



# Decree 139 implementing the Enterprise Law

Important progress was made in the Vietnamese legal reform process last September when the Government issued Decree No. 139/2007/ND-CP (Decree 139) on the 2005 Enterprise Law and 2005 Investment Law. This addressed some, but not all, of the lingering issues and questions relating to both laws, which have been hailed as landmarks in the reform process but require much clarification. This briefing provides an update.

The 2005 Enterprise Law (EL) and 2005 Investment Law (IL) have been hailed as landmarks in the Vietnamese legal reform process, but landmarks are normally precise. The EL and IL are not. Indeed, it is conceptually rather more useful to regard the EL and IL, like the web of Penelope, as the beginning of a work that will probably not end any quicker than Ulysses' visit to Troy. One important part of the web was woven last September when the Government issued Decree No. 139/2007/ND-CP (Decree 139). This clarified some, but by no means all, of the lingering issues and questions in the EL and IL. This briefing provides an update.

## Foreign ownership in Vietnamese companies

The applicable limitations on foreign ownership of unlisted Vietnamese companies have been in a state of flux. Before 1 July 2006, under Decision 36 (Prime Minister, 11 March 2003) and Decision 260 (Ministry of Planning and Investment, 10 May 2003), foreign investment in unlisted Vietnamese shareholding companies was restricted to 35 specific business sectors. Simply put, a foreign investor could not purchase shares in companies operating outside these permitted sectors. Furthermore, total foreign investment in a company operating in the permitted sector was limited to a maximum of 30 per cent.

In theory, the EL and IL repealed both Decision 36 and Decision 260 as of 1 July 2006 (the effective date of the IL and the EL). However, due to the lack of guidance on the precise meaning of these laws, as a matter of practice the

Department of Planning and Investment (DPI) in many provinces continued to follow Decision 36 and Decision 260 in determining whether or not to register a foreign investor's purchase of shares in a Vietnamese company.

In addition, pressure has been emerging from other sources to clarify the restrictions and limitations imposed on foreign ownership in Vietnamese companies. Under Vietnam's World Trade Organization (WTO) commitments, Vietnam was permitted to limit the total equity held by foreign investors in Vietnamese companies to 30 per cent of charter capital until January 2008. However, after January 2008, WTO commitments required Vietnam to remove the 30 per cent cap on foreign ownership unless the companies are (i) banks or (ii) in other service sectors specifically excluded by Vietnam's WTO commitments.

Decree 139 lifts the 30 per cent cap. Foreign investors are now permitted to purchase shares without restriction (ie up to 100 per cent) in Vietnamese companies operating in all industries and sectors with the following qualifications:

- foreign ownership of listed companies is limited to the percentage set out in the securities laws, which limit foreign investment to no more than 49 per cent of a listed company's shares (30 per cent for listed banks);
- foreign ownership in businesses subject to sector-specific regulations (eg banking regulations) is limited to the percentage set out in such regulations;
- foreign ownership in 100 per cent state-owned enterprises undergoing equitisation is limited to the

percentage set out in regulations on equitisation (under these regulations the body making the equitisation decision decides the percentage that can be sold to foreign investors, whether strategic or ordinary); and

- foreign ownership in companies operating in certain service sectors is limited to the percentage set out in Vietnam's WTO commitments.

Decree 139 did not address one issue many foreign investors regard as important: namely, the level of foreign investment that is permissible in a domestic company engaging in business operations in both restricted and unrestricted sectors. Some contend that the argument for permissibility is particularly persuasive if the company's operations in the restricted business sector are only a small part of its overall operations. However, Official Correspondence 6803 of the Ministry of Planning and Investment dated 19 September 2007 clarified the matter. Under this ruling, if the domestic company's business operations extend between multiple business sectors, some unrestricted and others restricted, the company is required to comply with the restrictions applicable to the restricted part of its business unless it amends its business registration certificate to remove the restricted businesses from its scope of business operations before selling shares to foreign investors.

## Investment procedures

### Setting up an enterprise with foreign capital

Article 50.1 of the IL provides that to establish an enterprise in Vietnam, a foreign investor investing in Vietnam for the first time must have an 'investment project' and carry out investment procedures in accordance with the provisions of the IL. According to article 29.4 of the IL, if foreign investors hold 49 per cent or less of the charter capital their investment will be subject to the same conditions as apply to domestic Vietnamese investors (who are not required to have a specific investment project to set up an enterprise in Vietnam). Unfortunately, the above provisions were not interpreted and applied by the local authorities in a unified way.

Decree 139 provides some clarification on the procedures for establishing companies.

- If more than 49 per cent of the charter capital of the proposed enterprise will be owned by foreign investor(s), there must be an investment project and the investment procedures set out in the IL must be followed. In this case, the enterprise will be issued with an investment certificate, which concurrently serves as the business registration certificate.
- If the foreign investor(s) will own 49 per cent or less of the charter capital of the proposed enterprise, the establishment of the enterprise should be implemented in accordance with the provisions of the EL and Decree 88 on business registration (Government, 29 August 2007).

### Purchase of interest in a Vietnamese company

If a foreign investor wishes to purchase over 49 per cent of the charter capital of a Vietnamese company, some procedural issues arise because the law is still vague. Most probably, the foreign investor would have to obtain an investment certificate. The process by which it can obtain an investment certificate is less than clear, as most relevant provisions in the IL contemplate investment certificates being issued for new investment projects.

However, there is one article in Decree 108 (Government, 22 September 2006) – article 56 – that applies to the 'acquisition of an enterprise'. This sets out a vague procedure that a foreign investor could attempt to use to obtain an investment certificate, under which the foreign investor files a request for acquisition consisting of the following documents:

- a request for acquisition, containing the name, address and representative of the foreign investor; the name, address, representative, charter capital and operational sectors of the acquired company; brief information on the contents of the acquisition of the acquired company; and the proposal (if any);
- a decision on the sale of the enterprise issued by the general meeting of shareholders (in case of a shareholding company) or the members' council (in case of a limited liability company) of the acquired company;
- a contract for acquisition of the acquired company, which must cover the name, address and head office of the acquired company; the procedures and conditions for acquisition of the acquired company; a plan for labour use; the procedures, conditions and time limit for assignment of assets or transfer of

capital, shares or bonds of the acquired company; the time limit for completion of the acquisition; and the responsibilities of the parties;

- the charter of the acquired company;
- the draft charter that will be adopted by the acquired company after permission for the acquisition is granted (if there are any changes); and
- written confirmation of the foreign investors' legal status (eg a copy of the establishment decision or other equivalent documents).

The above documents are to be submitted to the Business Registration Authority of the relevant province for consideration and issuance of the investment certificate. Unfortunately, the law contains no detail about the standards applied by the Business Registration Authority in ruling on requests.

### **Rights and obligations of foreign-invested companies (FIEs) that choose not to re-register**

The EL established a two-year window for FIEs to re-register under the new laws. According to Decree 101 (Government, dated 21 September 2007), enterprises opting 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 will have to comply with the IL and EL. Decree 139 specifies that FIEs choosing not to re-register under the EL will have the right to conduct business only in areas and for the duration stipulated in their existing investment licences. Although Decree 139 does recognise the right of FIEs that decide not to re-register to develop new investment projects and to open branches within the scope of business stipulated in their investment certificates issued under the old foreign investment law regime, it does not extend the rights of these FIEs any further.

### **Establishment of branches and representative offices**

Before Decree 139, there was no detailed guidance on the procedures applicable to the establishment of branches and representative offices of FIEs in Vietnam. This lack of guidance has limited the ability of companies to expand their business operations and geographic

presence. Decree 139 provides that FIEs established or re-registered under the EL and IL regime have the right to open branches and representative offices. The procedures for establishing such entities are set forth in the relatively straightforward Decree 88 (Government, 29 August 2007) on business registration.

### **Prohibited and conditional business sectors**

Decree 139 lists 14 prohibited lines of business, including drugs, gambling and marriage brokering with a foreign element. This list of 14 is not exclusive and does not come close to representing the full list of prohibited business sectors. Decree 139 broadly prohibits any other business lines that are not permitted in sector-specific regulations.

Decree 139 signals a major step forward in reducing the number of prohibited, protected or otherwise 'encumbered' business sectors. The Working Group on the Implementation of the EL and IL has identified approximately 300 types of licences that are currently required by more than 400 legal instruments issued by central government ministries, provincial governments and other regulatory bodies. To date, the Working Group has identified 42 of these licences as inconsistent with or not required by the EL. Boldly, as of 1 September 2008, Decree 139 eliminates any and all licences or sub-licence requirements imposed by ministries or local authorities that are not expressly required by laws or ordinances passed by the National Assembly, decisions issued by the Prime Minister or decrees of the Government.

### **Legal capital requirement**

Decree 139 provides that sector-specific regulations are necessary to determine the relevance of legal capital to a particular line of business, the level of legal capital required, and the competency of organisations and procedures for certifying it. Enterprises whose most recent balance sheet reveals equity equal to or higher than the statutory legal capital requirements need not have an authorised organisation certify their legal capital.

However, Decree 139's apparent trust and flexibility regarding legal capital certification requirements is balanced by punitive provisions that signal an intention to punish those who misstate legal capital. Under Decree

139, the chairman of the members' council and the general director of a limited liability company, as well as the chairman of the board of management (BOM) and the general director of a joint stock company, are personally responsible for the honesty and accuracy of the amount certified as legal capital when the enterprise was established.

## Legal representative

The EL provides that the legal representative of a company must be permanently resident in Vietnam. As a foreigner has to obtain a 'permanent residence card' to have permanent residency, and few such cards have ever been issued to foreigners in Vietnam, an obvious consequence is that the EL's requirement of permanent residence is impractical for many foreign companies.

Decree 139 appears to eliminate the requirement for permanent residence under the EL and to substitute the concept of 'temporary residence'. Under Decree 139, a legal representative who is a foreigner must stay in Vietnam for the entire term of office and must register such temporary residence in accordance with the law. Thus, it appears there is no longer a need for foreigners serving as the legal representative of a company to obtain a permanent residence card.

Decree 139 clarifies several other issues. For instance, when a company's legal representative stays out of the country for more than 30 consecutive days, the legal representative must (i) authorise another person in writing to perform the duties of the legal representative in accordance with the company charter and (ii) send, at least two days before exiting Vietnam, a copy of this letter of authorisation to the DPI or to the management board of the Industrial Zone or Economic Zone where the enterprise has registered its office.

## Number of authorised representatives

The EL provides generally that a corporate member of a limited liability company or a corporate shareholder of a joint stock company may appoint one or more authorised representative(s) to the members' council or the general meeting of shareholders, respectively. The EL is silent on the maximum number of authorised representatives that each qualified corporate member/shareholder may appoint.

Decree 139 clarifies this issue by providing that, unless otherwise stipulated in the company charter, a corporate member of a limited liability company owning at least 35 per cent of the charter capital may appoint up to three authorised representatives to participate in the members' council. Likewise, a corporate shareholder of a shareholding company owning at least 10 per cent of the total number of ordinary shares may authorise up to three persons to attend the general meeting of shareholders.

## Professional practising certificates

Under the EL and Decree 88, the general director/director (Director) and other managerial positions must possess a practising certificate in order for their company to apply for a business licence in certain sectors. This requirement is widely regarded as inappropriate because a Director may have other professional qualifications and experience relevant to the position and the company always has the right to hire others with the required professional experience. Furthermore, for many companies it is simply impossible for a single Director to personally possess every practising certificate for each and every business sector in which the company is engaged. Finally, under the EL and Decree 88 it is unclear whether practising certificates issued by foreign countries will be recognised in Vietnam.

Decree 139 clarifies these issues as follows:

- if the law requires the Director to have a specific practising certificate, the Director must have this certificate;
- if the law requires the Director and another person to have specific practising certificates, the Director and at least one other staff member must have these certificates; and
- if the law requires practising certificates, without specifying who must hold them, at least one staff member must have the relevant certificates but this staff member does not have to be the Director.

Decree 139 also provides that practising certificates granted in foreign countries are not recognised in Vietnam, except as otherwise stipulated in specific laws and international agreements binding on Vietnam.

## Corporate governance

### Cumulative voting

Article 104 of the EL provides that the BOM and supervisory board elections must be implemented by way of cumulative voting. Cumulative voting (i) requires the total number of votes of each shareholder to be determined by multiplying the total number of shares owned by each shareholder by the number of members to be elected and (ii) allows each shareholder the right to accumulate all their votes for one or more candidates. A different provision of the EL states that a shareholders' resolution will be passed only if it is approved by a number of shareholders representing at least 65 per cent of the total voting shares of all attending shareholders, unless a different percentage is stipulated in the company charter. This suggests that a shareholders' resolution on the election of board members must exceed the 65 per cent threshold to pass.

Decree 139 clarifies this ambiguity by providing that election to the BOM or supervisory board does not depend on specific percentages. Those gaining the highest number of votes received will be elected up to such point as the number of members elected satisfies the requirements of the company charter. Therefore, the EL's 65 per cent voting threshold does not apply to elections for the BOM and supervisory board.

Decree 139 sets out the number of candidates each group of shareholders may nominate for election as follows (unless the company charter provides otherwise).

Percentage (of the total voting shares) held by the shareholder(s)	Maximum number of candidates
10 per cent to less than 20 per cent	1
20 per cent to less than 30 per cent	2
30 per cent to less than 40 per cent	3
40 per cent to less than 50 per cent	4
50 per cent to less than 60 per cent	5
60 per cent to less than 70 per cent	6
70 per cent to less than 80 per cent	7
80 per cent to less than 90 per cent	8

Where the number of candidates nominated by a shareholder or group of shareholders is lower than the number of candidates they are entitled to nominate, the remaining candidates will be nominated by the BOM, the supervisory board or other shareholders.

### Meetings of the BOM

Under the EL, a BOM meeting is permitted to be conducted after an initial 'first notice' when 75 per cent or more of the total number of BOM members are present. The EL does not contemplate situations in which the stipulated number of members are not present. Decree 139 allows a BOM meeting to be convened for a second time within 15 days after the first meeting was noticed if more than 50 per cent of the total number of BOM members are present.

### Conversion

In addition to corporate conversions contemplated under the EL (ie conversions from joint stock companies to limited liability companies and vice versa), Decree 139 allows investors to restructure their investments by setting forth several additional forms of conversion between different types of companies, including conversions from (i) one-member limited liability companies to multiple-member limited liability companies and vice versa and (ii) private enterprises to limited liability companies. Procedures and application documents required for effecting such conversions are set out in Decree 139.

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