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Investment Law

Acquisition of domestic company's shares – Better choice for foreign investor?

By Ngo Trung Hieu, Attorney at law

Other than forms of direct investment such as establishment of 100% foreign own company, joint venture company or via business cooperation contract, foreign investors who wish to nurture their investment in Vietnam may select another option by purchasing shares or capital contributions of domestic enterprises. Before 1st July 2006, the applicable legal instruments is the Regulations on contribution of capital to, and purchase of shares from, Vietnamese enterprises by foreign investors issued by the Prime Minister's Decision 36/2003/QĐ-TTg dated 11 March 2003 (Decision 36) and Decree 144/2003/ND-CP of the Government dated 28 November 2003 on Securities and securities market. Under these two legal instruments, the acquisition of shares by foreign investor is considered as indirect investment as the foreign investors are not allowed to participate in management of the domestic company, however, there are two different regimes applicable to sell and purchase of shares/capital contribution of non listed companies and the purchases of shares of listed company.

For non-listed company, foreign investor is only allowed to purchase shares/capital contribution up to 30% of the charter but for listed company such proportion is 49% of the listed shares. Foreign investor may purchase shares of any listed companies, but they are only allowed to purchase shares/capital contributions in company operating in the business sectors/areas announced by the Prime Minister or Minister of Planning and Investment on his behalf (for the time being, this is the list attached to Decision 260/2002/QĐ-BKH of the Minister of Planning and Investment dated May 10, 2002).

To pay for the purchase of shares/capital contribution of non-listed companies, foreign investors shall have to open a bank account in Vietnam Dong at a commercial bank operating in Vietnam and permitted to carry out foreign exchange activities, then register such with the State Bank of Vietnam as *the account for contributing capital, buying shares in Vietnam Dong*, while for purchasing shares of listed enterprises, foreign investors shall have to deposit their money in a deposit account held by a securities firm.

The listed companies have to comply with strict provisions of laws on reporting and disclosure, but non-listed companies who offer newly issued shares/capital contribution to foreign investor shall be required to make public disclosure on mass media (central and local newspaper, radio, television) for at least three times information relating to name and address of company, number of shares/capital contribution sold, tentative price for sale, date of commencement of sale, necessary information as per business situation, capital, fund of the company for current

year and previous two years. These regulations on public disclosure applied to non listed companies seem not to be strictly observed partly due to no penalty for non-compliance is stipulated and of its generality in respect of information to be disclosed.

Apart from the threshold mentioned above, after acquiring shares/capital contribution by foreign investors, the non-listed company shall have to report to the business registration agency, while the foreign investor shall have to report to the State Securities Commission if their acquired shares reach 5%, 10%, 15%, 20% of a listed company's equity.

Things are changing due to introduction of the twin laws, Law on Enterprises 2005 (LE) and Law on Investment 2005 (LI), both are effective on 01 July 2006.

First, acquisition of shares by foreign investor is no longer merely classified as a form of indirect investment but also a form of direct investment. This is reflected in Article 21 of the LI on the forms of direct investment allowing investor (including foreign investor) to buy shares or contribute capital and participate in management of investment activities, and Article 26 stipulates that investors shall make indirect investment in the form of purchase shares, shares certificates, bonds and other valuable papers. However, there is a difference in the applicable laws in respect of shares acquisition through direct and indirect investment. It is interpreted that acquisition of shares in form of direct investment shall be in accordance with the LE, LI and their implementing legal instruments, while the purchase or sale of shares, shares certificates, bonds other valuable papers and procedures for carrying out indirect investment activities shall comply with the provisions of securities laws and relevant provisions. It is apparent that there should be different provisions of laws governing the sale and purchase of shares of listed companies and non-listed companies, but the delineation drawn in the LI as whether investors participate in investment management activities could be hardly assessed in reality. In fact, an investor purchase shares of either a listed company or non-listed company may or not participate in management of such company at their own discretion if they holding a certain proportion of shares.

Second, according to Article 25 of the LI, acquisition of shares by foreign investors is no longer limited to certain areas, sectors and the threshold of 30% (as stipulated in Decision 36) but to threshold(s) to be stipulated by the Government for certain areas, sectors and industries. This would mean that foreign investor may purchase entire shares or capital contribution of a domestic company if such company does not operate in the areas, sectors and industries stipulated by the Government. This approach is completely different to what is provided for in Decision 36, but it contains a conflict with provision of securities laws on the limit of 49% of listed shares that foreign investor could purchase. So, the question is that which law will be applicable when foreign investors purchase shares of a listed company and they are intent to participate in management activities? And for non-listed company, if their majority shares, let say, 50% of charter capital are acquired by foreign

investor, then such company shall not be allowed to be listed if they satisfy all other listing requirements?

Third, as noted above, before the 1st July 2006, the purchase of shares by foreign investor have to strictly comply with foreign exchange regulations, but Article 89 of the LE provides that shares and bonds of a shareholding company can be paid in either Vietnamese currency, convertible foreign currencies, gold, value of land use right, value of intellectual property rights, technology and know-how or other types of assets as stipulated in the company charter. This provision alone shall enable us to interpret that foreign investors may purchase shares of non-listed company by foreign currency. But this is not the cases provided for in the Ordinance on foreign exchanges where all foreign currency must be converted into Vietnam Dong for carrying out indirect investment in Vietnam.

Nevertheless, for foreign investor, those changes referred to in first and second points above are far more than enough. While the Government, especially the MPI, is getting a serious headache in drafting decrees guiding the LI and LE so as to allow the state agencies conducting ex-ante control over foreign investment flow while maintaining the “opened” provisions of the LE, foreign investor may think of other possibilities to avoid such. Although it is not clear on whether the list of areas/sectors in which investment (especially foreign investment) is conditional coincide with the list of areas, sectors and industries where shareholding by foreign investors is subject to threshold(s) (this is not the case in the recent 16th draft of the implementing decree of the LI), there are lots of chances for foreign investors to (i) acquire shares/capital contribution of existing limited liability or joint stock companies, or (ii) structure the incorporation of a purely domestic limited liability or joint stock company then purchase part or all of its shares/capital contribution from shareholders/owners of such company and participate in management of such as if a joint venture company or 100% foreign owned company under former Law on foreign investment. The procedures for implementing these two options are much simpler than the registration for a brand-new company with foreign shareholder/owners with a compulsory requirement of having an investment project.

It may not be difficult for legislators to notice this, but the different approach introduced by the LE and the LI, the out-dated intention to imposing ex-ante control on foreign investment projects may make them hardly cover this gap.

Apparently, even the implementing decrees of the LE and LI are under debates and lots of resources have been put forward by the Government for perfecting them, foreign investors have the right to hope of a better choice for their investment in Vietnam without facing the cumbersome and unclear procedures.

Other Sectors

Finance

- On July 25, 2006, the State Bank of Vietnam issued Circular 05/2006/TT-NHNN, guiding a number of articles on financial leasing operations and authorised of leasing according to Decree 16/2001/ND-CP, dated May 02, 2001 and Decree 65/2005/ND-CP, dated May 19, 2005.

Taxation

- On July 28, 2006, the Ministry of Finance issued Decision 39/2006/QD-BTC, promulgating Preferential import, export tax tariff.
- The Ministry of Finance issued Circular 72/2006/TT-BTC on August 10, 2006, on amendment of and supplementation to Circular 100/2004/TT-BTC, dated October 20, 2004, guiding the value added tax and corporate income tax in the field of securities.

Banking

- On July 31, 2006, the State Bank of Vietnam issued Decision 35/2006/QD-NHNN, regulating the risk management principles in electronic banking operations.

Trading

- The Government issued Decree 72/2006/ND-CP on July 25, 2006, providing in detail provisions of the Commercial Law on representative office, branch of foreign traders in Vietnam.

Investment

- The Government's Decree 78/2006/ND-CP, dated August 09, 2006, regulating the direct investment abroad.

Healthcare

- The Government's Decree 79/2006/ND-CP, dated August 09, 2006, providing in detail the implementation of a number of articles of the Pharmacy Law.

Education

- The Government issued Decree 75/2006/ND-CP on August 02, 2006, providing in detail and guiding the implementation of a number of articles of the Law on Education.

Transportation

- On August 01, 2006, the Ministry of Transportation issued Decision 29/2006/QD-BGTVT, on amendment of and supplementation to regulation on registration of railway traffic means, issued with Decision 55/2005/QD-BGTVT, dated October 28, 2005, of the Minister of Transportation.

Land

- On July 21, 2006, the Ministry of National Resources and Environment issued Decision 08/2006/QD-BTNMT, promulgating the regulations on Certificate of land use right.
- Circular 70/2006/TT-BTC, dated August 02, 2006, of the Ministry of Finance, guiding the amendment of and supplementation to Circular 117/2004/TT-BTC, dated December 17, 2004, giving guidelines on the implementation of Decree 198/2004/ND-CP, dated December 03, 2004, on collecting land use fees.

Post & Telecommunication

- On August 09, 2006, the Prime Minister issued Decision 182/2006/QD-TTg, on the list of State top secrecy in the field of Post, Telecommunication and Information Technology.

Environment

- The Government's Decree 80/2006/ND-CP, dated August 09, 2006, providing in detail and guiding the implementation of a number of articles of the Law on Environmental Protection.
- The Government's Decree 81/2006/ND-CP, dated August 09, 2006, on dealing with administrative violation in the field of environmental protection.

Miscellaneous

- On July 17, 2006, People's Committee of Hanoi issued Decision 118/2006/QD-UBND, on the establishment of Hanoi Official Gazette Centre.

- Decision 171/2006/QĐ-TTg, dated July 24, 2006, of the Prime Minister, on the distribution and using of Government's bond for the period of 2003-2010.
- Decree 71/2006/ND-CP, dated July 25, 2006, on the management of seaports and maritime routes.
- The Government issued Decree 73/2006/ND-CP, on July 31, 2006, on dealing with administrative violation in vocational training.
- The Government issued Decree 74/2006/ND-CP, on August 01, 2006, on the organization and operation of judicial inspector.
- The Government's Decree 76/2006/ND-CP, dated August 02, 2006, on dealing with administrative violation in the field of justice.
- Decision 186/2006/QĐ-TTg, dated August 14, 2006, of the Prime Minister, promulgating the regulation on forest management.

Contact Details

Hanoi Head Office

Mr. Pham Nghiem Xuan Bac

Managing Partner

Mr. Pham Minh Hai

Partner, Consulting Practice

Ms. Le Quynh Anh

Partner, Legal Practice

Ms. Le Thi Kim Dzung

Partner, Intellectual Property Practice

Unit 308-310, 3rd Floor, Hanoi Towers

49 Hai Ba Trung, Hanoi, Vietnam

Tel: 84-4 934-0629 / 826-4797 Fax: 84-4 934-0631

E-mail: vision@hn.vnn.vn

Ho Chi Minh City Office

Mr. Dang The Duc

Partner, HCMC office

Unit 1801, 18th Floor, Saigon Trade Centre

37 Ton Duc Thang Str., District 1, Ho Chi Minh City, Vietnam.

Tel: 84-8 823-6495 Fax: 84-8 823-6496

E-mail: hcmvision@hcm.vnn.vn

www.vision-associates.com