some products reserved to 'state-trading' enterprises (eg tobacco products and petroleum products), (ii) products for which the import right will be phased in on 1 January 2009 (eg pharmaceuticals), and (iii) the right to export rice, which will be not be granted until 1 January 2011; and
- allow FIEs with less than 49 per cent foreign-owned capital to be established to engage in distribution from 11 January 2007, when Vietnam became an official member of the WTO. From 1 January 2008, there will be no limit on a foreign investor's equity in a joint

venture distribution company, and from 1 January 2009, foreign investors may establish a wholly foreign-owned enterprise in the distribution sector.

The government's Decree 23 dated 12 February 2007 implementing the Commercial Law on purchase and sales of goods by FIEs in Vietnam begins to fill in the details on what this will mean in practice. Under Decree 23:

- existing FIEs will be required to obtain a separate business licence, in addition to their current investment certificates, to engage in trading and distribution services. Provincial people's committees can issue these business licences after obtaining a written approval from the Ministry of Trade (MOT);
- investors that wish to establish a new FIE in these sectors must submit an application to the state administrative body for investment. This body must obtain the written approval of the MOT before issuing an investment certificate. In this case, the investment certificate will also serve as the business licence for the FIE;
- for FIEs that want to conduct trading but not distribution, the state administrative body for investment may issue the business licence by reference to Vietnam's commitments in international agreements (hardly the easiest task for a non-specialist) without having to obtain written approval from the MOT; and
- FIEs licensed to engage in distribution can establish one retail outlet without having to apply for a licence. However, they will be required to apply for a licence for the opening of any subsequent retail outlets from the MOT and the provincial people's committee.

Equitisation of state corporations

To speed up the SOE equitisation process in Vietnam, the PM issued Decision 1729 on 29 December 2006 approving the list of state-owned corporations and business groups to be pushed forward for equitisation in the period from 2007 to 2010. Some of the better-known SOEs to be equitised in this period are:

- 2007 – Hanoi Beer, Alcohol and Beverage Corporation (HABECO), Saigon Beer, Alcohol and Beverage Corporation (SABECO), Vietcombank, Mekong Housing Bank;
- 2008 – Vietnam Textile Group, Vietnam Airlines, Bank for Investment and Development (BIDV);

- 2009 – Vietnam Paper Corporation, Vietnam Steel Corporation, Northern Foodstuff Corporation, Bank for Agricultural and Rural Development (Agribank), Saigon Construction Corporation, Saigon Real Estate Corporation; and
- 2010 – Vietnam Chemical Corporation, Vietnam Cement Corporation, Song Da Corporation, Vietnam Machinery Erection Corporation.

Classification of SOEs

The government is trying to reduce the number of industries and sectors that require the existence of companies with 100 per cent state capital.

Under Decision 58 of the PM dated 26 April 2002, classification of SOEs was based on four criteria: (i) amount of state capital, (ii) state budget contribution, (iii) ability to apply science and technology, and (iv) role in the macroeconomy of Vietnam. At that time, the state indicated its intention to retain 100 per cent of the capital of companies operating in 60 sectors and industries. Under Decision 155 of the PM dated 24 August 2005, the criteria were reduced to just three: (i) amount of state capital, (ii) state budget contribution, and (iii) application of science and technology, and the state indicated that it would retain 100 per cent of the capital of companies operating in just 30 sectors and industries.

Under the latest regulations, Decision 38 of the PM dated 20 March 2007, the state will only retain 100 per cent SOEs in 19 industries, which include companies operating in national electricity transmission; large scale electricity production; national defence; management and maintenance of the national railway, airports and large seaports; flight and railway transportation control; maritime transportation safety management; public postal services; broadcasting and television; lotteries; publishing; money printing and coin production; and cigarette production.

The state will not sell more than 50 per cent of the following companies:

- companies involved in the production and supply of public services and commodities (eg maintenance of the national railway, management and maintenance of land and waterways, management and exploitation of some seaports, production of scientific and

- documentary films and films for children, urban drainage, prospecting and exploration for natural resources, production and storage of plant and animal breeds, and production of vaccines); and
- companies having roles in 'balancing the economy and market stabilisation' in the following sectors:
 - (i) electricity production with capacity of more than 100MW; (ii) exploitation of coal, bauxite and other minerals; (iii) production and exploitation of oil and gas; (iv) building and repair of air transportation vehicles; (v) provision of communication information infrastructure; (vi) production of steel and cast-iron with capacity of over 300,000 tons per year; (vii) production of cement with capacity of over 1.5m tons per year; (viii) production of certain chemicals; (ix) growing and processing of rubber and coffee; (x) production of paper for newspaper printing and of high-quality paper; (xi) wholesale distribution of food; (xii) wholesale distribution of petroleum; (xiii) wholesale distribution of pharmaceuticals; (xiv) production of beer with capacity of over 100m tons per year; (xv) exploitation, purification and provision of freshwater; (xvi) international sea transportation services, railway and airway services; and (xvii) insurance and money-related businesses.

New corporate income tax (CIT) regime

The government updated the CIT laws in Decree 24 dated 14 February 2007. The basic CIT rates remain the same – 28 per cent for normal businesses and between 25 and 50 per cent for oil and gas and other natural resources businesses.

Decree 24 abolishes tax preferences formerly available to shareholding companies after equitisation or to enterprises using domestically produced materials.

Investors will be entitled to tax preferences if their investment projects fall into one of the following categories: (i) industries or trades with investment incentives under the IL, (ii) industries or trades on the list of projects with special investment incentives announced by the government, or (iii) projects located in areas categorised as having extremely poor socioeconomic conditions as specified in the IL.

Tax preferences include:

- CIT rate of 20 per cent for 10 years for newly established enterprises in industries or trades with investment incentives under the IL or located in areas categorised as having extremely poor socioeconomic conditions;
- CIT rate of 15 per cent for 12 years for newly established enterprises in industries or trades with investment incentives under the IL and located in areas categorised as having extremely poor socioeconomic conditions; and
- CIT rate of 10 per cent for 15 years for newly established enterprises in industries or trades on the list of projects with special investment incentives.

Tobacco management

The PM had a meeting with the Ministry of Industry (MOI) on the future management of the tobacco industry on 3 January 2007. The content of the meeting is summarised in Notice 12 of the Government Office dated 16 January 2007. Although a notice does not have the force of law, it sets out the policy direction of the government, which will (theoretically) drive the ministries and other relevant authorities in their actions.

- As a general policy, tobacco products are not encouraged, but can still be manufactured and traded. The state will control the supply, and exclusively manage the manufacture, trading, export and consumption, of tobacco products. The management and organisation of trading in tobacco products must be centralised through state-owned trading companies.
- None of the following will be permitted: foreign investment in tobacco, new investment, expansions of current investment projects or increases in tobacco manufacturing capacity for domestic consumption. Tobacco products must be manufactured through joint ventures or co-operation contracts with local manufacturers in accordance with the plans for the tobacco industry.
- The state must hold a majority in such ventures. Approval of the PM will be required for issuance of a tobacco manufacturing or trading licence.
- The manufacture of new foreign tobacco brands for domestic consumption must fall within current allocated manufacturing capacity and be approved by the PM.
- Tobacco manufacturers may not be equitised.

Industrial zones

The PM issued Decision 1107 dated 21 August 2006 approving the master plan for development of industrial zones in Vietnam to 2015, with a vision to 2020. Under this Decision, there will be 117 industrial zones on the priority list for establishment by 2015, and 27 industrial zones with priority for expansion.

The MPI also issued Official Correspondence 1214 dated 27 February 2007 guiding the procedures for establishment of industrial zones in Vietnam. Projects for the establishment and expansion of industrial zones within the master plan approved by the PM can obtain an investment certificate without having to obtain an approval from the PM. By contrast, projects that are not listed on the master plan will have to obtain approval from the PM.

Infrastructure

Connection to the national electricity system

The MOI issued Decision 37 on 16 October 2006 (Decision 37) to provide for specific conditions applicable to entities that have electricity plants and need to connect to the national electricity system or to change their current connection points. To connect, such entities are required to submit an application file to the management unit of the electricity grid. The connection may only be conducted upon: (i) the connection agreement having been signed; and (ii) the inspection, commissioning and acceptance having been performed.

The maximum time limit for consideration of the application file and preparation of the connection agreement by the management unit is two months.

Financial and capital markets

Minimum capital

The government issued Decree 141 on 22 November 2006 to increase capital requirements for credit institutions. Banks and credit institutions are required to meet a specified capital level by two deadlines, 31 December 2008 and 31 December 2010, as illustrated in the table below.

Type of credit institution	Required capital level	
	by 2008	by 2010
State commercial banks	VND3,000bn	VND3,000bn
Joint stock commercial banks	VND1,000bn	VND3,000bn
Joint venture banks	VND1,000bn	VND3,000bn
100 per cent foreign-owned banks	VND1,000bn	VND3,000bn
Branches of foreign banks	US\$15m	US\$15m
Investment banks	VND3,000bn	VND3,000bn
Co-operative banks	VND1,000bn	VND3,000bn
Finance companies	VND300bn	VND500bn
Finance leasing companies	VND100bn	VND150bn

Under the previous Decree 82 of the government dated 3 October 1998, commercial banks in Hanoi and Ho Chi Minh City and other localities were only required to have VND70bn and VND50bn, respectively. Joint venture banks and branches of foreign banks were required to contribute capital of US\$10m and US\$15m, respectively.

Secured transactions

Decree 163 of the government on security transactions was passed on 29 December 2006.

It replaces Decree 165 of the government on security transactions dated 19 November 1999, as well as Decree 178 of the government dated 29 December 1999 on security for loans obtained from credit institutions. This means that, among other things, Decree 165's cumbersome requirements on valuation and the holding of documentation relating to secured property and the confusing parallel provisions on realisation of secured property no longer apply.

Most importantly, Decree 163 implements the new framework for secured transactions in Vietnam introduced by the Civil Code of 2005. Before the Civil Code of 2005, pledges and mortgages (the two most common forms of security transaction in Vietnam) were distinguished on the basis that a pledge was security taken over movable property and mortgages were taken over immovable property. However, the Civil Code of 2005 turned this upside down. A pledge is now a security created where possession of the secured property is handed over to the secured party, while a mortgage is for security over property retained by the securing party.

This change created some confusion in relation to certain forms of intangible property that are difficult to physically hand over or retain (such as book-entry shares or contractual rights).

Part of the confusion at least has been removed by Decree 163. Security over the right to claim a debt (and presumably, by analogy, security over other forms of contractual rights) is to take effect as a mortgage (under the old Decree 165 the latter type of security was seen as a pledge). Importantly, Decree 163 provides that the right to claim a debt can be mortgaged without the consent of the debtor, although there is some uncertainty about whether this provision would take effect over a requirement in the underlying contract for the debtor's consent.

Aside from the above, Decree 163 contains numerous other improvements over its predecessor.

- Whereas Decree 165 somewhat unsatisfactorily held all security transactions to terminate upon the merger, consolidation or transformation of a securing party, Decree 163 provides detailed provisions on how security transactions may continue in existence following such an event (these provisions are similar to those previously contained in Decree 178).
- When security is taken over future property, Decree 163 no longer expressly requires the execution of an annex to the security document when the future property is formed or comes into the securing party's possession. However, in practice this may still be the most practical way of ensuring that security over the relevant property is properly taken, especially where the security must be registered.
- Decree 163 addresses the issue of when the secured property is not owned by the securing party (such as leased property) and sets out the principles for determining priority between the secured party and the actual owner of such property.
- Decree 163 strengthens the position of a secured party on enforcement. In several cases secured property can be realised without any waiting period, including where the secured property consists of shares or where the secured property is in danger of losing value (under Decree 165 this principle applied only if the secured property was in danger of being 'damaged'). Decree 163 also allows a secured party to seize the secured property directly in certain

circumstances (although one suspects that in practice the successful enforcement of this right will still depend on the good graces of the local constabulary).

However, some new points of uncertainty have also arisen.

- Unlike Decree 165, Decree 163 does not contain any priority of application for the proceeds of realisation between reimbursing the expenses of realisation, repaying outstanding principal and paying outstanding interest.
- Decree 178 contained a provision that made it clear that a credit institution could take security over property attached to land separately from the accompanying land use rights. It is now not clear whether property attached to land can be mortgaged separately from the relevant land use rights.

Government guarantee

The government is trying to reduce the number of guarantees it gives. The PM issued Decision 272 on 28 November 2006 on government guarantees for foreign loans to replace Decision 233 dated 20 December 1999. Decision 272 made certain changes.

- The authority in charge of granting government guarantees is the Ministry of Finance (MOF). Previously, both the MOF and the State Bank of Vietnam (SBV) were able to grant government guarantees in certain contexts.
- A foreign loan must have a term of at least 10 years to be eligible for a government guarantee. Previously, the required minimum was five years.
- The guaranteed amount is capped at 80 per cent of the total investment capital of a project, including fees and interest during any construction period. Previously, the ceiling was based on the equity capital of the borrower and the field of operation of the relevant enterprise.
- Guarantee fees are determined based on the risk level of each project but must not exceed 1.5 per cent per annum of the outstanding guaranteed amount. Decision 272 provides for a list of applicable fees. Previously, the guarantee fee was 0.5 per cent per annum on the balance of the loans guaranteed by the government for infrastructure projects. For other projects, the rate was 1.0 per cent per annum on the balance of the guaranteed loan.

The MOF recently refused a proposal from Electricity of Vietnam (EVN) to exempt it from the guarantee fee applicable to its foreign loans that have been guaranteed by the government. In Official Correspondence 2956 dated 1 March 2007, the MOF said that it will now treat all projects guaranteed by the government on an equal basis and that there will be no subsidy from the government to enterprises due to WTO commitments. As the risk levels of EVN's projects are low, the government will consider applying the lowest possible guarantee fee in accordance with the fee rates stipulated in Decision 272.

Debt sale and purchase

Another indication of the increasing flexibility of financial markets is Decision 59 of the SBV dated 21 December 2006 providing regulations on the sale and purchase of debts between credit institutions. It replaces Decision 140 dated 19 April 1999, which made the sale of bad debts very difficult.

Debt buyers can be domestic or foreign organisations. Previously, approval of the SBV was needed if the debt buyer was a foreign entity. Decision 59 simply requires that the sale and purchase of debts involving foreign entities and foreign currencies must comply with foreign exchange control regulations.

Unlike its predecessor, Decision 59 does not set out the procedures for the sale and purchase of debts. Credit institutions have flexibility to adopt their own procedures. The sale and purchase of debts may be carried out via: (i) auction, or (ii) direct arrangements between the parties.

Decision 59 only requires the debt seller to inform the debtor or other relevant third parties of execution of the contract for sale and purchase of debts. Under Decision 140, approvals for the debtor and the guarantor were needed if the original loan agreement did not specifically allow the assignment or transfer of the debt.

Capital control in indirect investment

On 12 February 2007, the Committee of National Monetary and Financial Policy Consultancy of the SBV proposed to the government several emergency measures to control capital flow into the buoyant stock market. The PM rejected this proposal in Official Correspondence

997 dated 27 February 2007, according to which it is not yet necessary to apply urgent measures to control foreign exchange from foreign indirect investment. However, the PM ordered close supervision by market watchdogs to ensure the sustainable development of the stock market and to avoid negative changes causing socioeconomic instability. Suggested solutions include:

- purchasing foreign currency in accordance with plans;
- issuing government bonds;
- issuing regulations on the conditions applicable to increases in capital in commercial banks;
- issuing regulations on the tax policies applicable to securities trading activities;
- speeding up the equitisation of SOEs; and
- increasing the supply of shares on securities trading centres.

Administrative sanctions in securities sector

The government will get tougher (from a low base) on violators of securities rules. Decree 36 dated 8 March 2007 deals with violations in: (i) offering of securities to the public, (ii) regulations on public companies, (iii) listing of securities, (iv) securities transactions, (v) information disclosure, (vi) reporting, (vii) obstructing inspections of the authorities, and (viii) other areas.

Unfortunately, the maximum fine stipulated under Decree 36 is VND70m (US\$4,400), which is unlikely to deter many crooks. Besides monetary fines, violators may be subject to additional sanctions and may have to return ill-gotten gains.

New regulations on securities market

The MOF has issued various new regulations to implement the Securities Law.

- Decision 12 dated 13 March 2007 on corporate governance applicable to listed companies. This decision aims to harmonise the Securities Law and the EL in relation to the protection of shareholder rights and ethics of directors and officers of listed companies.
- Decision 13 dated 13 March 2007 provides a model prospectus to be used in public offerings and listings of securities.
- Circular 17 dated 13 March 2007 on registration dossiers for public offering of securities.

- Circular 18 dated 13 March 2007 guiding public companies on the purchase and resale of treasury shares and on additional issuances of shares. Circular 18 prohibits public companies from purchasing treasury shares in various situations. The previous Circular 58 dated 17 June 2004 was silent on these prohibitions.

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