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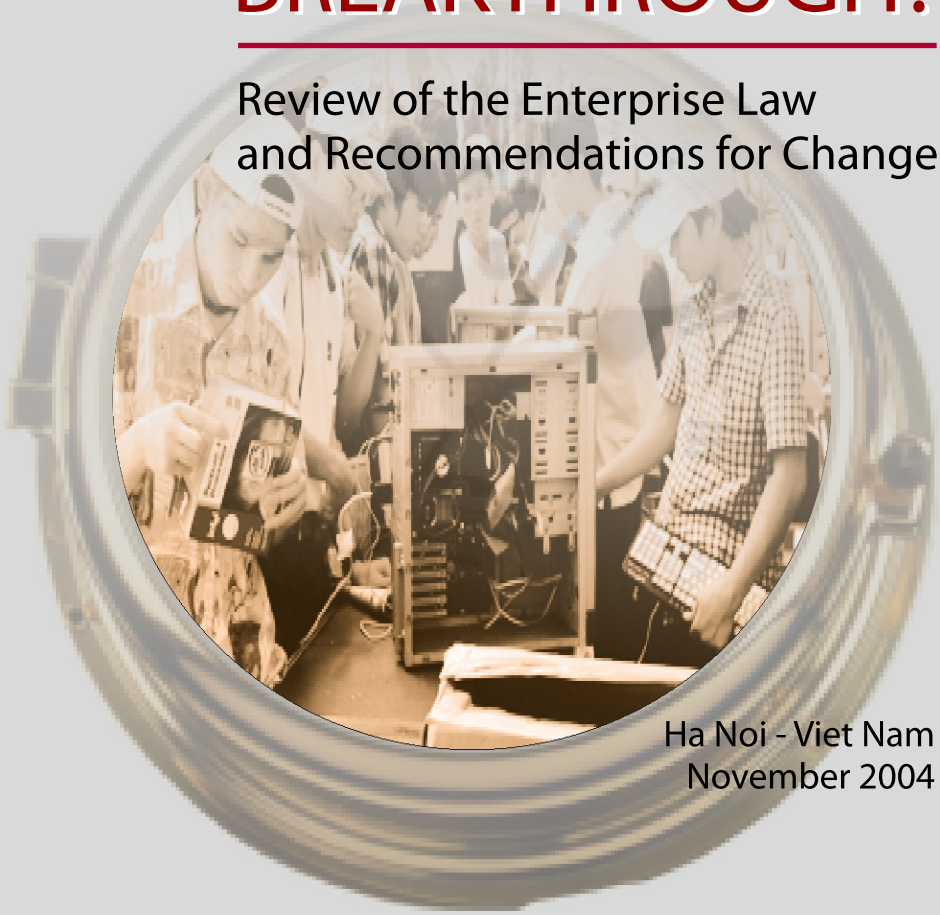
HIGH TIME FOR ANOTHER BREAKTHROUGH?

Review of the Enterprise Law and Recommendations for Change



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Review of the Enterprise Law and Recommendations for Change

Ha Noi, November 2004

EXECUTIVE SUMMARY

The Enterprise Law is rightly considered a major symbol of the success of Viet Nam's economic and administrative reform processes. Viet Nam's legal framework for business regulation, however, remains highly fragmented and unnecessarily complex. This report reviews the strengths and weakness of the 1999 Enterprise Law. In doing so, it aims to support and inform the ongoing legislative effort to stimulate further economic growth and job creation through a broadening of the mandate of Vietnam's most successful business law to date to cover all of the country's enterprises.

The strengths of the Enterprise Law include:

- Simplification of bureaucratic procedures involved in enterprise registration, as part of a general shift from the granting of licenses to a system of voluntary registration and active regulation;
- Clarification of entrepreneurs' basic right to operate in any and all business arenas not explicitly forbidden by law; and
- Diversification of enterprise forms and investment opportunities, including establishment of basic parameters for firm-level corporate governance.

The main limitation of the Enterprise Law is that it applies only to domestic private companies. As such, it is relevant to a group of enterprises that account for only ten percent of Viet Nam's GDP and less than five percent of the country's total employment. State-owned enterprises (SOEs) and foreign direct investment—which combined account for over half of GDP—are each regulated by their own separate pieces of legislation. This leads to a situation where not only are different ownership forms treated differently, but the exact nature of these differences is not always clear to all parties.

Identification of the other shortcomings of Enterprise Law implementation—and the appropriate means for addressing these shortcomings—is a necessary precursor to successful expansion of the law's scope. It is also necessary to take the further step of analyzing how the unique characteristics of new enterprise forms might create new difficulties for implementation not yet seen when the the Enterprise Law was applied to only domestic private firms. Most prominent, in this regard, is the unique set of challenges facing corporate governance of companies where profit motive is not the clear, guiding principle governing internal management. In other words, the corporate governance of SOEs.

Existing weaknesses of the present Enterprise Law discussed in this report include:

- Continued issuance of inappropriate licenses and sub-licenses at local levels and lack of systematic means for countering such new regulations;
- Lack of effective national system for avoiding duplication of firm names;
- Irrational, ineffective limitations on foreign investment in domestic firms;
- Poor legal framework for facilitating use of non-cash assets, such as real estate, for the purpose of business investments;
- Insufficient and weak shareholder rights, particularly in the case of minority shareholders;
- Basic requirements regarding shareholder meetings still minimal relative to international norms and leave open too many obvious opportunities for insufficient consulting of shareholders on key decisions;

- Management structure of limited liability companies does not yet sufficiently distinguish between the roles and responsibilities of firm owners and managers;
- Mechanisms by which owners exercise oversight over managers, such as auditing or internal investigations, are not defined clearly enough and are generally not implemented as effectively as is required;
- The concept of "related persons"—i.e. family connections of owners and managers—is not sufficiently defined and applied in order to avoid abuses of power; and
- Dissemination of key company information to shareholders is insufficient and inconsistent.

While the overall success of the Enterprise Law should not be underestimated, the collective impact of the above weaknesses on business development in Viet Nam has been—and continues to be—significant. The impact is felt both at the individual firm level and by the economy as a whole, which suffers when potential investors hesitate because they lack confidence that investment agreements will be properly enforced.

Addressing identified weaknesses will clearly be a process that requires significant time. This, however, is no reason not to move forward aggressively in the present to move this process along. Similarly, the process of bringing all enterprise forms under one business law will also be one that is sure to face substantial challenges. Decisions may be made to maintain certain preferential treatment for some enterprise forms over others. The exercise of creating the Unified Enterprise Law will, nevertheless, prove extremely valuable, as it will increase the transparency of such decisions—facilitating more informed discussions among legislators and affected groups within society. This increased clarity can also be expected to reduce confusion and variance in the subsequent implementation of business legislation at local levels of government.

INTRODUCTION

The Enterprise Law (hereafter often to be referred to simply as "the EL") has been proven to be a breakthrough in Viet Nam's economic reform process. So successful has been implementation, that the EL is now being touted as a model for law drafting and enforcement, in general, in Viet Nam. A key component of implementation has been continuous parallel assessment of the EL and its impact by the Government, relevant bodies, associations, researchers and donors over the past four years.

Compared to previous reports on the Enterprise Law, this report differs in the following respects: (i) the purpose of the report is not to promote enforcement of the current version of the EL, but rather to contribute to the drafting of a new *Unified* Enterprise Law; and (ii) the report focuses primarily on the content of the EL (i.e., the strengths and weaknesses of the EL), with less attention paid to issues relating to the enforcement of the EL than in earlier reports.

The report assesses the content of each provision and section of the Enterprise Law. As a result, the report is organized according to the same structure as the EL itself. The extent to which each provision is assessed depends on the level of problems that have arisen from application of the respective provision.

Assessment of individual provisions covers each of the following main areas: (i) objectives; (ii) main content; (iii) completeness, level of detail and reasonableness (or lack thereof); (iv) effectiveness, i.e, whether the EL has made a difference and to what extent this difference is attributable to the content of a provision and its enforcement; (v) problems that have arisen and the issues to be dealt with; and (iv) reasoning behind suggested solutions.

The following materials were used in preparation of this report: (i) past assessment reports on the EL, in particular those written by the Taskforce on Enforcement of the Enterprise Law and by other interested experts and researchers; (ii) assessments and opinions from relevant experts; (iii) sources on typical difficulties, problems and disagreements amongst enterprises and between enterprises, investors and relevant State bodies; (iv) sources on difficulties and problems from the perspective of State bodies in the enforcement of the EL; (v) sources from the region and throughout the world on experiences and trends in reforming State laws on enterprise management at the macro-level and firm-level administration at the micro-level.

I. GENERAL PROVISIONS

Scope of application

1. The Enterprise Law provides for four legal forms of business organizations: limited liability company, shareholding company, partnership and private enterprise (hereafter referred to collectively as "forms of business"). These four business organizations are the main forms of business in market economy. Indeed, there are some other derivative forms of business, created to satisfy the diverse demands of business operations. Nevertheless, most South Asian and South East Asian countries provide only for the above four main forms of business.

2. Importantly, the four main forms of business delineated in the EL, apply only to the formal domestic private sector and do not apply to the State- or foreign-owned sectors. Due to this limitation in scope, enterprises operating under the EL account for only 10 percent of GDP and five percent of the total labor force (i.e., over two million employees). Although total investments by enterprises covered by the EL have increased over the past few years, they still only accounts for 27 percent of total investments in Viet Nam.[1]

   In sum, the EL is fundamentally consistent with the realities of today's Viet Nam, with the principles of the country's developing market economy, and with international standards, but the scope of the EL's application and objectives remains limited. As a result, its impact is also limited with regard to certain important regions, sectors, and players in the economy.

3. The limitations of the Enterprise Law have historical and practical roots. Establishing and developing a "multi-sector" economy[2] is a central and guiding tenet of Viet Nam's *doi moi* economic reform programme but doing so involves a process and different economic sectors begin from different starting positions. FDI and private companies, for example, are products of reform. These sectors are emerging, developing and gaining full recognition as reform is pushed forward. Because reform is a process, laws governing different forms of businesses have frequently been promulgated separately and at different points in time. Practically speaking, in 1999, there was no clear need to unify different forms of businesses regardless of the ownership form. The reform principles, policies and the State apparatus were not yet ready for a uniform legal regime encompassing the different forms of business as prescribed in the current Enterprise Law.

The Enterprise Law and Specialized Laws

4. Article 2 of the Enterprise Law states that "the establishment, management, organization and operation of enterprises within the territory of Viet Nam shall comply with this Law and other relevant provisions of the Lław. Where this Law and a specialized law differ with respect to the same issue, the provisions of the specialized law shall apply."

5. There are three points worth noting about Article 2. First, the term "specialized law" or "specialized legislation" means a law regulating a specific area of business. However, this is not a "specialized law" in the legal sense.[3] Second, if there are conflicts between the Enterprise Law and a specialized law regarding the conditions for establishment, structure and/or business autonomy, the provisions of the specialised law shall supersede and apply. However, if there is a conflict between the EL and a specialized ordinance or decree regarding the conditions for establishment, structure and business autonomy, the provisions of

[1] Based on the ratio between State owned enterprises (38%) and FDI (13%)

[2] The main sectors comprise the State economy, cooperative economy, private capital economy and foreign invested economy.

[3] "Specialised" laws include: Law on Credit Institutions, Law on Minerals, Law on Oil and gas, Law on Natural water, Law on Civil Aviation, Law on Publishing, Law on Press, Law on Education, Law on Maritime…

the EL shall apply. Third, specialized regulations shall regulate the operations of the enterprise, especially enterprises operating in conditional sectors.

6. The supremacy of specialized laws over the Enterprise Law is somewhat inconsistent with the principles on application of laws laid out in Viet Nam's Law on Promulgation of Legal Instruments. Up through 1999 (and, in fact, all the way until the present), private domestic enterprises have been restricted from entering certain fields (media, printing, publication, broadcasting, television). However, the concept that private enterprises could conduct business in unrestricted fields (education, medical services, etc.) has not been uniformly accepted, ideologically, socially, legally or practically. An important goal of the Law on Promulgation of Legal Instruments was to reduce the discretion of local authorities to recommend or issue regulations in their territories on establishment conditions or business autonomy, thereby increasing the uniform application of law. This is also the legal basis for a provision in Clause 2 of Article 2 of Decree 02/2000/ND-CP (which is now clause 2 of Article 2 of Decree 109/2004/ND-CP) which states clearly: "Ministries, ministerial equivalent bodies, bodies of the Government, people's committees of provinces and cities under central authority may not issue regulations on business registration specifically applicable to their lines of business or localities." Empirical evidence has shown that this provision has substantially reduced discretion in applying the Law, leading to a more uniform and consistent application of the Enterprise Law in recent years. Therefore, it is no accident that among all regulated business procedures, business registration procedures are the most uniform throughout the country.[4]

7. Some notable issues have arisen in practice over the past four years. First, there have been ordinances and decrees (e.g., the Ordinance on Lawyers) that contained provisions inconsistent with the abovementioned principle of uniform application of laws. Relevant State bodies have required compliance with the provisions in the ordinances and decrees. Second, over the past period, several "specialized laws" were enacted and were being drafted. Some of these laws contained provisions inconsistent with the Enterprise Law. Since these "specialized laws" have supremacy over the EL, their enactment has somewhat muted the latter's impact.

8. The above reality demonstrates a lack of uniformity and consistency on the part of both the State and society in the application of laws regarding removal of obstacles and expansion of autonomy for business development.

   Article 2 of the Enterprise Law (notwithstanding its limitation on market entry for the private sector) has not yet been strictly enforced and its provisions are still violated by some State bodies. What is most disconcerting is that positive change is not yet possible given current institutional conditions.

Related Persons

9. The Enterprise Law is arguably the first law in Viet Nam's legal system to define "related persons". The purpose of defining "related persons" is to control and limit inappropriate transactions for private and personal gain, ensuring that transactions be fairly conducted at market values and cause no detriment to respective companies and/or minority shareholders.

10. Experience has shown that this is still a somewhat new concept in Viet Nam's legal psychology, legal drafting, enactment and enforcement. In spite of the EL and other legal initiatives, instances of inappropriate transactions for private gain by related persons have been—and continued to be—far from uncommon. State owned enterprises (SOEs) have been particularly guilty.[5] Therefore, it is necessary to clearly define

[4] VNCI-VCCI

[5] For example, a chairman of a corporation appointed his son-in-law, who heads a research center

a "related person" in an effort to identify correctly and completely all related persons. This will assist in the uniform application of the Enterprise Law with respect to shareholding companies in which the State has shares or capital contributions.

11. The definition of "related persons" in the Enterprise Law is not comprehensive and does not cover all cases. Moreover, the listing method in Clause 14 of Article 3 will not be able to provide total inclusion.[6] However, the language is more specific, easier to understand and the provisions easier to enforce than prior laws.

The fact that Viet Nam does not have a fully comprehensive definition of "related persons" makes it possible for those related persons who are not covered by the Law to conduct or conceal transactions which benefit themselves or their own group. This is detrimental to minority shareholders. The significant danger of harm to minority shareholders is supported by the fact that most breaches related to corporate governance involve transactions with related persons. As a result, a broader definition of related persons is needed than what is now in Clause 14 of Article 3 of the Enterprise Law.

12. Mekong Capital has recommended the following amendments to Clause 14 of Article 3:

- Replace (d) with "Husband, wife, father, adoptive father, mother, adoptive mother, children, adopted children, grandchildren, adopted grandchildren, siblings of any manager of an enterprise or any shareholder holding a controlling share in their own capacity or together with other parties holding over 10 percent share of the enterprise under any form."
- Add (e) as follows: "Any person living in the same household with those provided for in clauses (a) to (d), any member of any enterprise directly or indirectly controlled by those provided for in clauses (a) to (d) in their own capacity or with other people, any member of an enterprise in which any person provided for in clauses (a) to (d) holds over 10 percent shares in their own capacity or together with other people or any employees of any person provided for in clauses (a) to (d)."
- Add (f) as follows: "Any individual appointed to positions referred to in (a) to (e) or any employee of any person referred to in (a) to (e) acting on behalf of his or her employer officially or unofficially."
- Add (g) as follows: "Any person receiving directly or through persons referred to in (a) to (e) any commission, payments similar to commission or benefits related to any new issue of shares of the company or any purchases by the company."

Business Sectors

13. Article 6 of the Enterprise Law regulates business sectors. According to Article 6, lines of business in the economy are classified into: (i) prohibited business sectors; (ii) conditional business sectors; and (iii) the rest, i.e. business sectors not prohibited or limited by conditions.

14. Clause 2 of Article 6 defines prohibited lines of business. Pursuant to this Article, the Government has identified, issued and published 12 prohibited business sectors.[7] The list of prohibited business sectors, however, is not specific and its application is pending issuance of a relevant Circular or Decision by the appropriate ministry.

15. Conditional lines of business are divided into a several categories.For instance, in one category, the conditional business sectors are issued a license or a "condition satisfaction certificate" by the relevant State body. However, all conditions are not expressed in the license requirements. In some cases, these

[6] For example, the representative of a majority shareholder or each shareholder controlled by a majority shareholder, etc., is not c onsidered a related person.

[7] Clause 1 of Article 3 of Decree 03/2000/ND-CP dated 3 February 2000 of the Government.

conditions are stated in regulations regarding environmental standards, food hygiene standards, traffic safety, etc. Some conditions must be satisfied prior to the registration of the business. These conditions are, in effect, preconditions to establishment of an enterprise (e.g., legal capital, practicing certificate). The majority of requirements, however, are post-registration conditions.

All enterprises must strictly comply with all conditions at all times in order to conduct their business. Article 6 of the Enterprise Law only identifies conditional business sectors, while the specific conditions and the mechanisms for enforcing such conditions are dealt with in specialised laws, ordinances or decrees.

16. Experience over the past four years has shown that the provisions of Article 6 in the Enterprise Law (as discussed above) have achieved some notable results. The jurisdiction to prohibit or condition lines of business is limited to the three most supreme bodies of the polity: the National Assembly, the Standing Committee of the National Assembly and the Government. This limitation has had two direct effects. First, Article 6 provided the legal basis for the removal of 316 licenses and the conversion of 46 licenses to business conditions without licenses or to other administrative forms. In addition, Article 6 has substantially limited the capricious exercise of discretion in the prohibition or imposition of conditions on businesses.[8] Second, for the first time, the prohibited or conditional lines of business are identified according to a "negative list". Importantly, this is the fundamental basis for the implementation of the principle that enterprises may operate in any business sector not prohibited by law. This concept increases business freedom as well as the autonomy of enterprises. This achievement has thus far been primarily limited to domestic private enterprises.

17. In spite of great progress, problems still exist with the content and practical implementation of the provisions on prohibited and conditional lines of business. For example, Clause 2 of Article 6, which includes a list of 12 prohibited lines of business, is not a comprehensive list of all the banned sectors, with regard to private companies.

Private enterprises are also prevented from conducting business in lines of business prohibited by specialized laws, ordinances or decrees (these are lines of business reserved for SOEs and enterprises of political and social organizations). For example, printing (except package printing), media, broadcasting, television, main telecommunication services, sending Vietnamese overseas for employment, auction (list more), etc., are all business sectors in which private entities cannot participate.

18. Over the past four years, ministries and people's committees in some provinces have issued (in writing or orally) prohibitions on business applicable only within their territory. The most common prohibitions are those relating to business sectors considered to be "sensitive". The pretext of "supply has exceeded demand" has also been used more than once to stop latecomers from entering markets. Examples include, taxi companies in Da Nang and cassava flour processing facilities in Tay Ninh. In addition, private enterprises may be refused the right to register and operate due to lack of planning or because the relevant line of business is said to be outside the authority of local authorities. It should be noted that over the past four years, the Prime Minister has, on three different occasions, instructed provincial people's committees to remove *ultra vires* regulations on suspension (which is in effect prohibition) of business and to amend their out-of-date planning in order to ensure the business autonomy granted under the Enterprise Law.[9] Nevertheless, this practice of subjective decision-making has not decreased, and has

[8] According to the Taskforce on the Implementation of the Enterprise Law, as of June 2004, there were some ministries and about 11 provinces and cities under central authority that still maintained prohibitions against or suspensions on business registration inconsistent with the provisions of the Enterprise Law.

[9] Directive 29/2000/CT-TTg; Directive 17/2001/CT-TTg and Directive 27/2003/CT-TTg.

instead increased and spread.[10] Some ministries have made their own subjective decisions (without a basis in law) in refusing to issue business registrations.[11] This high level of discretion reduces the uniform application, and overall effectiveness of the Enterprise Law.

19. Provincial authorities often refuse to allow business registration on the grounds that it is new or unfamiliar. Examples include enterprises proposing to transport cash or assist with visa applications. Due to different perceptions of a particular line of business, registration may be refused in certain localities and allowed in others. Education services and legal consulting services are typical examples. For example, in Bac Ninh, enterprises are not allowed to register vocational schools because it is not considered a business activity. In Ha Noi and various other localities, in turn, vocational training is a highly popular form of private enterprise. The case of VINAJUCO can also be interpreted as a typical case wherein a difference in perceptions (between society and the State administrators) gets in the way of a company being able to do business as it intended.

20. The Enterprise Law classifies business sectors in a manner similar to that of other countries in that lines of businesses are differentiated between regulated and unregulated industries. Furthermore, regulated industries are further classified according to the extent they are regulated. However, in contrast to Viet Nam, most countries classify lines of business according to a negative list.

21. Some countries have no prohibited lines of business. Instead, what exists are industries specially reserved for the State sector. For example, in the Czech Republic, only the State could exploit, trade, transport and use radioactive substances. According to experts, when a country prohibits a line of business, that prohibition is motivated more by politics than by economics or legal concerns. In Russia, for example, private enterprise are prohibited from building space satellites. This policy was the inspiration of a member of the DUMA who was once an astronaut for the former Soviet Union.[12] In other words, aside from politics, it is difficult to reasonably justify prohibition of a particular business sector.

22. Regarding entities subject to a prohibition of a business sector, (depending on the type of prohibition) the prohibition may apply to all investors, or may apply only to foreign investors. For example, in Thailand, apart from prohibitions applicable to both domestic and foreign investors, the Alien Business Law prescribes the prohibitions applicable only to foreign investors. Usually, in developing countries, foreign investors are subject to restrictions in lines of business where foreign investment is not encouraged. Market entry is therefore made more difficult for a foreigner than for a domestic investor. However, prohibitions against foreigner investors must always be in compliance with MFN principles.

23. There are also a few points worth mentioning regarding conditional lines of business. The Enterprise Law does not specify the conditional business sectors or required industry specific conditions. Specifics are provided for in specialized laws, ordinances and decrees.

    As of November 2003, VCCI had identified 246 licenses (prescribed by specific Government documents) still required of businesses in conditional sectors. Among these, there were still many licenses inconsistent

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[10] According to preliminary data collected by the Taskforce on the Implementation of the Enterprise Law, as of June 2004, some ministries and 12 provinces and cities under central authority still maintained bans or suspension on business registration inconsistent with the Enterprise Law.

[11] Official Letter 552/NHNN-PHKQ dated 28 May 2004 states "transportation of cash, precious assets, valuable papers is considered transportation of special goods, the business of which is a special type requiring satisfactions of conditions relating to security and safety to be prescribed by the State". Official Letter 664 BCA (V11) dated 27 April 2004 of the Ministry of Public Security states "…from the perspective of ensuring security and safety, licenses should not yet be granted to enterprises outside the banking industry to transport cash, precious assets and valuable papers".

[12] The report of the Chairman of the equitised SOE association of the Russian Federation, –supported by the research team of CIEM investigating the Russian experience of economic reform and privatization.

with Article 6 of the Enterprise Law and Decision 19/2000/QD-TTg dated 3 February 2000 of the Prime Minister.[13] In addition to these licenses, there are also many other "permissions" that are required. For instance, approval for opening inter-provincial bus lines, approval for travel routes, and certificate of zoning compliance. These indirect licenses can be found throughout the country and in various different sectors. It is worth mentioning that these licenses are usually prescribed by circulars or decisions of ministries or people's committees and generally characterised by unclear conditions, procedures and time limits for issuance. Authorities frequently do not consider these requirements to be licenses, thereby making it difficult to control and eliminate them, let alone to identity them.

24. Over the past four years, there have been more 10 newly issued licenses. Based on the process by which newly issued licenses are being introduced and the nature of many of these new licenses, there is growing concern about how many new additional licenses may be added in the coming years, adding to transaction costs (both in time and money). This may occur both directly and through creation of increased discretion that allows some officials to hassle and cause trouble for enterprises. This potential upward trend in unnecessary licenses would have the effect of stymieing planned improvements in the business environment. Importantly, there has been no systematic assessment and analysis of current effective licenses in order to assess the costs and benefits of these licenses. In addition, there are no reliable measures of the reasonableness or lack thereof of the licensing documentation, procedures, conditions or the general effectiveness of each type of license. As a result, there is no basis for reforms or changes as existed at the start of the year 2000.

25. Business conditions not requiring licenses are a new concept in Viet Nam, introduced by the Enterprise Law. This new concept has helped change the mentality of State administrators, and has affected the methods of State administration, in general, and the administration of business conditions, in particular. It has considerably reduced administrative procedures and increased the autonomy of enterprises. Changes in administrative methods have also increased the sense of responsibility of both administrators and entrepreneurs in implementing the proper business conditions.

26. Unlike with licenses, no list has yet been created of non-license based business conditions. There are some noteworthy issues related to business conditions not requiring licenses. There has been an increase in legislation prescribing these business conditions. Not only by the National Assembly, the Standing Committee of the National Assembly, and the Government (within power), but also by ministries, and people's committees at different levels.[14] As a result, restrictions of this type are on the rise, increasing costs for both enterprises and administrators. In addition, many of these new conditions imposed on conditional business sectors are unreasonable (e.g., the legitimate objective of these conditions is not clear). These conditions also tend to create monopolies for certain enterprises and individuals operating in the targeted lines of business. In addition, a condition may be designed to create special prerogatives and personal gain for some individuals in connection with the satisfaction of such business conditions.[15] Some conditions are not only contrary to the prescribed powers of involved officials, but also been created without a corresponding system and plan for implementation.

27. Experience during the past four years indicates that it is more difficult to effectively control the creation of non-license based business conditions as compared to business condition licenses. Practically speaking, apart from the existence of unreasonable conditions (as mentioned above), the methods and institutions of State administration required for the control of non-license based business conditions do not really yet exist in Viet Nam.

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[13] Secondary airline bill of lading agent certificate; …

[14] Decision 1247/21001/QD-BGTVT of the Ministry of Transport and Telecommunication, Decision 21/2004/QD-BTC of the Ministry of Finance, Decision issued in 2001 of the People's Committee of Ben Tre province.

[15] Conditions for maritime business (Decree 10/2001/ND-CP),tourist guide cards (Decree 27/2001/ND-CP, etc) are typical examples.

Box 1: Justification of Business Condition Licenses in the OECD

Business conditions, in general, are a diverse collection of tools used by the Government to delineate State requirements of citizens and enterprises. Substantive conditions fall into two main categories: economic conditions and social conditions. Economic conditions directly interfere with decisions of the market such as price fixing, competition, and market entry or withdrawal. Social conditions are intended to protect community interests such as health, social safety, environment and social unity. The conditions justifying the use of licences as a business condition only exist when the business poses a danger to the public and there is a real problem getting sufficient information to consumers.

Source: From Red Tape to Smart Tape: Administrative Simplification in OECD countries, 2003.

28. What are the reasons for this?

- First and foremost, there exists a lack of vision regarding how to implement reforms, as well as how to improve the business environment and the institutions required for reform.
- There is a lack of consistent political commitment for speeding up reform.
- There is a lack of methodology for the specific reform measures.
- There are currently no able, competent specialized personnel with sufficient resources to implement these reforms.

The research process supporting drafting of the Uniform Enterprise Law may help to complete the guiding methodology required to implement reforms regarding business conditions. Although methodology is necessary for reform, it is, however, by itself, insufficient to create a breakthrough and to sustain reform measures.

29. For the past several years, many nations, in particular OECD member nations, have been researching and reporting on their own experience with institutional reforms. Institutional reforms have been conducted frequently in order to eliminate and simplify administrative procedures, reduce and eliminate social and economic constraints in order to reduce social costs, and to increase the flexibility of the business environment.

Rights and obligations of the enterprises

30. The provisions on the rights and obligations of enterprises are defining features of the Enterprise Law. In the former central planning system, enterprises could only perform what was permitted by laws and given by rights to enterprises. In addition, the manner in which an enterprise could perform and function was regulated by centralized administrative orders given from the top down. The Enterprise Law specifically prescribes the rights of enterprises, which is a change from the old system, creating more comfort and confidence in investors.

31. According to Article 7, enterprises under the Enterprise Law have all the rights required to have the freedom to conduct business. In practice, enterprises have effective rights, and have successfully exercised the rights granted by law. This is a real advantage for enterprises under the EL compared to foreign invested enterprises.

32. Article 8 provides for eight core obligations of enterprises. Similar to the rights of enterprises, the content of the obligations and the manner in which they would be performed would be pursuant to the relevant laws.

Unlike with rights, the sense of complying with the obligations of enterprises is still poor, especially with respect to the obligations prescribed in Clauses 2, 3 and 5 of Article 8.

33. Unlike the exercising of rights, the performance of obligations requires a mechanism for enforcement due to weak provisions. The lack of effectiveness of the provisions on obligations is attributable to several factors. The provisions are not yet transparent and clear regarding the content of the obligations and the way in which they should be performed. Also, the enforcement machinery is neither competent professionally nor wellequipped with the needed funds and facilities. In addition, implementation is not yet publicly transparent and has not yet gained the confidence of the public, in general, and enterprises, in particular.

II. ESTABLISHMENT OF ENTERPRISES AND BUSINESS REGISTRATION

The Achievements in general

34. Simplification of the procedures for business registration and business establishment is considered one of the breakthroughs of the Enterprise Law. This differentiates the Enterprise Law from other laws.

The Enterprise Law has created equal access to business opportunities. Currently, all organizations and individuals (other than those prohibited from conducting business) that have a business initiative or opportunity may establish enterprises appropriate to their circumstances pursuant to their business initiative or opportunity. In addition, the Enterprise Law has been considered a breakthrough in terms of administrative reforms in three aspects. First, the procedures and documentation for the establishment of enterprises have been simplified. According to empirical data, the time it takes to establish an enterprise has been reduced from 90 days from the receipt of proper documentation to seven days on average. In some provinces, the time has been reduced to only two or four days. Ho Chi Minh City has tested an online registration system that cuts the time to one hour. In addition, the cost of business registration has been significantly reduced, from an average of VND10 million to about VND500,000. Second, laws have been created clearly defining the rights of the State, as well as the rights of State officials *vis a vis* the rights of the investor and the enterprise, having the effect of gradually reducing the tendency by State bodies to over administer and create hassles for enterprises. Third, 150 business licenses have been abolished, removing a significant amount of unreasonable administrative barriers on the operations of enterprises. The Enterprise Law has expanded the autonomy and the ability for initiative in regards to an enterprise's operations while at the same time creating a legal basis ensuring the stability of State policies, as well as a transparent relationship between the State and enterprises. As a result, business operations in many industries have become more certain and stable, no longer restricted by the terms of a particular license. This has helped to considerably reduce the costs and risks of obtaining and renewing licenses.

All of the above factors have given more confidence to enterprises in starting their business and in expanding the scale of their operations.

Shortcomings

35. The drafting language and the provisions relating to the establishment of enterprises and business registration still require some discussion.

The Enterprise Law differentiates the right to establish, the right to contribute capital and the right to manage. Therefore, the EL provides for three groups of investors: the first group possess all three rights (right to establish, contribute capital and manage); the second group has only the right to contribute

capital and the right to manage, and the third group only has the right to contribute capital (without the right to manage).

Different from prior legal systems, the right to establish an enterprise to conduct business is a basic right of the people. The procedures involved in setting up an enterprise require some professional skills. Therefore, investors have tended to authorize other people (i.e., consultants) to complete the formalities for setting up an enterprise. Technically, it is the consultants who set up the enterprises.

It is unusual to separate the right to manage from the right to contribute capital because the right to manage is an outcome of the right to contribute capital. One who contributes capital normally has the right to manage. If the law takes away their right to manage, they must be compensated in the form of an equivalent right or benefit. Without this compensation for loss of rights, investors may (i) only make short term investments in super profitable ventures; (ii) only contribute capital if they can find proxy managers controlled by the investor (such that the investor has effective managerial control over the enterprise; or (iii) they do not contribute capital at all.

36. Article 9 of the Enterprise Law prescribes eight cases where investors are prohibited from setting up or managing enterprises. Article 9 also provides for three cases where investors can only contribute capital without the right to manage. In discussing this article, it is important to stress that the technique of clearly identifying the distinct groups that are not eligible for the same rights and obligations as others is, in itself, a major achievement. The seven cases (from one to seven) in Article 9 concern investors who are prohibited from setting up or managing an enterprise as already prescribed by other legislation. The 8th case is foreign organizations and individuals. The exclusion of foreign organizations and individuals is natural since it has always been clear that the Enterprise Law does not apply to foreign invested enterprises.

37. The prohibition against State officials, military officers, professional servicemen and managers of SOEs from setting up and managing their own enterprises has not been effective in achieving its objectives. In other words, we have not been able to prevent the use of public office for personal gain or to benefit enterprises belonging to families or related people. Preliminary surveys show that many private enterprises are currently run by the spouses, children, or families of senior officials, or even directly by the chairmen, Directors or board members of SOEs. As long as State bodies have the power to grant concessions (e.g., a land use right), or an SOE still has privileges, and there is a lack of transparency and accountability in the State machinery, provisions to eliminate personal gain will not be effective. There are even some cases where local officials still have enterprises in their own name in spite of the Enterprise Law.

38. Those who have been criminally convicted or are serving a jail sentence (Clause 6 of Article 9) are prohibited from setting up or managing an enterprise. This provision only looks at a particular point in time without taking into account issues of equity. For example, many people have been convicted or served a jail sentence only after they had set-up or managed an enterprise. A strict application of Clause 6 of Article 9 in such cases would lead to dissolution or bankruptcy of the relevant enterprise, which may lead to an unjust outcome to that person and to any related persons involved with the enterprise.

39. According to Clause 8 of Article 9 and Clause 2 of Article 10, foreign organizations and individuals not resident in Viet Nam may only contribute capital without having the right to set up or manage an enterprise and their capital contribution will be regulated by the Law on Promotion of Domestic Investment. Article 5 of the Law on Promotion of Domestic Investment states that “the Prime Minister decides specific cases permitting foreign investors to contribute capital or buy shares in Vietnamese enterprises not exceeding 30 percent of the charter capital of the enterprise.”

40. For foreign investors, the Law differentiates between non-resident and resident investors. For resident investors in Viet Nam, they may contribute capital as a Vietnamese investor. For non-resident investors, they may only contribute capital up to 30 percent of the charter capital of the enterprise pursuant to a

decision of the Prime Minister. This was subsequently elaborated upon in Article 5 of Decree 51/1999/ND-CP.[16]

41. There are four noteworthy points in the interpretation of Article 5 of Decree 51. First, it is unclear whether foreign investors are classified as residents or non-residents as stipulated in Article 5 of the Law. Second, the Prime Minister decides on the list of industries and trades in which foreign investors may contribute capital or purchase shares equivalent to up to 30 percent of the charter capital (specific cases are interpreted as the list of industries in which investment is permitted)[17]. Third, with respect to capital contributed to SOEs or equitized SOEs, the ownership of which was converted, the Minister or Chairman of the provincial People's Committee will decide respectively on whether a foreign investor will become a member or a shareholder. Fourth, with respect to enterprises in other economic sectors, the capital contribution or purchase of shares will be implemented in accordance with agreements made between each foreign investor and the enterprise concerned. In such cases, the enterprise shall notify the body issuing its business registration certificate no later than 15 days after the date of implementation of the capital contribution or share purchase.

42. In summary, the restrictions imposed on foreign investors under the Enterprise Law include:

(i) Restriction on the maximum ownership ratio of 30 percent of the charter capital;

(ii) Restriction on industries and trades: investment is only permitted in the industries and trades identified in the list decided by the Prime Minister or decided by the Minister of Planning and Investment and authorized by the Government's Prime Minister;

(iii) Not entitled to management of enterprises;

(iv) The administrative procedures to carry out investment (capital contribution, purchase of shares) are not clearly provided for, and are unclear in terms of documentation requirements, procedures, orders, conditions, deadlines for approval or registration, etc.

43. It is worth saying that the restriction on capital contribution by foreign investors in "the list of permitted industries and trades" is, in reality, ineffective. In practice, enterprises subject to the Enterprise Law do business in multiple industries not prohibited by law, including industries and trades in which capital contribution by foreign investors is permitted. As a result, in the end, capital contributed by foreign investors is used not only for industries in which they are permitted to contribute capital, but also used for other business activities of the enterprises. In other words, it is impossible to classify the purchase of shares and capital contributions by foreign investors based on industries and trades with respect to enterprises under the Enterprise Law because funds are fungible. An enterprise only needs to carry out an additional registration of industries and trades on the permitted list to be entitled to raise capital by way of capital contribution or purchase of shares from foreign investors. Therefore, the provision limiting foreign investors rights to contribute capital or purchase shares to the list of industries and trades is unnecessary and ineffective in terms of State administration. Instead, the list simply creates more expenses that the enterprises and the concerning State bodies have to incur; at the same time, it makes foreign investors feel that they are not trusted and not treated equally. These factors make Viet Nam's investment environment less attractive and competitive compared with other countries.

44. It is clear that the restrictions on foreign investment under the Enterprise Law are stricter than the restrictions on foreign investment under the Law on Foreign Investment in Viet Nam. However, the interests of foreign investors (under the EL) are not clearly provided for and their rights are not more favorable than the rights

[16] Article 5 of Law on SOE.

[17] In fact, there are two decisions: Decision 145-1999-QD-TTg and Decision 260-2002-QD-BKH. Subsequently, Decision 36-2003-QD-TTG was replaced by Decision 145-1999-ND-TTg.

granted under the Law on Foreign Investment in Viet Nam. An example of the strictness of the Enterprise Law is that a husband who is a foreigner may not manage an enterprise owned by his wife. (The strictness of the Enterprise Law may lead to unreasonable outcomes)

45. Up to now, foreign investment under the Enterprise Law is not much.

46. The restrictions on foreign investors raise a series of questions. Why is the ownership ratio restricted to 30 percent? (Under laws of other countries, foreign investors are entitled to 100 percent ownership). Similarly, why is the management right of foreign investors "divested"? What is the basis for the list of permitted industries and trades? Why is this list different from the list under the Law on Foreign Investment in Viet Nam? Why is the maximum investment only 30 percent of the charter capital? Notwithstanding the 30 percent maximum investment, why are the procedures so unclear, unspecific and complicated such that investment becomes infeasible? Why are the bodies with the authority to issue permits different with respect to investment under the Law on Promotion of Domestic Investment and the Law on Foreign Investment? It seems that these questions were not discussed during the formulation and implementation of these policies. The policies were passed and implemented in a manner consistent with traditional discretionary administrative habits.

    The substance of these policies and the way they have been implemented in this field is clearly not compliant with policies designed to reform and open Viet Nam's economic doors, diversify the ways to raise capital, and actively carry out economic integration as called for by Viet Nam's Communist Party and State.

47. Articles 12, 13, 14, 15, 16, 17 and 18 of the Enterprise Law provide for the orders, types and contents of documents, conditions, deadlines and the authority to issue business registration certificates. The above-mentioned provisions of the Enterprise Law provide for significant relationships between the State bodies in charge of registration of enterprises for establishment. The provisions are clear, specific, easy to understand and consistent in terms of each type of document required. In addition, the provisions are clear in their contents, the orders and procedures required, the rights and responsibilities of the investors, the authority and responsibilities of the concerning State bodies, the conditions for business registration certificates, and the time for commencement of operations (a prominent strength of the Enterprise Law compared to other laws).

48. However, the establishment of an enterprise does not occur merely with the registration of business; it is a process involving the formation an idea, investigation of investment opportunities, research into building the investment project, calculation of costs and benefits, deciding whether or not to invest, finding and selecting partners, selecting technology, deciding on the location of investment, business strategy[18], etc. Managing the process is the job of the investor. The investor ultimately decides whether to invest and must do so in accordance with the applicable provisions of Vietnamese laws. The registration of a business is simply the legal manifestation of the startup process. The success of starting a business seems to depend on the quality of preparations for doing business; simple procedures for business registration only facilitate implementation of the business ideas, initiatives and business opportunities.

49. Currently, business registration is just a procedure to join the market. After business registration, the next steps are: seal engraving (at the police office), registration for a tax code, purchase of VAT invoices, registration of labor rules, registration for a customs code (for direct import and export), applying for business licenses (with respect to the lines of business requiring licenses). A survey of the Research

[18] This is the preparatory stage for establishment of an enterprise carried out by the founders including 3 types of responsibilities: preliminary investigation (finding an investment opportunity for development), investigation and study (collecting information, analyzing the feasibility of the investment opportunity) and finally, finding and gathering the resources and necessary conditions to establish an enterprises and to organize business.

Committee of the Prime Minister and Ha Noi Industrial and Commercial Association (2003) showed that it took at least 54 to 63 days to complete the above three steps. Research by the World Bank (2004) showed that in Viet Nam, 11 types of procedures must be fulfilled, taking 63 days to complete and costing USD170 (i.e. 1/3 of the average GDP per capita) to fully "join the market". Comparatively, there are only two types of procedures that can be completed in two days and costs two percent of GDP per capita in Australia; seven types of procedures can be completed in eight days with the cost of 1.2 percent of GDP per capita in Singapore. The above findings indicated that although procedures have been simplified in the past few years, the improvements have placed Viet Nam in the middle of the pack, compared to the rest of the world. There is still much room for improvement. Procedures can be simplified, the time involved can be further shortened, and the costs further reduced.

50. There have been many instances over the past four years of business registrations carried out in a manner not compliant with Vietnamese laws. Two rather common situations are mentioned below. First, the requesting of supplementary documents contrary to the applicable regulations. These documents commonly include: certification (by the people's committee of the ward or commune) with respect to the legal record of the owner of an enterprise (with respect to a shareholding company with many shareholders, the request can be for the biggest shareholder), certification of the addresses of the head office, branches and representative offices, and certification or copy of evidence for the assets contributed as capital, contract for lease of office, lease of business premises. Second, requiring additional procedures not compliant with applicable regulations such as certification of contracts by a district people's committee with respect to a number of industries and trades, or the request for the certificate for satisfaction of business conditions prior to the registration for establishment of an enterprise.

51. Further consideration of requests contrary to the Enterprise Law indicates a number of noteworthy issues. First, with respect to the certification of personal status, the people's committee of the ward or commune where the person concerned registers his civil status is the authorized body. In fact, many people do not reside at the location where they register their civil status. The contents, conditions and deadlines for the certification are not provided for. Therefore, the certification is done completely at the discretion of the official requesting the certification. Similar problems appear in other types of certification. Setting out the above requests and procedures increases the costs involved and lengthens the time for establishment of an enterprise without achieving its initial goals or intent[19]. The abuse of purchase of invoices and refund of value added tax occurs right in the localities where documents and regulations contrary to the Enterprise Law are set out.

52. There are a number of causes leading to the above situations. Many authorized officials were concerned about State administration. In their opinion, without the certification of personal status, as well as the address, it would be difficult to know if a person who wishes to establish an enterprise is a good person and would not use the establishment of the enterprise to do illegal business. Other officials were concerned about their own responsibilities and accountability. They requested the certification in order to share the liability with another person in case an investor uses the registered business for illegal purposes. In addition, a number of authorities set out more procedures to avoid the gathering of an excess number of industries within a particular area, leading to a situation where "supply exceeds demand" and adversely affects local socio-economic conditions.

53. Experience has shown that during the first years of implementation of the Enterprise Law, the simpler processes of business registration have been abused by individuals illegally seeking profits through the purchase and sale of invoices, and the refund of value added tax. Some people illegally sought profits directly for themselves, while in other cases people were hired to be the nominal owners while those who hired them sought profits illegally. The people hired to be owners are often poor, have little qualifications

[19] Report on 4 years of implementation of the Enterprise Law, October 2003.

and are not trained for any profession or trade. The above facts were the basis for the recommendation to use a number of procedures and requests for certification of personal status as previously discussed; or to continue to maintain a number of certifications and procedures contrary to the Enterprise Law as indicated above.

54. The above situations mainly occurred in the first two years of the implementation of the Enterprise Law, because: (i) abuse of the regulations and mechanism for the refund of value added tax (for illegal profit) was not controlled and effectively prevented; (ii) from the beginning, officials who carried out business registration procedures interpreted and implemented "mechanically" their authorities and responsibilities without minimum examination and verification of the truthfulness of the documents; and (iii) State administration did not follow the changes and new requirements of the Enterprise Law; the relevant authorized bodies did not coordinate effectively.

Publication of business registration

55. The Enterprise Law requires both the business registration body and the enterprise to publicize information relating to business registration. According to Clause 1 of Article 20, within seven days from the date of issuance of the business registration certificate or the certificate of business registration alteration, the business registration body must send a copy of such certificate to three State bodies, namely (i) the tax office, (ii) the Department in charge of the relevant industries, and (iii) the people's committee of the district where the enterprise has its head office.

56. The intent of the above provision is to facilitate effective coordination between the State administrative bodies responsible for regulating enterprises after registration. The requirements of this provision are reasonable. However, a number of problems arose during the provision's implementation. First, while there are many and various industries and trades, there are only a limited number of industries and trades under the direct administration of a Department. Therefore, in many cases, business registration bodies did not know with which State bodies it needed to share information and to coordinate with in order to fulfill the requirements of the provision. In some cases, information regarding business registration was sent to Departments who had no desire to coordinate with the registration body because the enterprise did not fall under their official administrative duties regarding a limited number of industries. Second, the Departments and district people's committees did not establish a focal point, or a single administrative body in charge of receiving, updating and analyzing the information from the enterprises. Third, the tax offices and business registration bodies have different systems and methods to administer enterprises making coordination efforts between them ineffective. As a result, implementation of the above provisions did not satisfy the EL's original intent. Even with the EL, the administrative bodies involved, especially the relevant Departments, still complained that they did not have sufficient information on enterprises, and that they did not know how many non-State owned enterprises were operating in the industries under their administration.

57. Article 21 of the Enterprise Law requires that an enterprise must, within 30 days from the date of issuance of a business registration certificate, cause to be published in a local newspaper or a daily central newspaper, in three consecutive issues, key information regarding the enterprise[20]. Where any alteration is made to the business registration, the enterprise must arrange for the publication of such alteration with the same method.

58. The provision on publication in newspapers in Article 21 of the Enterprise Law is intended to provide initial information relating to the enterprise to people who are interested in the enterprise; and to create favorable

[20] Name, addresses of the head office of the enterprise, branch, representative office (if any), objectives and lines of business, charter capital (in the case of a company) and initial investment capital (in the case of a private enterprise), names and addresses of the owner, all founding members, full name and permanent address of the legal representative of the enterprise, place of business registration.

conditions for interested people to observe, supervise and to accomplish transactions with the enterprise. However, the implementation of the above provision is still very ineffective. First, the definitions of local newspapers and daily central newspapers are unclear. For instance, do they include specialized newspapers? Historically, there have not been many daily newspapers at both local and central levels. Most newspapers are every other day newspapers or newspapers with three, four or five issues a week. Second, only a few enterprises publish their information in newspapers. Most of enterprises publishing their notices of establishment are located in cities. Third, the cost of publishing notices of establishment is expensive, ranging from VND450,000 to VND1,000,000, depending on the kind of newspaper, the volume of information of the enterprise published and on what page the notice is published, etc. This cost is three to five times higher than the cost of business registration. Fourth, there are no effective penalties imposed on enterprises that fail to publish the required information in newspapers. Finally, the required information is not very useful to a person interested in the enterprise. Further research is required in this area to make this requirement more effective. Examination of how other countries apply and enforce this requirement may be useful.

59. Experience has shown that if a national, uniform information system is established, the intent of the above provisions would be carried out effectively with little cost to the parties concerned. Initial results of the business information network in Ho Chi Minh City have supported this assertion.

Capital, assets contributed as capital, capital contribution and a number of other related issues

60. Two widely recognized reforms of the Enterprise Law are: (1) the elimination of the requirement for compulsory minimum capital as a condition for establishment of an enterprise and for business registration and (2) the elimination of the requirement for certification of capital, etc. These changes help to reduce the costs of establishing an enterprise, bringing into full play and facilitating the opportunities, initiatives and other necessary factors (management capacity, qualifications, workmanship, etc.) needed for the operation and development of an enterprise. While at the same time, preventing the use of formalistic and automatic approval and certification (solely to fulfill a procedural requirement) in order to establish enterprises for illegal profits.

61. Initially, after the implementation of the Enterprise Law, there was some concern regarding the establishment of enterprises without any capital. Critics believed there would be enterprises registering a minimal amount of capital (several thousand VND) and would be in essence "bankrupt" (from a financial balance standpoint) right from the start, creating financially unhealthy enterprises. Experience has shown, however, that in general, the actual capital invested in a locality was often not less than the capital registered in the same period. The lowest registered capital of for individual enterprises was VND five million (typically for service businesses like restaurant services, tourism, retail of goods, etc.). The highest registered capital was VND 200 billion (typically in the field of business of construction and development of infrastructure). Empirical data indicates that there were cases where the capital registered was higher than the actual capital used in the business of construction[21]. The purpose of declaring a higher capital amount than the actual capital amount is to satisfy the conditions for tender participation. Improvements in the efficiency of investment management and construction, especially the exact evaluation of the capacity of the tender participants, shall significantly contribute to a reduction and removal of false statements of capital in business registrations.

62. Clause 4 of Article 3 of the Enterprise Law provides that assets contributed as capital may be in the form of Vietnamese currency, freely convertible foreign currency, gold, value of land use rights, value of intellectual property, technology, technical know how, or other assets authorized by the charter of the company to count towards the capital of the company. In principle, any kind of asset can be used for

[21] The literal translation is "observations in practice indicated that there were cases where the capital registered was *less* than the actual capital used in the business of construction" - Translator.

capital contribution if approved by the members of the company and authorized by the charter of the company.

63. Experience has shown that most of the registered capital was in cash (80%). Although the 1988 Law on Land stated that the use of the value of land use rights was a basic right of people who owned or leased land, value of land use rights has rarely been used for capital contribution. This suggests that a considerable resource has not been mobilized and used for the purpose of investment and production.

Box 2: "Idle capital" in developing countries

Billions of people in developing countries are living in poor housing conditions in slums without any certificate of ownership. It seems that these cheap houses and slum real estate have insignificant value.

However, there are a countless number of these houses and the aggregate value of all of these houses and real estate would exceed the total wealth of the world's richest people. In Haiti, the value of land without certificates of ownership in the country side and in cities is appropriately US$5.2 billion which is four times higher than the total assets of all companies legally operating in Haiti, nine times higher than the assets of the Government, 158 times higher than the total value of foreign investments in Haiti. In Peru, the value of land without certificates of ownership is appropriately US$74 billion which is equal to five times the total value of the Lima Stock Exchange (before its collapse in 1998), 11 times higher than the value of Government enterprises and establishments which can be privatized, and is equal to 14 times the total amount of foreign investments Peru has ever received. The situations in Haiti and Peru are not unique.

Source: The Mystery of Capital (the Vietnamese version translated by Nguyen Quang A in 2003)

64. The process of converting land use rights has created unreasonable obstacles, such as rigid, time-consuming and onerous administrative procedures. Regrettably, the transfer of land use rights means the loss of farmers' rights to use land. The amount of "dead capital" in Viet Nam is not small.

65. It has been commented that a basic success of the Vietnamese revolution was the distribution of land to farmers. Currently, this basic tenet of the revolution has been eroded due to administrative procedures and the unreasonable distribution of benefits from the conversion of land use rights away from farming. The current environment has created a paradox where the supply of land for development, industry and urban areas has been restricted due to burdensome procedures required for the conversion of land use rights; while at the same time, demand for such land has increased significantly. The result is an increasing imbalance of supply and demand. This irrationality has caused difficulties and contradictions in the process of industrialization and urbanization. This contradiction is one of the major obstacles impeding industrialization and urbanization, and acts to slow Viet Nam's development.

66. Realizing the above irrationality, the leaders in one province have recommended a 70/30 split of land use rights. When agricultural land is converted for use in development of industry or urbanization, the farmer's household retains land use rights over 30 percent of the land for the usage purpose to which the land was converted, while the remaining 70 percent is for State purposes[22]. With this remedy, it is hoped that the farmers will have assets to contribute as capital to companies. In this way, the ambition of turning farmers into "shareholders" may be realized.

[22] This mechanism is similar to the previously used centralized planning mechanism of "five percent land."

67. It has been recommended that farmers should be permitted to decide whether their land should be converted to a site of industrial production without the need for State authorization and interference. Diversification has gradually spread among the farmer households in a number of localities, especially in localities where traditional industries and trades exist. A number of households have quit farming to concentrate solely on business enterprises. These households no longer use the land they were allocated for the purpose of agricultural production.

Facing the demands of urbanization and development of industry, some agricultural land has been converted. But as a result of rigid land use planning, the land of households specialized in agricultural production was often used for development of industrial clusters, while the land of households specialized in industry was commonly used for the development of agriculture. The new thinking is that policy must be constructed so as to motivate and allow people to make their own decisions regarding whether and how to convert their allocated land (with guidelines from local authorities). In this way, farm households will have more land for agricultural production, and the industrial households will have enough land for use as the site of production and business without incurring additional expenses. The State can, therefore, accelerate the development of both industry and agriculture without increasing expenditures.

Box 3: The whole hamlet contributes farming land to establish a company

In Bac Vong Hamlet, Bac Phu Commune, Soc Soc District in the outskirts of Ha Noi is a farming locality with 800 laborers. In early 2003, Mr Thuc (an agricultural engineer) proposed that farmers consolidate their land and use the value of the land as capital contributions to start a big business, challenging the notion that investments should be made only in small businesses and that farmers are not willing to take large risks. His idea was well received by the municipal authorities, the Party cell and the farmers. A number of investors, like the Central Seeds Company No. 1 and Viet Ha Beer Company, also supported this idea and cooperated in doing business. In early May 2004, 227 farmer households signed contracts to contribute their small farming land areas to the company and effectively became shareholders of the company; while another 43 households signed contracts for the long-term lease of their lands to the company. A big business plan, using the capital from the land contributed by the farmers, is being carried out. With this method, Bac Vong Shareholding Company had 50 hectares of land at the time of its establishment without incurring any costs for compensation or clearance.

Source: Law Newspaper of Ho Chi Minh City dated 14 July 2004.

68. Many believed that the technique used in Bac Vong hamlet was effective and was met with social approval. The ability of land users, through the value of land use rights, to contribute capital to an enterprise allayed farmers' fears that their lands would be taken as had happened with past projects. With this method, farmers maintain an interest in the land contributed to the company in the sense that they, as shareholders, receive dividends distributed by the company, the value of which may equal the value of using the land in traditional agricultural production. In addition, they are employed as paid workers. This mechanism also facilitates and diversifies the ways in which investors can obtain land at low cost, helping in the establishment of a stable and enduring business.

69. In practice, there are many projects in many localities where farmers and investors can make their own agreements. These arrangements for land on the basis of the mutual benefits and compliance with the planning for use of land are made with little cost and effort to the involved State bodies.

Box 4: Houses cannot be contributed as capital due to unclear procedures

Mr Anh[23] is a shareholder in H.A. Shareholding Company registered in Ho Chi Minh City. In 2001, the shareholders agreed to allow Mr Anh to use the house No. X, T.D street, district 3, Ho Chi Minh City as capital to purchase more shares. When visiting the business registration office to fulfill the procedures, H.A. Shareholding Company was instructed to come to the Housing and Land Department. When visiting the Housing and Land Department (the Centre for Information and Registration of Houses and Land), it was referred to the Notary Public Office No. 1. When visiting the Notary Public Office No. 1, the Office received a notice that "…Currently, we have no regulations on increasing the charter capital of a company by way of receiving more capital contribution being real estates (residential houses) from members of the company without issuing new shares". As a result, Mr. Anh was not allowed to purchase of shares with real estate.

70. However, there are many barriers to the use of non-cash assets as capital contribution. These include, unclear certification of the ownership rights over assets, especially assets which can be used for capital contribution; complicated and costly procedures for assignment of ownership rights over assets; no mechanism and institutions for professional, objective, high quality and reliable valuation of the asset.

71. Regarding the "mechanism" to determine the value of non-cash assets contributed as capital, Article 23 of the Enterprise Law distinguishes two main cases: capital contribution upon establishment and capital contribution during the course of operations. With respect to capital contribution upon establishment, the value of assets is determined by the unanimous approval of the founding members. With respect to the second case, the Board of Management (for a shareholding company), Council of Members (for a limited liability company) and all partners (of a partnership) shall be the parties responsible for valuing the assets contributed as capital. Clause 4 of Article 23 clearly lays out the obligations of the persons responsible for valuing the assets in terms of the determined value of the assets. This Clause also outlines joint liability in the case of incorrect valuation causing loss to the company and to concerned parties.

72. Experience has shown that the above provisions have a number of strengths and weaknesses. Strengths include flexible and convenient procedures needed to satisfy the requirements to be founder (of a business). Typically, most founders of businesses are related to each other, as family members, siblings and relatives. They know each other well, including each other's property status. Therefore, the approval of each asset's valuation by members of the enterprise is both rational and cost saving. The enterprise benefits by avoiding unfair treatment of capital contributions, such as overvaluing of an asset contributed by a family member. The requirement of unanimous approval of valuation ensures equal treatment and fair dealing with individuals contributing capital.

73. The weaknesses of the above provisions are indicated in a number of points. First, there is a danger that the valuation is higher than the actual value, and subsequently, that the registered capital is higher than its actual value. This can be mislead and put at a disadvantage inexperienced creditors. Second, the method used to value the assets contributed as capital during the course of operations is unclear. For example, permitting the Board of Management of a shareholding company to determine the valuation of assets contributed as capital during the course of operations can create a loop-hole, which can affect the interests of the company and minority shareholders. The measures to deal with incorrect valuation (either intentionally or in good faith) are weak; and the mechanisms for enforcement is unclear and ineffective.

[23] Name of the shareholder and name of the company in this box have been changed.

74. Experience has shown that the provisions of Article 23 were consistent with Viet Nam's under-developed market, especially the market for assets for capital contribution. Professional valuation organizations have not yet developed and are therefore unable to provide professional and reliable services. However, with the development of greater market regulations, additions to the above provisions are needed to strengthen the provisions and to overcome the weaknesses (mentioned above).

Name, naming an Enterprise and the office of an Enterprise

75. Clause 1, Article 24 of the Enterprise Law provides for names and the naming of an enterprise. The Law has set out four key requirements with respect to names of enterprises including: (i) not be the same as, or cause confusion with, the name of another enterprise; (ii) not contravene national historical traditions, culture, ethics and fine customs; (iii) be written in Vietnamese, and in addition may be written in one or more foreign languages in smaller letters; and (iv) the type of enterprise must be specified.

76. Compared to the Law on Companies and the Law on Private Enterprises (1990)[24], the above provisions of the Enterprise Law are an improvement. However, the above provisions are still unspecific and insufficient to deal with matters that arise in practice relating to names of enterprises. In practice, difficulties have arisen during the application of these provisions.

77. First of all, the above provisions on names of enterprises only apply to enterprises registered under the Enterprise Law. Therefore, there is no legal basis to provide guidelines on names and a uniform method for naming applicable to all types of enterprises without distinguishing (the forms of) ownership.

78. The concepts of having the same name or a name that could cause confusion is unclear. In practice, the name of an enterprise may include (i) its full name in Vietnamese; (ii) its name in a foreign language (normally English); and (iii) an abbreviated name (which can be abbreviated from its Vietnamese name or English name). However, there are no provisions addressing the relationship between a name written in Vietnamese and the same name written in a foreign language. As a result, a number of enterprises have Vietnamese names that bear little or no similarity with foreign language name. Up to now, because Vietnam has not had a unified national network to address naming issues, the management of same names and names causing confusion can only be carried out within each province and city under the Central authority. Therefore, in practice, it is not yet possible to distinguish same names and names causing confusion[25].

79. The connotation of "national historical traditions, culture, ethics and fine customs" is unclear. Viet Nam is a multi-ethnic nation (54 ethnic groups) making the determination of a "national historical tradition, culture", as stated in the above provision, difficult to define clearly. Experience has shown that this concept usually depends on the subjective evaluation of a person or a group of people[26]. Experience suggests that if this provision remains, the business registration body should be empowered to evaluate, approve, or refuse a "controversial" name.

80. The provision stating that "names must be written in Vietnamese" is not interpreted consistently. A frequently asked question is: What is Vietnamese? Many enterprises have given themselves non-sensical Vietnamese names in that the letters and the sounds do not exist in the Vietnamese language (e.g., IES company, ARTECH company, etc.).

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[24] The Law on Companies and the Law on Private Enterprises permitted enterprises to name themselves at their discretion.

[25] In Ha Noi, there are thousands of companies named "Thang Long", with hundreds of companies having the same abbreviated or English names.

[26] For example, there was a limited liability company named "An Nam" in Ho Chi Minh City. A veteran felt that the name"An Nam" was unacceptable because this name was attached to a tragic period in the nation's history. Others disagreed because Viet Nam's political party was once named "An Nam". However, veteran's objection overcame the critics and the enterprise had to change its name.

81. The above shortcomings of the provision have helped to cause a number of negative outcomes. First, there is a rise in overlaps of names and in names causing confusion, threatening the interests of both enterprises and consumers. In addition, disputes over names between enterprises, the founders of enterprises, and the business registration body are also on the rise. Business registration bodies are having increased difficulties in managing names of enterprise in a consistent and uniform manner. The above difficulties have been partly resolved by adding a chapter on naming enterprises in Decree 109-2004-ND-CP dated 2 April 2004 replacing Decree 02-2000-ND-CP dated 3 February 2000 on business registration.

III. LIMITED LIABILITY COMPANIES

A number of issues in relation to the concept of limited liability companies

82. First, the Enterprise Law distinguishes two types of limited liability companies: one-member limited liability companies and limited liability companies with two or more members. However, only "organizations"[27] may establish one-member limited liability companies; individuals are not permitted to use this type of enterprises to do business.

83. The above provision has diversified and increased the types of enterprises allowed, creating favorable conditions for socio-political organizations and associations to make better use of and to maximize their resources, as well as to fully exploit their comparative advantage in the market. These entities are able to set up businesses without having to go through a particular individual, as was previously required. Therefore, the management and use of land of these organizations have become more effective[28]. A Limited liability company structure also helps enterprises to become more active and self-controlled in expanding the scale, areas and scope of business. For instance, thousands of enterprises have used the one member limited liability company form to expand their investments to other provinces and cities and/or to do business in other industries.

However, with regard to the prohibition of individuals to establish one-member limited liability companies, a number of shortcomings have arisen. For example, the provision limits the types of enterprises individual investors may enter. This does not foster favorable conditions for individuals who do not wish to share their business ownership with others (even to reduce and to allocate risk more effectively).

84. Practical surveys have shown that Vietnamese people tend to do business alone or with family members. The above restriction prohibiting the formation of one-member limited liability companies by individuals has forced many people to comply with laws by adding one or more merely nominal members to their enterprise ownership structure. This nominal member is taken on in name only and contributes an insignificant amount capital[29]. Nominal members often sign secret contracts regarding the use of only their name without any real involvement or rights in the business as a member.

There are several consequences of this nominal compliance with the EL. First, the provisions of the EL are not as effective as intended (many limited liability companies are still one member companies, wholly managed by that member). Second, merely nominal compliance has caused a number of contradictions

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[27] "Organization" is a political rather than a legal concept. There is no definition of "organization" in the current legal doctrines.

[28] For example, the guest houses and hotels of socio-political organizations have been officially registered as one member limited liability companies. As a result, the cost accounting has been clearer, taxes are paid and the limited liability corporation receives legitimate income.

[29] The owner of a company, with business capital of hundreds of millions of dollars, has acknowledged to the public that he has "hired" the names of two more members to comply with the required procedures.

and disputes between the real members and the hired nominal members[30]. In these disputes, the members in name always win legal decisions, making them full members of the company with the rights, interests and obligations prescribed by law. Not only do these decisions create greater costs and dilutes benefits to the company, but they also strain important personal relationships, vitally important in Vietnamese life and culture, such as the relationships between a father and his children, siblings and friends.

85. In conclusion, not permitting individuals to establish one-member limited liability companies denies the individual investors the right to freely select a type of enterprise and to limit and allocate risks reasonably. At the same time, this threatens to cause undeserved negative consequences to a number of investors and companies. There is potential for the impact to be widely felt, considering that many *de facto* one-member limited liability companies started by an individual exist and are currently in practice.

Limited liability companies with two or more members

86. In general, limited liability companies with two or more members have been provided with clear and consistent the principles commonly recognized in the legal systems of other countries. Since implementation of the Enterprise Law, empirical evidence has shown that this type of enterprise is very common in our country[31] and suitable to the custom and method of management of the domestic private investor. The evidence has also shown, however, a number of shortcomings.

Rights of limited liability companies

87. The provisions and mechanisms for protection of members holding minority shares are not yet complete, clear, and effective. The legitimate interests of members holding minority shares are provided for in Clause 2 of Article 29, Article 31 (redemption of shares of equity), and Article 38 (Conditions and procedures for conducting meetings of the Council of Members). Although Clause 2 of Article 29 grants to minority shareholders the right to request that a meeting of the Council of Members be convened, it does not clearly stipulate the process, order and authority to implement that right.

In addition, Clause 2 of Article 29 provides discretion to determine a minority percentage (and therefore minority shareholder status) of less than 35 percent of the ownership. This flexible and improved provision favors minority shareholders. However, in practice, many minority shareholders in limited liability companies own less than the required 35 percent of the enterprise. The charter does not address ownership percentages less that 35 percent. As a result, when the legitimate interests of groups holding less than 35 percent ownership are affected, they have no recognized rights, such as the right to request a meeting of the Council Members, and are powerless. Due to this lack of authority, the right to request a meeting of the Council of Member has not been exercised and the legitimate interests of this group have not been effectively protected[32].

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[30] In a limited liability company in Hanoi, the father permitted his daughter to nominally own 30% of the enterprise. When the business became successful, his daughter moved to another city. At that time, the daughter, as a shareholder, exercised her rights of ownership over 30% of the enterprise. The father had to "compensate" his daughter otherwise the 30% ownership would have been assigned to another person.

[31] Currently, the number of limited liability companies with two or more members accounts for 50.8**%** of the total number of registered enterprises (compared with**...%** in the period prior to 2000).

[32] A rather common case, in practice, is when a majority member owning more than 65% of the enterprise, being the legal representative of the company, is prosecuted for a criminal offense. With the above shortcomings, the remaining members have little recourse, even a meeting of the Council of Members cannot be convened to elect a replacement legal representative. As consequence of having no legal representative, the daily operations and transactions may be considered illegal. This leaves an enterprise with the unfortunate choice of either to not operate the enterprise or to break the law by conducting business.

88. The provision granting minority shareholders the right to redeem their shares of equity has not been effective because there is currently no market price for the equity and therefore no way to determine the value of the equity shares to be redeemed. In addition, the charters of companies studied did not prescribe valuation methods of shares of equity to be redeemed. The Enterprise Law has provided no remedy where a company refuses to redeem the equity shares as required. In practice, this situations leads either to members agreeing to stay with the company in exchange for improvements to existing rights and interest, or the company redeeming shares at a low price and allowing the member to withdraw from the company.

89. The provision (Point g, Clause 1, Article 29) determining the right of a member to commence a court action against a Director (General Director) for failing to perform fully his or her obligations in such a way that it causes direct damage to the interests of the member is an improvement in the Enterprise Law. The intent of the above provision is to pressure the management personnel to strictly uphold their obligations and to prevent abuses of power causing damage to the company and to interested parties. However, this right to commence legal action has rarely been exercised. This is partly due to a culture of rarely taking a legal action, as well as a wait and see attitude in the absence of issuance of provisions explaining the procedures for bringing such an action.

90. A limited liability company is a “closed” company. Therefore, shares of equity will not be assigned freely as in the case of shareholding companies. Articles 32 and 33 of the Enterprise Law have set out the strict provisions on forms of assignment. In particular:

- A member wishing to assign his/her shares of equity must first offer to sell such shares to all other members. Each member has a right to purchase a percent of the offered shares in proportion to their ownership of shares of equity in the company. Any remaining equity shares may be assigned to non-members.
- With respect to the shares of equity of member has died, his or her heir(s) may receive the shares and become a member of the company, subject to approval of the Members’ Council. Similarly, if a member has limited or restricted mental capacity, the rights and obligations of that member shall be exercised by his or her guardian subject to the approval of the Members’ Council.
- If a member is an organization that has been dissolved or has declared bankruptcy, its equity shares shall be redeemed by the company or assigned in accordance with Article 32.

91. Experience has revealed some problems, particularly in the case where a majority member (usually the legal representative of a company) dies or loses his or her mental capacity. In this case, a number of unreasonable outcomes have occurred, including:

- A meeting of the Members’ Council may not be convened, the business of the company may not be conducted normally and transactions of the company may be deemed to have been void (as mentioned above). Ironically, even a decision on acceptance of his or her heir as a member may not be made.
- Where the company is running smoothly, the other members usually have a tendency not to accept his or her heir as a member of the company. Instead, the equity shares will be redeemed by the company. However, the redemption, if so performed, will not be fair.
- The above-mentioned provisions have significantly restricted the utilization of shares of equity for mortgages or pledges due to limitations on the mortgagee or pledgee to dispose of such shares in the most advantageous manner, when necessary.

In short, the extremely strict provisions on the forms of assignment of shares of equity have caused damage to the legitimate interests of majority members in some cases, and have made the normal operation of companies difficult. In addition, provisions for giving or donating a share of equity to another

are not available. It can be said that the above shortcomings have excessively restricted the right of limited liability company members to dispose of equity shares.

A number of issues in relation to internal management of companies

92. The internal management structure of a limited liability company is comprised of the Members' Council and the Director (or General Director). The Director (or General Director) manages the day-to-day operations of the company, while the Members' Council decides all the affairs of the company. In addition, the Members' Council supervises the activities of the Director (General Director). The Members' Council performs the same duties and has the same function as the General Meeting of Shareholders, and the Board of Management of shareholding companies.

93. Thus, in limited liability companies with two or more members, there is no difference between an owner and a manager. Members both control and directly manage the business activities of the company. However, this is only true if the member is an individual. In cases where the member is an organization, the member is only an authorized person; and in many cases, the authorized person receives orders from a higher level authorized person, but not from the owner. This situation has revealed issues relating to authorized persons in the Members' Council.

94. A majority shareholder may control an authorized person[33], belonging to the same group of shareholders, in order to further his or her interests, while damaging the interests of minority shareholders and other persons concerned. Authorized persons at different levels may co-ordinate their efforts to further their collective interests and to damage the interests of the company, as well as other concerned parties, including the owner. Conversely, each authorized person may use his or her position and power for personal gain and benefit. The issues mentioned above may become more serious if the authorized person is also the acting Director (General Director).

95. Obviously, the above-mentioned matters should be taken into consideration when the scope of the Enterprise Law is expanded to include enterprises with State and foreign shareholders.

96. The Members' Council is only required to hold at least one meeting a year. One meeting is not enough compared to the position, functions and powers of the Council. In addition, with exception of the chairman, the other members are comparatively passive at the meetings. There are no provisions giving members the power to have any impact or affect on business matters discussed at the meetings, even when they (members or group of minority members) request the meeting.

97. With regard to the mechanism for the internal management of limited liability companies with two or more members, the Enterprise Law has set out open and flexible provisions (with minimum limits), in particular:
    - The agenda and documents for a meeting of the Members' Council must be sent to members of the company prior to the first day of the meeting. How much notice to be given to the members prior to the meeting shall be stipulated in the charter of the company (clause 2 of Article 37).
    - A meeting of the Members' Council shall be deemed convened and effective when the attending members represent at least 65 percent of the charter capital. But a higher percentage may be stipulated in the charter of the company (clause 1 of Article 38).
    - Approval of "ordinary decisions" by the Members' Council requires at least 51 percent of the total votes of members attending the meeting. For "special decisions", at least 75 percent of the total votes

[33] For example, a majority member may pay "remuneration" to "an authorized person" to purchase his or her right to vote in order to influence the vote in a way favorable to the majority shareholder's self-interest.

of members attending the meeting is required for approval. Higher percentages for voter approval may be stipulated in the company's charter (clause 2(a) and (b) of Article 39).

- Where the Members' Council makes a decision through written opinions, the decision shall be passed if approved by members representing at least a 65 percent of the charter capital. Higher percentages may be stipulated in the company's charter (clause 2 (e) of Article 39).

98. The well-known strength of the above provisions is increased flexibility and discretion (*du dia*) for members to mutually agree and to discover the most efficient ways to comply with the legal limits of the ownership structure and to maximize production given the actual capacities of each of the members of the company. By maximizing efficiencies within the regulations, the members may better protect both their own and the company's interests.

99. However, the implementation of the above-mentioned provisions has exposed several practical problems. First, the minimum limits referred to in the above provisions are low (compared with other countries)[34]. In other words, the aperture is too wide. In many cases, members, in general, and minority members, in particular, are unable to recognize opportunities granting them the right to manage in the way that conforms best with the specific conditions of the company and ensures a harmony of rights and interests of members. In other cases, although minority members are aware of their rights provided by the Law, they do not have sufficient power and capacity to enter into negotiations for greater management control of the company. As a result, the rights and interests of the minority members are often infringed. The majority member (holding 65 percent ownership) controls both the management and the operations of the company at his or her discretion. In addition, the interests of creditors may also be infringed if the majority member is the owner of the corporate group.

100. In limited liability companies with two or more members, the members are concurrently, both the owners and the managers. As owners, they are entitled to profits; and as managers, they are entitled to wages. These entitlements should be clearly determined in order to improve the transparency of the company's internal management. This is especially true when a number of the members are persons only authorized to exercise the rights of the owner. Such persons are only entitled to wages and other benefits, but are not entitled to profits. However, due to the persons' concurrent legal identities (as authorized person and manager), they may be entitled to two wages. The owners will pay wages to the authorized person and the company will pay wages to the manager. The necessity for reasonable, clear wages and benefits with proper disclosure is crucial. This contributes to the transparency and general health of not only the persons with dual legal identities, but also the internal management functions, including the upholding of rights, duties and interests in management's organization, and the operation of the company.

101. Clause 2 of Article 35 of the Enterprise Law provides that the Members' Council shall make decisions on investment projects valued at more than 50 percent of the total value of the company's recorded assets, and approve loan agreements and contracts for sale of assets valued at 50 or more percent of the total value of a company's recorded assets. Transactions with large scale of companies, especially contracts for selling assets and raising or providing a loan, will have a great impact on the financial structure of the company and creates a negative risk for the position and interests of the company members. Therefore, these provisions are appropriate in limiting the Members' Counsel's decision-making authority in order to safeguard the interests of the company members.

102. Strengths of this provision are its clarity, straight forwardness and ease in implementation. This is apparent especially in situations where the rules on the conduct of managers have not been established, where society has little knowledge of a market economy and where the court has not become a tool for the resolution of commercial disputes in general, and internal disputes of companies in particular.

[34] This percentage in Asian countries is 75% (compared to corporate management in a number of Asian countries, CIEM-VNCI-2004).

103. Nevertheless, it must be recognized that book value is not an accurate measure for the size and importance of a transaction. Using a certain fixed percentage of the book value to determine a cut off point for assigning management responsibilities may be too flexible. In some cases, such an approach may prove not specific enough. For example, the fixed percentage may not include cases where the transaction value is less than half the book value and yet the nature of the specific transaction may be such that it really should be decided upon by the Member's Council.

An issue arising from the implementation of the EL is the counterfeiting of Members' Council decisions. In many cases, the counterfeit decision is made "in good faith" (for example, in order to complete the filing for borrowing) and also to truly serve the business of the company. If the transaction is successful and has a positive result, no legal liability arises. However, the question is whether or not the official in charge of credit assessment (who has failed to discover "the counterfeited file") jointly assumes the responsibility and many be prosecuted for the oversight. Several bank officials have criticized the provision for causing banks to be cautious and to favour mortgage credit transactions with non-State enterprises.

Supervision of transactions with related persons

104. The provisions regarding the supervision of company transactions with related persons are designed to ensure that such transactions are conducted fairly. These are new and progressive developments of the 1999 Enterprise Law.

However, this provision has some problems. In addition to the failure to sufficiently define related persons, Article 42 only requires Members' Council approval of company "contracts" with related persons. Therefore, transactions that require no contract will not require the special approval of the Members' Council. This loophole may allow for abuses by related persons.

Nevertheless, supervision of transactions to ensure fair dealing and to prevent personal gain is difficult. It requires investigation, collection of evidence, analysis and evaluation of transactions.

105. The contents of Article 42 are not clear. Contract terms to be disclosed to members is not stipulated. In general, members must conduct their own investigation and collect evidence in order to prove an unfair transaction leading to personal gain. Who will bear the costs of this work? The costs of investigation may lead to a situation of "ignoring and benefiting (*an theo*)" where the unfair transaction is allowed in exchange for sharing in the benefits. If a member investigates and considers a transaction unfair, but the Members' Council still approves the transaction, is the member allowed to initiate court action? Who will bear the costs incurred from the proceedings? The provision that a contract shall be void without approval by the Member's Council is somewhat unreasonable and impracticable, especially if the contract has been performed in good faith. In addition, there is no remedy in cases where related persons failed to compensate for damages or failed to return gains from the performance of the contract.

IV. SHAREHOLDING COMPANIES

Shareholding Company Concept

106. As in the case of limited liability companies, the general term shareholding company, uniformly defined in the Enterprise Law, is compatible with common principles and provisions widely used in systems of laws in other countries.

107. However, with regard to the right to issue shares, clause 2 of Article 51 provides that "Shareholding companies may issue securities to the public in accordance with legislation on securities". A common question is: Can a shareholding company carry out a private limited share issue (not to the public)? The above provision implies that if a company carries out a limited share issue, not to the public, the Enterprise

Law shall apply[35]. Unfortunately, "limited share issue", in general, and the issue of each class of shares[36], in particular, have not been provided for in the current Enterprise Law. So, even in cases where the public issue of shares is not a favourable tool, the limited share issue may not be conducted.

Shares and other types of securities

108. Regarding tools for raising capital, the Enterprise Law has provided ordinary shares and a number of classes of preferred shares (but has not provided for derivative tools such as option etc.). This has restricted shareholding companies from creating inside opportunities for their staff to purchase shares and raise additional capital.

109. The Enterprise Law provides for voting preference shares. The purpose of voting preference shares, as stipulated by the Enterprise Law, is to give the founding members discretion in the management, control, and development of the company in the first years. However, this tool is rarely used.

110. While the Enterprise Law provides for voting preference shares, the Law on State Owned Enterprises and the Decree on equitization provide for "controlling capital contribution or controlling shareholding". Both the voting preference shares and controlling shares grant persons possessing these types of shares greater voting rights than other shareholders. Unlike other types of shares, controlling shares have "absolute" powers[37]; and when the State holds controlling shares, the voting rights of the other shareholders will no longer be valid. This is one of the incompatible issues between the Enterprise Law and the Law on State Owned Enterprises and has led to a number of situations where SOEs have carried out equitizations that are subject to the Enterprise Law.

111. In regards to capital contribution, the provisions of clause 1(d) of Article 14 and clause 5 of Article 12 are inconsistent with clause 1 of Article 51. Clause 1(b) of Article 51 implies that shares must be paid in full upon purchase. However, shareholders are only required to state the number of shares subscribed by them in the filing for establishment. Moreover, the purchase of shares with deferred payment is allowed. The above inconsistency has allowed abuses from some persons who become founding members of the company without any capital contribution; and are not jointly liable for the debts of the company, even a debt amount within the value of the shares subscribed. In practice, the items of Articles 14 and 15 have been widely performed in the first three years of the implementation of the Enterprise Law.

Rights of ordinary shareholders

112. Article 53 of the Enterprise Law provides most of the basic rights of ordinary shareholders. The rights so provided are compatible with the best corresponding practice. However, based on the best practice regarding corporate management and matters arising practically, the rights of shareholders have several defects.

113. Shareholders are not provided with or given access to all information, records and documents of the company. Shareholders do not have the right to inspect accounting books, minutes of General Meetings of Shareholders or the Board of Management, and no right to access other important information needed

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[35] This sentence does not make sense in Vietnamese.

[36] Namely, ordinary shares, dividend preference shares, redeemable shares and so forth.

[37] In enterprises in which the State holds controlling shares or has a controlling capital contribution (fifty (50) or more percent ownership), the State shall have the right to control such enterprises (clause 5 of Article 3 of the 2003 Law on State Owned Enterprises). In addition, a "controlling right in an enterprise means the right to decide the operational charter of the enterprise; to appoint, suspend or dismiss key managerial positions in the enterprise; and to organize management and make important management decisions of such enterprise" (Clause 8 of Article 3 of the 2003 Law on State Owned Enterprises).

as the basis for investment decisions. In addition, Article 93 refers to a summary of annual financial statements, but does not specify requisite items to be disclosed in these summary financial statements. The fact that shareholders are not entitled to full and timely access to information regarding the future plans of the company increases the risk to shareholders, especially minority shareholders. While at the same time, making it more difficult for shareholders to protect their legitimate rights and interests in the company.

114. Shareholders are entitled to access information on other shareholders only in the register of shareholders and the list of shareholders entitled to attend General Meetings of Shareholders. Only a shareholder or a group of shareholders holding at least ten percent of total shares has the right to view and receive a copy or extract of the list of shareholders entitled to attend General Meetings of Shareholders. The above provision is unfair and prevents small or minority shareholders from discussing, exchanging and gathering in groups to coordinate votes, thereby jointly protecting their rights and interests. In other words, the above restriction has further weakened small or minority shareholders. In other words, minority shareholders, already isolated, will become more scattered, further inhibiting their ability to consolidate votes and power).

115. Clause 2 of Article 35 focuses on a number of rights of minority shareholders. In particular, a shareholder or a group of shareholders holding ten percent (or a smaller percentage as stipulated in the charter of the company) of the company's ordinary shares for a consecutive period of six months or more shall have the right: (i) to nominate candidates to the Board of Management and the Inspection Committee (if any); (ii) to request the convening of a General Meeting of Shareholders; (iii) to view and receive a copy or extract of the list of shareholders entitled to attend General Meetings of Shareholders; and (iv) to recommend items to be included in the agenda of the General Meeting of Shareholders (clause 2 of Article 73). The above-mentioned provisions are intended not only to create better conditions and tools for the protection of the interests of minority shareholders, but also to prevent the possibility of harassment by minority shareholders that might damage the interests of the company and other shareholders.

116. The right to nominate candidates to the Board of Management and the Inspection Committee is intended to allow minority shareholders to have representatives in the management bodies of the company. However, the Law has not provided for principles to determine the number of candidates minority shareholders may nominate. In addition to minority shareholders, who else is entitled to nominate candidates to the Board of Management and the Inspection Committee? Furthermore, is there any priority given to candidates in the selection of the final list of candidates prior to the official election?[38]

117. The right of minority shareholders to request the convening of a General Meeting of Shareholders is limited to the following cases: (i) where the Board of Management commits a serious breach of the obligations of managers, or (ii) passes a resolution beyond its delegated authority (clause 2(b) of Article 71)[39]. In addition, the Law has not specified the required form and content of such a request, as well as the time period for the performance of the request. The above limitation has, in practice, caused two contradictory results. First, in a number of cases, shareholders have failed to find an effect way to use their rights. Second, a group of minority shareholders (with the support of several State employees) has used this tool to create pressure to change the Board of Management in a way to further their own intentions and objectives. Experience has shown that minority shareholders will be unable to effectively exercise these rights if there is no system for independently, professionally and effectively resolving disputes.

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[38] The above-mentioned problems are one of the reasons for different understandings and interpretations of the validity of the Board of Management and the Inspection Committee (in the second term of Phan Thiet Hotel Shareholding Company).

[39] The reader should "connect" paragraph (b) of Clause 2 of Article 53 with paragraph (b) of Clause 2 of Article 71 to understand the scope of the right of minority shareholders to request the convening of a General Meeting of Shareholders.

118. Founding shareholders are restricted in their assignment of shares. Founding members of a company usually perform three types of works. In addition, the Enterprise Law has used "involvement in approving the first charter of the company" as "evidence" of being a founding member. The evidence mentioned above is clear, specific and has legal basis. However, experience has shown that the application of this evidence to define a founding member in SOEs carrying out equitization is not appropriate in regards to the definition of a founding member and the limitation on assignment of shares (as discussed below).

119. Basically, the Enterprise Law recognizes the right to freely assign shares. The only restriction on assignment is applicable to shares of founding shareholders; and the period of restriction is only three years from the date of issuance of the business registration certificate. The purpose of this restriction is to assign responsibilities and risks of founding members to their business project. It is also considered a tool for protecting the interests of newcomers. This restriction is also intended to prevent the possibility of a number of persons taking advantage of their position as founding members to deceive and misappropriate capital and assets of other persons, especially persons lacking knowledge and experience.

120. Several provisions of Article 58 are unclear. Pursuant to Article 58, founding shareholders must, as a group, collectively hold, at least, 20 percent of the company's total ordinary shares that may be offered for sale. Founding shareholders may assign ordinary shares to persons who are non-shareholders upon approval by the General Meeting of Shareholder. In practice, a common question arises regarding whether or not founding shareholders are permitted to assign a portion (including most) of their shares: Must the minimum percentage of 20 percent of the number of ordinary shares be held by all of the original founders in the first three years from the date of business registration or can it be transferred to one or more within the group?

121. In the past four years, there has been no case in which a shareholder took advantage of his or her founder status to misappropriate capital of another. However, this does not mean that the provision has achieved its objective. Conversely, some shareholders have wished to assign their shares to other persons (in some cases seeking out the purchaser) in-spite of current restrictions. These shareholders were unable to carry out the assignment or conducted the assignment underground. In practice, some shareholders effectively carry out the assignment but do not re-register the assignee as a shareholder in the register of shareholders. In this case, the assignee authorizes the assignor to continue to attend and vote in General Meetings of Shareholders and to exercise the other rights of a shareholder under the instruction of the assignee (the true shareholder). In other words, the assignee enjoys and exercises all the statutory rights of a shareholder, except for official registration of his/her name in the register of shareholders. In some cases, a shareholder has the right to assign shares, but the assignment may not be completed because the Board of Management refuses to register the assignee in the register of shareholders which is required for him or her to become a shareholder of the company. The above practice is relatively common in SOEs carrying out equitization.

122. The unreasonable restriction on the assignment of shares has caused a number of negative outcomes. First, this restriction is a barrier to the expansion and making public of the operations of the share market, in general, and of the capital market, in particular. Second, the restriction on assignment of shares reduces the pressure on managers and restricts the appearance and development of a corporate management market.

In the assignment of shares in underground transactions, the assignor is always at a disadvantage because the price of the shares is lower that the true market value, ultimately damaging the interests of shareholders. Underground assignment creates many difficulties for State administration of laws regarding shares and reduces the transparency of corporate management. The reduced transparency gives a person interested in buying shares, including those inside or outside the company, inaccurate information regarding the true shareholders of the company or the specific person (or group) with the right to control the company.

Decreased transparency limits a person's ability to know clearly the true strategy, policy and future plans for the company's development.

Experience over past years has shown that the lack of transparency described above in corporate management has (intentionally or unintentionally) caused unclear administrative interference in the internal management of companies. This interference, as a result, will further complicate already complicated internal disputes.

123. The negative impacts (as discussed above) arising from the restriction on assignment of shares should be seriously considered. Since the first days of drafting the United Enterprise Law, there have been recommendations that the assignment of shares of foreign shareholders and State shareholders should be restricted when the scope of the EL is expanded to include foreign invested enterprises and enterprises with capital contributions by the State.

124. The issues mentioned above show that the rights of shareholders have not been fully provided for in the Enterprise Law. EL implementation has exposed many breaches of the basic rights of shareholders. The charter of many companies, including listed companies, states that any shareholder or a group of shareholders holding at lease one percent (or some absolute monetary value, such as VND50, 100 or 500 million) of the total shares may be entitled to attend General Meetings of Shareholders. The assignment of shares in a number of companies could not be performed because the Board of Management has refused to permit or to register the purchaser in the list of shareholders. The fact that the majority of shareholders are unable to access information about the company or may not access complete, accurate and truthful information is common and widespread. In addition, shareholders do not receive the required notices of decisions of the General Meeting of Shareholders, the summary of annual financial statements and even notices of payment of dividends. Shareholders have to come to the principal office of the company to receive dividends; forcing shareholders who live far from the principal office of the company to incur unnecessary expenses.

125. In addition to the infringements on the basic rights of shareholders, there are also cases where the rights of shareholders are taken advantage of. There are two common forms of such abuse. First, a number of minority shareholders disturb or obstruct the business of the General Meeting of Shareholders in ways unrelated to their rights of shareholders[40] in protest or disagreement. The second form of abuse relates to the State as shareholder. In many SOEs carrying out equitization, some related officials and State bodies are unable to distinguish between the shareholders rights and administrative management rights and interfere with administrative measures directly into the internal management of the company. Such interference may include not permitting the convening of a General Meeting of Shareholders, directing the convening of a General Meeting of Shareholders, replacing a member of the Board of Management or the Inspection Committee and so forth. The above-mentioned cases mainly occur in State-owned enterprises carrying out equitization[41].

126. Experience has shown that many shareholders (especially minority shareholders) and employee shareholders have not been aware of and understood their rights prescribed by the Law. First, they have not distinguished their rights as a shareholder from their rights as an employee. Therefore, the General Meeting of Shareholders in a number of shareholding companies, which have been converted from SOEs via equitization, is held as a general meeting of employees and officials. The habit of relying on the State is also still pervasive. Typically, when the Board of Management is in breach of the charter, or fails to

[40] Such as snatching the microphone rudel from chairperson, roughly taking the papers and documents of the chairperson, obstructing the chairperson from presiding over the General Meeting or disturbing the General Meeting from -inside and outside the conference room.

[41] Phan Thiet Hotel Shareholding Company, Ha Noi Photography Company, Huu Nghi Hotel Shareholding Company, Hai Phong Trading and Service Company are typical examples.

strictly perform its delegated functions, powers and duties, the shareholders do not exercise their right to replace the Board of Management; but instead, lodge a complaint with State administrative bodies requesting State interference. In addition, when there is evidence indicating that the company is in violation of the regulations on financial management, shareholders do not typically request the Inspection Committee of the company to investigate, but instead look to a State body for help. Poorly informed shareholders are taken advantage of and used to disturb corporate management, to divide shareholders causing internal disputes between them, to inhibit the business activities of company, and to discourage shareholders, specifically, the minority shareholders. As a result, persons who take advantage of these shareholders then buy shares at prices below true market values.

127. Unlike limited liability companies with two or more members, there is no provision permitting a shareholder or group of shareholders in a shareholding company to initiate a court action against a Board of Management member. From experience, the provision permitting a court action to be initiated for revocation of a decision of the Board of Management has been encouraging. In a number of companies[42], minority shareholders initiated legal actions requesting the court to revoke a resolution of the General Meeting of Shareholders: a number of unfair or illegal decisions have been revoked by the court[43].

128. At what price should shares be offered? Article 61 of the Enterprise Law provides that the price at which shares shall be offered must not be lower than the market value at the time of offering, except for in a number of cases[44]. It has been recommended[45] that, pursuant to the standard practice of issues of new shares in many countries, companies or underwriters carrying out underwriting of the issue of shares must sell shares at a discounted price in order to encourage investor participation. Therefore, provisions like Article 61 may prevent companies from issuing new shares.

129. In addition, the "market value" concept is relatively familiar and is regularly used, but there has been no common understanding of the nature and definition of market value[46]. Even if there is a common understanding, it is difficult to collect the information required to determine a market price in an underdeveloped market. Therefore, the implementation of such a provision is not simple.

130. Redemption of shares. The Enterprise Law distinguishes two cases of redemption of shares: redemption of shares upon demand by shareholders and redemption of shares pursuant to a resolution of the company. Article 64 of the Enterprise Law provides that a shareholder voting against a resolution of the General Meeting of Shareholders on the re-organization of the company or against a change to the rights and obligations of shareholders stipulated in the charter of the company, may demand the company to redeem its shares. The time-limit for making the demand shall be fifteen (15) days from the date on which the General Meeting of Shareholders passed the resolution. In this case and pursuant to this provision, the company is forced to redeem the shares of the shareholder at the market price or the price determined on the manner stipulated in the charter of the company. Where there is disagreement over the value of the share, the parties may request arbitration or legal adjudication.

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[42] From 1997 to 2003, there have been only three cases in which shareholders took court action against the Board of Management in South Korea.

[43] But in several cases, the judgment of the court has not been fair and did not revoke the unfair or illegal decision of the General Meeting of Shareholders.

[44] Initial offering of shares after business registration; shares offered to all shareholders in proportion to the respective numbers of shares they hold in the company; shares offered to brokers or underwriters (in this case, the difference shall be the commission for brokers or underwriters).

[45] Mekong Capital: "Viet Nam Private Sector Obstacle Status Report", October 2003.

[46] In economic terms, market value is defined as the price at a certain point of time accepted by both the purchaser and the seller based on the most complete information and without any coercion (the purchaser is not forced to purchase and the seller is not forced to sell). This concept has been used in relevant legal instruments of most countries throughout the world.

131. The intent of this provision is to protect the interests of minority shareholders in cases where a majority shareholder or a group of majority shareholders takes advantage of its controlling position to make decisions damaging the legitimate interests of the group of minority shareholders. In this case, the affected shareholders may withdraw from the company through the assignment of their shares to another person. Nevertheless, upon demand, the company must redeem their shares as provided in Article 64 (as mentioned above) because the market of Viet Nam, especially the share market, is underdeveloped, and the assignment of shares to other persons is not favourable or easy. Moreover, in urgent cases, the calculated value may fall short of the real market value.

132. Beside the provision on redemption of shares upon demand, the Enterprise Law also provides the conditions for redemption. In particular, a company may only redeem shares if, after the redemption, the company is still able to satisfy in full its debts and other property obligations. This provision ensures that redemptions will not adversely affect the interests of creditors and/or the company.

133. Since the implementation of the Enterprise Law four years ago, there has been no case in which a shareholder has demanded the redemption of his/her shares as stipulated in Article 64. Notwithstanding, implementation issues remain. Issues including, the determination of purchase prices, procedures and powers needed to resolve disputes regarding the valuation of redeemed shares as well as the failure of the company to redeem shares upon shareholder demand, have not been resolved fairly and effectively. Thus, this provision, in practice, has not been enforceable.

134. Critics of this provision argue that companies forced to redeem shares, as referred to in Article 64, may be forced to use all their cash on hand to redeem shares, leading to the possibility of bankruptcy. This situation also increases the risk to shareholders who did not vote against the re-organization of the company or against a change to the rights and obligations of shareholders stipulated in the charter of the company. Critics have also said that no country has provisions like Article 64, and have proposed the removal of Article 64.

135. Finally, the Enterprise Law has not yet anticipated and provided for cases in which a group of dissenting minority shareholders prevents the sale of the shareholding company to another person (the third party) by way of refusing to sell their shares to the purchaser. This situation will make the sale less attractive, and may even prevent the acquisition of the company damaging the interests of the majority of other shareholders. Article 65 of the Enterprise Law provides the right of a company to redeem shares sold with the following restrictions: (i) redeemed shares shall not exceed 30 percent of the total number of shares sold; (ii) the redemption of more than 10 percent of the total number of shares sold shall be decided by the General Meeting of Shareholders and the redemption of shares at a lower percentage shall be decided by the Board of Management; (iii) the price for redemption of ordinary shares shall be decided by the Board of Management but shall not be higher than the market price of ordinary shares at the time of redemption[47], and with respect to shares of other classes, the price for redemption shall not be lower than the market price; and (iv) the company may redeem shares of each shareholder in proportion to the number of shares each holds in the company.

136. This provision, on the one hand, facilitates a company's restructuring of sources of capital for business as well as the returning of equity to shareholders, especially in the case where the company is only allowed to pay dividends when its business earns profits. On the other hand, this provision prevents a majority shareholder from taking advantage of "redemption of shares" to withdraw capital of the company to use for their own benefit. In a context where the provisions of the Law have less effect, it is likely that the above objectives may not be fully achieved.

[47] Except for the redemption of shares of each shareholder in proportion to the number of shares each holds in the company.

137. The delegation of power to the Board of Management to decide on redemption of shares within the limit of ten (10) percent of the total number of shares sold creates a likely possibility of damage to the company, minority shareholders and creditors. This possibility may be especially high in Vietnam where members of the Board of Management almost all companies are, concurrently, also large shareholders. In cases where the company has difficulties or has reached "the maximal level" of development, large shareholders have inside information unavailable to the public and may act on this information to gradually withdraw their capital from the company through the redemption of shares by the company. The Board of Management may approve share redemption on several occasions, but any single redemption may not exceed 10 percent of the total amount of the total shares. It is likely that the limit provided for in Article 66[48] will not be strong enough to prevent the possibility of abuse.

138. As mentioned above, the provision that a company may redeem shares of each shareholder in proportion to the number of shares each holds in the company, by its nature, is a tool for the company to return part of the equity[49] to shareholders; while leaving the ownership and power structure of the company unchanged. However, this provision is only appropriate for and may only be implemented by small companies with a small number of shareholders and where all the shareholders know each other. With respect to large companies with many shareholders, especially listed companies, this provision is inappropriate and less effective. And in practice, this practice may be abused and would be unfair to shareholders. Some shareholders would have a chance to sell their shares, while other shareholders may not.

139. The register of shareholders may be considered an original document certifying and recording information on ownership of a company. Article 60 of the Enterprise Law lays out the basic items required in the register of shareholders. A person will be recognized as a shareholder of the company, and enjoy the statutory rights and interests, only when the statutorily required information on the shareholder of the company is included in the register of shareholders.

140. Unlike the register of members of limited liability companies, the register of shareholders is not registered with the business registration body. Therefore, changes in shareholders and assignment of shares need not be registered, but requisite information should be stated fully and accurately in the register of shareholders. The strength of this provision is the flexibility and reduction of cost in the establishment and maintenance of the register of shareholders, the assignment of shares and changes in shareholders.

141. Nevertheless, in practice, investors have had some concerns. A major concern is the uncertainty of legal ownership even after the purchase of shares. The person in charge of management may delay registration, intentionally make an incorrect registration or refuse to file the "registration of a shareholder". In such cases, the shareholder's rights and interests are seriously infringed. While the system for resolving disputes and dealing with breaches is weak, the above-mentioned concern is reasonable. As mentioned above, the Board of Management of a number of companies have refused to register assignments of shares and changes in shareholders. This practice has adversely impacted the business environment and has discouraged the development of capital contribution and the purchase of shares as a form of investment.

Internal Management Structure of Shareholding Companies

142. The internal management structure of shareholding companies, pursuant to the Enterprise Law, comprises a General Meeting of Shareholders, an Inspection Committee, a Board of Management and a Director (General Director). The General Meeting of Shareholders is a tool for shareholders to exercise their rights to manage the company and is the highest decision-making authority of a shareholding company.

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[48] A company may only pay for redeemed shares if, after such redeemed shares are paid for, the company is still able to satisfy, in full, its debts and other property obligations

[49] The literal translation is "owner's capital".

Subordinate to the General Meeting of Shareholders, the Board of Management has full authority to manage the company, except for issues that fall within the authority of the General Meeting of Shareholders. The Board of Management manages, directs and supervises the Director (General Director) in the management of the company's business activities. The inspection committee is a body of the General Meeting of Shareholders and is authorized to supervise the Board of Management in exercising the powers and performing the duties of the Board in general, and of each Board member in particular.

143. It can be said that the internal management structure of a shareholding company, pursuant to the EL, is somewhat different to both the "single board" mode in the common law, and the widely applied "dual-board" mode in a number of Europe countries, especially Germany.

144. As mentioned above, the Enterprise Law has provided for the rights of shareholders, as well as the mechanisms and tools for exercising such rights. Nevertheless, in large shareholding companies with State or foreign shareholders, the person directly exercising such rights is not a true shareholder, but instead, a representative. In some cases, the true shareholder directs the representative with effective and close supervision. In other cases, the authorized person acts with discretion without appropriate and effective supervision of the true shareholder. Therefore, the manner in which the authorized representative exercises ownership rights may not be an accurate reflection of the desires or intent of the true shareholder. The representative may not serve the interests of the shareholder, company and related persons.

145. Where the rights of shareholders are exercised by "an authorized person", the right to control and supervise may be exercised by "an sub-authorized person". In this situation, the possibility that authorized persons might abuse their powers for their own benefits is great, especially in Viet Nam where a market constitution has not been developed. The EL has not anticipated the above circumstances. This is a shortcoming that must be addressed before the EL is expanded to also cover enterprises with shareholders that include the State or foreign investors.

146. The Enterprise Law outlines the authority of the General Meeting of Shareholders, the method and procedures for convening a General Meeting of Shareholders, the right to attend meetings, conditions and procedures for conducting a meeting and the passing of resolutions by the General Meeting of Shareholders. In addition, the EL allows the General Meeting of Shareholders to pass a resolution by way of obtaining written opinions.

147. Article 71 provides that the Board of Management shall have the power to convene a General Meeting of Shareholders. Where the Board of Management fails to convene, the Inspection Committee or a group of shareholders shall have the right to request[50] the meeting. In general, this is a reasonable provision. But a number of practical, technical matters have arisen. First, the Board of Management of several companies has failed to convene annual General Meetings of Shareholders as stipulated. Is this failure by the Board of Management a serious breach of its rights and obligations? In this case, both shareholders and the Inspection Committee have failed to request the convening of a General Meeting of Shareholders. Second, there is no provision regarding the obligations and responsibilities of the Board of Management, the relation between the Board of Management and the Inspection Committee or the group of requesting shareholders in the case where the Board of Management fails to convene a General Meeting of Shareholders. The Board of Management manages the seal, register of shareholders, books of account and other equipment and instruments, and the staff of the company. Therefore, when the Board is not willing or is not forced to share its powers with the Inspection Committee or the group of requesting shareholders, the convening of a General Meeting of Shareholders as requested by the Inspection Committee or such group of shareholders is not likely to be successful.

[50] Clause 2 of Article 53 of the Enterprise Law.

148. Basically, Articles 72 and 73 have set out appropriate provisions on the preparation of the list of shareholders entitled to attend the General Meeting of Shareholders, as well as the program of the meeting. As stated above, a shortcoming, which limits the exercise of the rights of minority shareholders, is the lack of public announcement of the list of shareholders entitled to attend the General Meeting of Shareholders. The provisions of clause 4 of Article 72 are not fair. While majority shareholders may obtain the list, individual minority shareholders do not have such right. In addition, provisions dealing with cases where the Board of Management fails to correct wrong information in the list of shareholders as requested by a related shareholder (clause 5) are not available.

149. Similarly, provisions dealing with cases where the Board of Management refuses to include recommendations of the group of minority shareholders in the agenda of the General Meeting of Shareholders are also not available.

150. Articles 76 and 77 of the Enterprise Law provides for basic quorum requirements of a General Meeting of Shareholders. Similarly to the Members' Council of limited liability companies, quorum requirements are not stipulated, but are open with a minimum limit (i.e., the EL only provides the minimum limit, but a higher limit may be stipulated in the charter of the company). Its purpose is to create conditions for shareholders to mutually agree on quorums which are most suitable for their specific conditions and which satisfy best their rights and interests. However, in practice, very few groups of shareholders (perhaps none) have used this right for chance to agree on charter quorum requirements different than those in the EL.

151. In order for a Meeting of Shareholders to be valid, the shareholders in attendance must represent at least 51 percent of the voting shares. In addition, at least 51 percent approval of the total voting shares of all attending shareholders is the minimum condition for passing an ordinary resolution by the General Meeting of Shareholders. "Special" resolutions require approval by a number of shareholders representing at least 65 percent of the total voting shares of all attending shareholders. The minimum requirement of 65 percent approval of total voting shares for the passage of special resolutions is the lowest voting requirement of any country in this region[51]. This low voting requirement, with respect to special resolutions, has prevented and even rejected, the ability of minority shareholders to make important resolutions; notwithstanding the fact that special resolutions usually have a significant impact on the position and interests of minority shareholders.

152. In addition to the passing of resolutions by way of voting at a General Meeting of Shareholders, the General Meeting of Shareholders may also pass resolutions through obtaining written opinions.

This allows the General Meeting of Shareholders to pass resolutions even when a General Meeting Shareholders cannot be convened in a timely manner in order to satisfy a pressing business need, or where it is not advantageous to convene a General Meeting of Shareholders due to cost.

153. However, the Law does not provide any specific conditions or restrictions for passing decisions by way of obtaining written opinions; leaving the decision and discretion instead to the Board of Management. As a result, there have been abuses in the use of written opinions to avoid the convening of meetings. Some shareholding companies have not convened any General Meeting of Shareholders in three consecutive years. Instead, the Board of Management has obtained written opinions of shareholders to decide on issues and pass resolutions regarding increases in the charter capital, amendments to the company charter, approval of annual financial statements and so forth. Almost all the issues mentioned above require approval by a special resolution of the General Meeting of Shareholders. The requirement of 51

[51] 75% in Bangladesh, 66.6% in China, 75% in Hong Kong, 75% in India, 75% in Malaysia, 66.5% in Singapore; 66.6% in South Korea and 75% in Thailand.

percent of the total votes[52] for the passage of all decisions, regardless of type, by the Board of Management using written opinions, has created favourable conditions for the above mentioned abuses. The abuse, in essence, allows majority shareholders to lawfully evade the requirements of super-majority approval in passing special resolutions. This harms minority shareholders, even when they hold up to 49 percent of the total shares.

154. The Enterprise Law requires the notification of all resolutions passed by the General Meeting of Shareholders to all shareholders entitled to attend meetings. In other words, only shareholders holding ordinary shares and shareholders holding voting preferred shares may receive information on General Meetings of Shareholders. In addition, the minutes of each General Meeting of Shareholders must be approved prior to the closing of each meeting. A criticism of this provision is that shareholders absent from the meeting are neither able to receive information regarding the meeting nor receive the agenda of the meeting. This is one of shortcomings related to the right of shareholders to be provided with or have access to information of the company.

155. Pursuant to the relevant provisions, resolutions of the General Meeting of Shareholders are automatically effective at the time of adoption. But in practice, some technical problems have arisen. The point in time when a resolution is passed occurs before the closing of the meeting. In some cases, General Meeting members had passed all or a number of items on the agenda, but dissolved prior to the closing of the meeting (i.e. there has been no closing ceremony). Some have argued that in such cases, the resolutions of the meeting have not become effective. In other cases, the resolutions passed by the General Meeting of Shareholders, especially resolutions to change members of the Board of Management, may not be performed because the member(s) of the Board to be replaced failed to hand over their office to the new Board member(s)[53]. This is another matter that should be considered when contemplating the Vietnamese situation.

156. The Enterprise Law (Article 79) grants to the courts the power to cancel a resolution of the General Meeting of Shareholders in two cases. First, when the procedures for convening the General Meeting of Shareholders do not comply with the EL and the charter of the company. Second, the content of the resolution breaches the Law or the charter of the company. Shareholders, members of the Board of Management, the Director and the Inspection Committee have the right to demand that a court consider and cancel a resolution of the General Meeting of Shareholders, where necessary. The time limit for this right is 90 days from the date on which the General Meeting of Shareholders passes the resolution.

157. This provision is necessary for granting shareholders, members of the Board of Management and the Inspection Committee more opportunities and tools to supervise the activities of the General Meeting of Shareholders, especially activities of majority shareholders, in order to prevent the abuse of powers. At the same time, the above provision aids in preventing minority shareholders from taking advantage of their powers by harassing operations of the company. But in practice, the implementation of this provision in past years has not achieved the desired result. Courts in some localities are still unprofessional, passive and non-objective in the resolution of demands referred to in Article 79 of the Enterprise Law. It is also not yet clear whether or not a decision by the General Meeting of Shareholders against which a complaint is lodged can be considered to be in effect before the complaint has been resolved[54]. There has been no

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[52] The Corporate Law of Singapore provides that a special decision shall be approved in writing by at least seventy five (75) percent of total voting shares.

[53] Experience has shown that the Board of Management may not conduct normal operations without a seal, which has to be handed over. Without this seal, all transactions of the company may be deemed void.

[54] In some cases when a complaint is made, the relevant resolution has not yet been performed.

provision addressing the consequences arising from the judgement of the court, especially in cases where the court decides on cancellation of the relevant resolution of the General Meeting of Shareholders.

Boards of Management

158. The Board of Management is defined as "the body managing the company" and "shall have full authority to deal with all issues in the name of the company, except for issues which fall within the authority of the General Meeting of Shareholders". The rights and duties of the Board of Management[55], provided for in clause 2 of Article 80, are generally sufficient. However, in practice, it seems that a Board of Management, in general, and each of members, in particular, has not used the provisions on statutory functions, duties and powers as the basis for their actions. If this is true, the relevant provisions of the EL have not conformed to the practice and are not enforceable.

159. Compared to the duties of a board of management specified in Rules on Best Management Principles of the OECD (according to official OECD practice), the role, functions and duties of the Board of Management provided for in the EL are different. First, the role of the Board of Management provided for in the EL tends toward direct management, while the role of boards of management in official OECD practice favors supervision and guidance for the development and management of companies. The provisions on the powers and duties of the Board of Management are relatively specific, while the relevant provisions in official OECD practice are general and qualitative. For example, in regards to investment, the Board of Management, as provided for in the EL, directly makes decisions on investment plans. Boards of management, as provided for in official OECD practice, only supervise the main costs of investment, purchases and sales of main investments. The role and functions of the board of managements in official OECD practice focus mainly on objectives, systems and the consistency of companies as good business entities. This includes setting objectives for the development of a company and supervising the realization of such objectives. In addition, according to official OECD practice, boards focus on supervising and controlling potential conflicts of interest within the management, board of management and shareholders, including the potential danger of misusing assets of a company and abusing their authority in transactions for personal gain. These boards also ensure the uniformity of the accounting system and financial statements of a company, ensure that the requisite internal auditing systems operate effectively, especially the risk control system, ensures the inspection of the financial system as well as inspection of business activities, ensures that operations of a company comply with the laws and other social rules, etc. These items are not included in the provisions of the Enterprise Law with regard to the duties of the Boards of Management.

160. The Board of Management shall have no more than 11 members. Due to the structure of "separate dual-board", all members of the Board of Management take part in management. There are no independent members as in the case of shareholding companies in countries in which apply common law.

161. Term of office, qualifications and specific number of members will be stipulated in the charter of the company. This provision creates discretion for investors to make decisions in compliance with their situation and specific conditions. Reality has shown that domestic private investors are at various levels of education, professions and have different ages, and are, especially large shareholders, all members of the Board of Management. Therefore, the fact that the EL has yet not provided qualifications of members of the Board of Management is not surprising considering the EL only applies to domestic private enterprises.

[55] There is an opinion that the powers of the Board of Management provided by the Enterprise Law are too limited and insufficient for the Board of Management to make decisions at its discretion to best serve the interests of the Company;

162. This provision may not be appropriate in cases where members of the Board of Management are "authorized persons" (and may be they are the persons sub-authorized by the authorized persons). In these cases, requisite qualifications must be provided for selected members of the Board of Management to perform their rights and duties; for supervision and prevention of the possibility that the group of authorized persons takes advance of their powers to act for their own benefits (persons exercising the rights of shareholders also are the authorized persons).

163. The Enterprise Law does not provide a rotation regime for the replacement of members of the Board of Management in order to ensure the continuity and stability of the Board. If a rotation regime was used, it would limit circumstances in which all members of the Board of Management could be replace at one time, and may exclude cases in which the Board of Management is removed because it disobeys orders of the General Meeting of Shareholders which leads to uncertainty and flip-flopping in the normal business activities of the company.

164. Clause 3 of Article 81 provides that where the Chairman of the Board of Management is absent or has lost the capacity to perform his or her delegated duties, a member authorized by the Chairman of the Board of Management shall exercise the rights and perform the duties of the Chairman of the Board of Management. And where no one is authorized, the remaining members shall select one member to hold temporarily the position of the Chairman of the Board of Management. In regards to its contents, this provision is well-organized and reasonable. But the provision has not anticipated all potential procedural problems[56]. The Chairman of the Board of Management is usually the legal representative of the company; and any change of the legal representative of the company must be registered in order for the change to be effective. In this case, the person temporarily replacing the Chairman of the Board of Management may be unable to perform a number of his or her duties if the enterprise lacks a legal representative.

165. The Chairman of the Board of Management is delegated with the power to convene meetings of the Board of Management (and is the sole person with this power). The procedures for convening and conducting meetings are stipulated by the charter of the company. Experience has shown that the charters of most shareholding companies do not provide procedures for convening meetings. Due to this fact, some companies could not replace the Chairman of the Board of Management (especially in the case where the Chairman concurrently is the legal representative) because the Chairman had delayed or refused to convene a meeting of the Board of Management even upon the demand of other members of the Board of Management. The absence of specific provisions on procedures for convening meetings of the Board of Management has created more opportunities for the Chairman to exclude members who disagree with him from participating in the making of resolutions by the Board of Management. These excluded members are therefore unable to perform their statutory rights, obligations and duties. This will certainly have a negative effect on the development of the company.

166. Clause 1 of Article 84 provides for two cases in which a member of the Board of Management shall be removed[57]; other cases are stipulated in the charter of the company. In practice, no company charters have provided for other cases and have only stipulated the same two cases described in the EL. As a result, Board of Management members are only replaced upon expiration of their terms, and such replacement is not based on their capacity, efficiency or performance of their duties. Clearly, this structure has not created enough pressure on the members of the Board to operate at optimal efficiency and to fully perform their obligations and duties.This shortcoming has no negative affect in cases where a member

[56] For example, where the chairman of the Board of Management is concurrently the legal representative of the enterprise and is replaced with another person, this change must be registered with the business registration body. To complete the filing, the chairman of the Board of Management who is replaced must sign the application for change of the legal representative. But if he or she refuses to sign the application, the change in the legal representative of the enterprise may not be registered and does not become effective.

[57] Loss or restriction of capacity for civil acts or resignation.

of the Board of Management is concurrently a shareholder. However, the situation would change if the EL is expanded to cover enterprises with shareholding or capital contributions by the State and/or foreign parties. Proposed amendments to the EL should create pressures and institutions encouraging the replacement of a member of the Board of Management at any time if he or she fails to exercise his or her delegated rights and duties, or fails to perform properly their statutory obligations and duties[58].

Inspection Committees

167. As mentioned above, the Inspection Committee of shareholding companies pursuant to the Enterprise Law is designed to be a body in the management structure of the company. Regarding legal status, the Inspection Committee is a body of the General Meeting of Shareholders and is authorized by shareholders to supervise and evaluate the operation of the Board of Management. Nevertheless, the EL has not specified the legal status of the Inspection Committee of shareholding companies. The nature and position of the Inspection Committee provided for in the EL are fundamentally different from the supervision committee of shareholding companies in Germany.

168. Clause 1 of Article 88 provides that shareholding companies of more than 11 shareholders must have an Inspection Committee. This provision is based on the assumption of small shareholding companies with few shareholders where there is no distinction between a manager and the owner. Shareholders are concurrently members of the Board of Management. Where the number of shareholders does not exceed 11 persons, all shareholders may concurrently be members of the Board of Management[59]. In this case, an Inspection Committee is not necessary.

169. This assumption will no longer be accurate when the Enterprise Law is expanded to include enterprises with State and/or foreign party shareholders. In this situation, the rights of shareholders, in many cases, will be exercised by an authorized person and not by the true shareholders. In addition, corporate management may be separated from ownership. The above structure will require not only internal control by an Inspection Committee but also objective supervision from outside bodies.

The activities of the Inspection Committee need to be researched and analyzed for appropriate planning

170. Article 89 is a provision regarding the procuring of information by Inspection Committees. This provision is a great development that facilitates the Inspection Committee's ability to conduct more effectively and practically its activities. However, the mechanism of providing information remains passive, i.e., information will only be provided to the Inspection Committee upon request by the Committee, and is limited to the requested information. Due to the high volume of information, the Inspection Committee is unable to regularly monitor and supervise activities of the manager and may not discover potential problems in time. Therefore, the Committee may not be able to prevent a manager from abusing his or her powers. A provision regarding the mechanism by which the Inspection Committee may obtain information should be considered when amendments and additions are made to the Enterprise Law. This mechanism should be minimal, equal to the mechanisms used to provide information to the Board of Management.

171. Article 90 specifies who may not serve on an Inspection Committee, but does not specify qualifications for its members. The job of the Inspection Committee is primarily professional in character. Therefore, they should be highly qualified in management, especially financial management.

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[58] Corporate lws of other countries permits shareholders to remove any member of the board of management at any time without declaration of any reason.

[59] Clause 4 of Article 80 of the Enterprise Law provides that the Board of Management shall have no more than eleven (11) members.

172. Experience has shown that the actual role of the Inspection Committee is weaker than its role as stipulated by law. Commonly, the Inspection Committee is ruled by the Board of Management. Members of the Board are also major shareholders who choose and vote for members of the Inspection Committee, and define the duties, positions, salary and other income for Committee members. Members of the Inspection Committee are usually not sufficiently qualified and may not have the enthusiasm to fight for fairness, justice and reasonableness. In such a position, it is difficult for members of the Inspection Committee to better perform their duties.

Director (General Director)

173. According to Vietnamese thought, a Director has full power in managing the day-to-day operation of a company. A Deputy Director acts as the assistant to the Director and is in charge of certain areas of the business. Therefore, their role considered subordinate and dependent. In addition, the latter does not have any decision-making power and is not assumed to have any specific obligations.

174. The Enterprise Law anticipates a new mechanism, in which the top managing person is the General Director, followed by several specialized Directors. This structure emphasizes the authority, rights, responsibility, and independence of each manager in his specialized area of operation (such as production manager, marketing manager, financial manager).

Salary for the Manager and Inspection Committee

175. The new EL grants the Board of Management, Inspection Committee, and the Director (General Director)[60] authority to decide on salaries and allowances for all company employees. It currently does not provide the principles by which salary and other benefits are calculated. Neither does it require salary and other income to be disclosed. Disclosure of the methods used to determine salaries and managers' annual income is, however, a key component of enterprise management best practices. A specific regulation stipulating the methods for determining salary and other benefits for managers will encourage development of managers' talents, initiatives, and devotion to the company. Together with salary and annual income disclosure, disclosure of methods used in salary determination is an effective tool to monitor management activities and to discourage potential abuses of power for personal benefit. This disclosure is necessary as management is separated from ownership of the company and salary becomes the essential motivation for their behavior. These provisions should be added to the Enterprise Law and should apply to enterprises with State owned capital contribution and State shareholding, and foreign invested enterprises.

176. Currently in Viet Nam, however, disclosure is not easy to do. Unlike other countries, especially developed countries, companies in Viet Nam cannot conform to the law while maintaining and developing normal business activities. Companies usually have to bribe and collude with pertinent State officials, and create two, even three types of documents and books for accounting. Turnover, cost, and profit are commonly reported inaccurately. Under these circumstances, disclosures of methods to determine salary and income for the manager may not reflect the truth.

177. The psychological effect that income disclosure has on people is considerable. In general, the common Vietnamese attitude is hide rather than to show off wealth. Psychology of envying others with higher incomes seems to exist. Even in State organizations, an administrative official may not be willing to accept a lower income than a Director or a member of the Board of Management. This can be clearly seen in the reform of salaries and in the current payroll of officials, State employees and employees in State-owned sectors. In addition, a Director of a big State-owned enterprise would not accept a salary

[60] Salary and allowance of the members of the Boad of Management and Inspection Committee are decided by the General Meeting of Shareholders; salary of the Director (General Director) is decided by the Board of Management

lower than a Director of an enterprise of a smaller size, even though its efficiency may be higher. Directors and members of the Board of Management of State-owned companies always want to compare their positions with administrative ranks in the government such as Directors of Departments or Deputy Directors of ministries, etc. In conclusion, the methodology of matching rank and income is most important in State-owned organizations.

178. In general, issues relating to transactions with related persons (Article 87) are similar to the case of limited liability companies (see Article 104 and 105 of this Report).

179. In general, the Enterprise Law does not require companies to e audited, not even shareholding companies. This regulation originated from an earlier circumstance when most companies in the domestic private sector were small, and there was no separation between ownership and management. The number of auditors in Viet Nam is small and their skills are of low standard. It should be noted that in the initial stages of development, a company adopts a cautious and anxious psychology.

180. Circumstances have changed since the early days of the domestic private sector. Currently, there are more and more requests for companies to be open and explicit about their management practices. The harm of informal and unclear management is becoming increasingly apparent. These issues should be resolved before the Enterprise Law is applied to all enterprises with capital contribution from the State and from foreign investors.

V. PARTNERSHIPS

181. The stipulation of a partnership company in the Enterprise Law is an improvement over previous laws. It increases the diversity in the types of enterprises in Viet Nam and offers investors yet another suitable business organization. However, partnerships have proven a less popular and less favorable form of enterprise in Viet Nam[61]. There are some reasons for this. Investors are aware of partnerships, but not yet comfortable the concept. The material, psychological, and cultural benefits for the Vietnamese still do not outweigh the disadvantages of partnerships. Moreover, the laws on partnerships are still incomplete.

182. The EL consists of only four articles[62] on partnerships. Therefore, it is not surprising that the coverage on partnerships lacks completeness and accuracy. The majority of the content was guided and specified by Decree 03/2000/ND-CP, dated 03 February 2000, which provides guidelines for the implementation of a number of articles in the Enterprise Law.

183. The Enterprise Law does not distinguish between different forms of partnerships. In other countries, there are two types of partnerships: general partnership and limited partnership[63]. Article 95 of the EL provides a definition of partnerships that includes two forms: general and limited partnership. In terms of partnerships, the EL has defined partnerships, distinguished between two types of partners (unlimited liability partner and limited liability partner) and has stipulated their respective rights and obligations.

184. Decree 03/2000/ND-CP, dated 3 February 2000, provides guidelines for the implementation of a number of articles of the EL and adds some details regarding partnerships. In particular:

- Article 10 (4) provides for basic contents of the charter of a partnership;
- Article 11 (4) provides a list of unlimited liability partners;

[61] There are fewer than 15 partnerships registered nation-wide.

[62] Articles from 95 to 98.

[63] Another translation is “registered partnership” and “unregistered partnership”.

- Article 26 makes a distinction between two types of partnerships: general partnership and limited partnership;
- Article 27 specifies five rights and eight obligations of unlimited liability partners;
- Article 28 specifies four rights and three obligations of limited liability partners;
- Article 29 provides for organization of management of partnerships;
- Article 30 provides for admission of partners;
- Article 31 provides for termination of status of partner; and
- Article 32 provides for withdrawal of partnerships.

Review of the related articles in the EL and the above Decree providing the guidelines on implementation reveals that:

- The nature of partnerships has not been fully researched and understood both in theory and practice, especially regarding legal liability, relationships, and methods of management and administration of the company;
- A method of capital contribution by provision of service is not stated;
- The structure of the capital and assets of a partnership, separated from the personal assets of the partners has not been provided for;
- The relationships among partners, between partners and the company and between partners and a third party are not discussed;
- In the above relationships, rights and liability of each type of partners and their joint liability relating to the duties are not specified completely and in detail;
- The internal regimes of decision making, managing, communicating and reporting are barely described;
- A conversion and a merge of partnerships are not provided for; and
- Cases of dissolution of partnerships as well as rights and obligations of partners after dissolution are not stipulated.

185. Critics argue that a weakness of the Enterprise Law is that it does not require certain lines of businesses to be formed in partnerships. According to this criticism, some provision of services such as health care, auditing, legal services, architecture design and advisory should be conducted in the form of partnerships. Whereas Decree 03/2000/ND-CP requires partners of a partnership to have professional qualifications corresponding to their line of business, this requirement may not be necessary for many types of businesses.

186. In many countries, laws require certain service sector businesses to be conducted in partnerships. However, as the investment environment becomes less restricted and more dynamic leading to a higher level of risk, the tendency of reform in nearly all countries is to facilitate investments and to minimize risk for investors. Therefore, in other countries, there is a tendency to remove provisions requiring the establishment of partnerships certain service businesses as mentioned above. In lieu of this requirement, professional indemnity insurance is applied.

187. This issue has been discussed and decided (as seen in the EL) in favor of the reform tendency discussed above. However, it is real world experience, not the above reason, which led to the decision to eliminate regulations requiring the formation of partnerships for certain business sectors. Until 2000, almost all service sectors - which, by tradition, would be operated in partnerships - have been provided for by State-owned or FDI enterprises. These enterprises are limited liability companies under Vietnamese Law. The issue is, if a law is passed that requires certain types of services to be carried out in partnerships, shall the

relevant limited liability companies be converted to partnerships? A positive response would mean that all State-owned enterprises would be converted. However, the issues related to the conversion have not been researched or resolved. Moreover, there has been no research to estimate the advantages and disadvantages of having the above services provided by companies that are not partnerships. Thus, there is no convincing basis for a regulation that requires certain types of services be provided in partnerships as seen in other countries.

188. Until now, there have been fewer than ten enterprises registered as partnerships; comprising an insignificant proportion of the total number of registered enterprises in Viet Nam. Partnership is an unpopular form of enterprise in Viet Nam. This may be caused by incomplete and proper regulations as stated above, the unique characteristics and psychology of Vietnamese businessmen, or the lack of awareness of this business form.

VI. SOLE PROPRIETORSHIPS

189. Sole proprietorship is a form of business that is considerably simple and a favorite form of enterprise in Viet Nam. Up to now, sole proprietorships have been in good compliance with the Enterprise Law. Problems that arise are often minor. However, there are some issues that may need to be addressed.

190. A sole proprietorship is owned by one individual who establishes, manages, and is personally liable for all debts and other obligations of the enterprise. In terms of liability, the enterprise and the owner of property are one entity. The EL itself does not limit the number of sole proprietorships that can be owned by one person. In the course of operating their sole proprietorship many persons have applied, for a number of reasons, to establish additional sole proprietorships. In some cases, disputes have arisen between the applicant and the official of the registry office. As a result, Decree 125/2004/ND-CP, dated 19 May 2004, specifies that one person is entitled to own only one sole proprietorship.

191. Legally speaking, a household business is identical to a sole proprietorship. The Enterprise Law, however, supposes that sole proprietorships are larger than household businesses. In reality, though, many household enterprises are much larger than supposed by the EL; and the respective regulations of the EL are not really effective in encouraging or compelling larger household businesses to register as one of the main four enterprise types under the EL. In reality, household businesses may enjoy some tax advantages over enterprises. In addition, unlike an enterprise, a household business is not required to retain accounting records, but it can pay taxes in compliance with the accounting regime. A practice survey has shown that even authorities in certain districts are not interested in having household businesses re-register as enterprises under the EL because these business would no longer be under their control [64]

192. Article 108 provides for the sale of sole proprietorships. The sale of a sole proprietorship is effectively the sale of its assets, including all the tangible assets used for the business, the intangible assets and all related rights. However, this article does not contain provisions or references to provisions relating to the sale of assets. Therefore, in practice, some owners of sole proprietorships have found it difficult to sell their enterprises to other parties. Instead, they often choose to dissolve the enterprise and then sell the assets. This practice does not ensure the continuity of the enterprise's business activity causing difficulties for both the vendor and buyer.

193. While there are provisions on the sale of a sole proprietorship, no provisions exist regarding the transfer, donation or inheritance of a sole proprietorship. Therefore, a transfer, donation or inheritance of a sole

[64] According to the law on taxation, individual business households are controlled by the division of General Department of Taxation, whereas enterprises are controlled by the General Department of Taxation.

proprietorship must also be conducted in such a way that does not ensure continuity of the enterprise. This often means owners cannot do what they want to do.

VII. RE-ORGANIZATION OF ENTERPRISES

194. The Enterprise Law provides five methods of enterprise re-organization: division, separation, consolidation, merger and conversion of enterprises. These are popular forms of re-organizations that are provided for in corporate laws of most of other countries. The provisions relating to the above-mentioned forms of re-organization are based on the relevant basic principles of the 1995 Civil Code.

195. With regard to the re-organization of enterprises, a number of other forms of re-organization are not available. First, the implementation of EL over the past four years has shown the need for smooth conversion from a sole proprietorship into a limited liability company or shareholding company. Nevertheless, because neither a prohibition nor a relevant provision is provided for in the EL, owners of sole proprietorships have dealt with the matter through a roundabout way, i.e., dissolving the sole proprietorship and using the assets to establish a new limited liability company. The strength of this method is the protection of creditors' interests, allowing for safe and reliable collection of taxes for the State. However, this method causes many disadvantages to the owner. The costs of conversion are high. In addition, advantages gained from the sole proprietorship, as well as previously created business relations for the now dissolved enterprise may not be easily transferred by this method. In addition, the acquisition of companies, which is a popular form of re-organization in other countries, has not been referenced and provided for in the EL.

196. The general procedures for the respective forms of re-organization of enterprises have also been provided for in the Enterprise Law (in Articles 105 to 110). Nevertheless, such procedures are generally sparse and determined based on the logic, rather than practical knowledge and actual experience of relevant matters. Upon re-organization of an enterprise, the interests of minority shareholders, creditors and employees should be taken into consideration and protected. But in comparison with other countries, measures for protecting creditors and employees are very sparse. For example, creditors are only notified of the owner's decisions regarding re-organization: provisions specifying how far in advance notice should be delivered do not exist. In addition, creditors have no tools or opportunities to request payment prior to re-organization.

197. Experience over the past five years has shown that most enterprises have not carried out re-organization in the form of division, consolidation or merger[65]. Instead, re-organization in the form of separation is applied more generally and regularly. It is likely that other forms of re-organization will not be well-received in Viet Nam. In addition, the conversion of enterprises from a limited liability company to a shareholding company has been carried out in a number of cases.

198. The survey of the implementation has shown that in cases of separation of an enterprise, the separations did not comply with the provisions of the Enterprise Law. Causes of a separation are usually internal disputes between members, members wishing to leave to have their own company, or division of business activities due to personal reasons or State preferential policy. There was a company with five members, but four members gradually withdrew from the original company and each member established their own company. Upon withdrawal from the company, part of assets of the original company was distributed among the members and such assets were used to establish a new company. The result was that after approximately seven years of operation, one company has separated into five different companies. But only the name of the original company remains unchanged.

[65] Merger by way of administrative measure is usually applied to State-owned enterprises. Enterprises that are suffering losses, are bearing debt burden and have laid-off employees will be restructured or re-organized through merger into an more effectively run an successful enterprise.

199. In practice, the separation of enterprises is not carried out in accordance with provisions of the EL. In other words, the provisions on procedures for separation of enterprises may not cover all practical requirements and actual developments. Separation of enterprises, in many cases, is carried out spontaneously, and not based on carefully considered and purposeful decisions. In addition, separation of an enterprise is often conducted by establishing a new enterprise that does not relate to the existing enterprise.

200. The separation of enterprises in any form is a re-organization. Separation facilitates expansion in the scale of the business and diversification of business activities, attracts more capital and other resources and leads to a more effective use of resources for business activities.

201. It can be said that the separation of enterprises always affects the interests of creditors. In the above-mentioned cases of separation of enterprises in Viet Nam, the interests of creditors, in theory, have not been protected, at least not by laws. But if measures protecting the interests of creditors are too strong, the separation of enterprises will not occur; or upon separation, the business capacity of the related enterprise will be seriously damaged making it impossible to maintain and develop the business. For example, due to various reasons, a member wishes to withdraw from an existing company in order to establish his or her own company. Before the withdrawal from the company and partial distribution of assets, creditors are notified of the matter. As a result, some creditors request the payment of debts prior to the due date. Obviously, such a situation affects the financial ability of the existing company, as well as the assets to be distributed to the member withdrawing from the company. Ultimately, the creditor may negatively impact the establishment of the new company by the former member. This case is similar to the case where an owner uses part of the assets contributed to the original business to establish a new limited liability company.

202. As mentioned above, acquisition is a form of re-structuring enterprises that has not been provided for in the Enterprise Law. It is likely that the acquisition of enterprises is a form of restructuring which is usually applied to shareholding companies in preference to other forms of enterprises. In general, experts believe that the acquisition of companies should be provided for in the corporate law of transitional countries, and the provisions should be accurate, specific, and closely monitored. For example, a percentage requirement for controlling shares should be specified (30 percent of the total shares or other specific percentage). Even in cases where this percentage is held by a group of related shareholders, the acquisition should be applied only to shareholding companies with a large number of shareholders[66]. In addition, the law should provide the minimum purchase price to be offered, the time period for an offer to purchase, and other conditions needed by a controlling shareholder to offer to purchase the shares of other shareholders.

203. The acquisition of an enterprise is, by nature, a change in the controlling shareholder of the company. Once the right to control the company is transferred to another shareholder, the opportunity for minority shareholders to sell their shares at a reasonable price will no longer exist. The price of shares at such a time will not depend on the actual efficiency and value of the company, but will depend, instead, on events that do not relate to performance or potential growth of the company. In such cases, laws of other countries provide for tools to protect the interests of minority shareholders, while at the same time creating conditions for completion of the acquisition. To protect minority shareholders, the laws of other countries usually provide that when any shareholder holds a controlling share in a shareholding company, such shareholder must make an offer to purchase the remaining shares at a fair price. This tool creates an opportunity for other shareholders to decide whether or not to stay in the company with the new controlling shareholder. The offered minimum purchase price must be equal to the price of shares at which the shareholder or group of shareholder had purchased shares for the acquisition of the company. The minimum

[66] Common principles of the corporate law of transitional countries are prepared with the assistance of OECD.

period for this offer to purchase will be 6 months from the date when the rights of the new controlling shareholder become effective. At the same time, the law should provide specific and strict penalties for violations in the requirements for the purchase of shares as mentioned above.

204. The law should also require advance notification to shareholders of a planned acquisition of the company. This allows managers time to look for purchasers who may offer a higher purchase price than the investors seeking to acquire the company. In the case where the manager purchases, it is also important for the company and for other shareholders that other potential buyers also have an opportunity to offer a higher price. In addition, the law should specify actions that manager is prohibited from taking in order to prevent the acquisition of the company or change in the controlling shareholder.

Dissolution of enterprises

205. The Enterprise Law provides for four cases of dissolution of enterprises, of which two cases are compulsory dissolution, namely where an enterprise has its business registration certificate revoked and where the company does not have the minimum number of members stipulated in the EL for a period of six consecutive months. In addition, the EL provides the procedures for dissolution. The dissolution of an enterprise will be carried out by the enterprise itself under the supervision of the business registration body.

206. Experience over the past five years has shown that the number of enterprises dissolved in accordance with the procedures provided for by the EL have been few, and far lower than the number of enterprises that were actually dissolved. The summary of the implementation of the EL in the past four years has indicated that the number of enterprises that no longer conduct operations (i.e., were actually dissolved) accounts for 20 to 35 percent of the total registered enterprises (approximately 16,000 to 35,000 enterprises). In contrast, the number of dissolved enterprises actually registered with the business registration body is only in the thousands. Some believe that the above-mentioned situation has made the business environment worse off and unhealthy.

207. The above situation resulted from many causes. The actual survey demonstrated that the main cause is the complicated, costly and unreasonable legal procedures. These procedures are complicated and costly because the provisions heavily emphasize the protection of the interests of creditors and employees. There is so much concern over the protection of these interests that even the business registration body hesitates and is reluctant to declare the dissolution of enterprises. In addition, dissolution is discouraged because dissolution and removal of a company from the business register may erase any outstanding taxes owed by the enterprise to the State. In this way, some individuals may take advantage of dissolution in order to evade taxes.

208. Issues relating dissolution procedures should be further examined. Because a majority of enterprises in Viet Nam are of small scale and under family ownership, informality and other nonlegal principles of conduct (blood relationship, relationship between relatives or friends and so on) are common and regulate the internal management relations of companies.Therefore, even on decisions regarding investment, assignment of management duties of the company, distribution of benefits, etc., the informal nature of management imply that the requirement that the decision for dissolution be made in writing and comply with Clause 1 of Article 112 is not suitable in practice[67]. In this structure of informal relationships, nearly all the employees working in small or medium enterprises are relatives and friends. Therefore, the dissolution of an enterprise may be considered not only a business loss; but, more importantly, a personal loss

[67] The decision for dissolution should contains: name of enterprise, reasons for dissolution, schedule and procedure for liquidation, options for dealing with liabilities rendered from employment contracts, establishment of the committee for asset management with regard to rights and obligations defined in the enclosed appendixes.

damaging to a family and to blood lineage, and not an option or obligation the owner should have to consider or deal with.

209. The requirement that decisions to dissolve an enterprise be published in newspapers and notices sent to all creditors is intended to protect creditors. But the above requirement causes some unreasonable outcomes and may not be necessary in all cases. First, as mentioned above, the dissolution of an enterprise, in most cases, is done by "giving quietly up" and not carried out with a decision in writing. As a result, notices of dissolution are not published in newspapers and no notice is sent to creditors as stipulated by law. Second, most small or medium enterprises raise capital from friends, family members and other relatives[68]. Therefore, all the investors become aware of the dissolution of the company through informal communication without the need for official notification as stipulated. Third, publication in newspapers is costly, requiring millions of VND. Fourth, the survey of companies has shown that all the owners of enterprises would regard dissolution of their company as a major failure and would be ashamed and not want others to know of this failure. Therefore, owners hesitate to publish the dissolution of their enterprise in newspapers.

210. In brief, the procedures for dissolution of enterprises are too complicated, costly and unreasonable, especially in regards to small and medium enterprises. In practice, these provisions have not achieved their objectives, and not only are not enforceable, but also cause unnecessary expenses for both State bodies and related owners of enterprises.

VII. STATE ADMINISTRATION, REWARDS AND DEALING WITH BREACHES

211. State administration is one of the items always included in economic laws promulgated during the transitional period, and the Enterprise Law is no exception. Chapter XIII "State Administration of Enterprises" is comprised of four articles regarding the contents of State administration of enterprises (Article 114), bodies in charge of State administration of enterprises (Article 115), powers and responsibilities of business registration bodies (Article 116), inspection of business operations of enterprises (Article 117), and the fiscal year and financial statements of enterprises (Article 118).

212. The language of the Charter on State administration of enterprises is simple, incomplete and one-sided. First, the content of State administration emphasize administrative and executive functions of the State, and does not address judicial functions. This bias is expressed clearly in Article 115 of the Law where the legislative and judicial bodies are not stipulated as "bodies in charge of State administration of enterprises". As a result, it can be interpreted that hearings and the resolution of disputes between shareholders and a company by courts, a judicial function, does not fall under State administration. However, the investigation on the legality of General Meeting of Shareholders resolutions of shareholding companies by State inspectors of localities is regarded as State administration of enterprises. As regards promulgation and implementation of laws, there are not only the direct regulations on enterprises (referred to in clause 1 of Article 114), but also the greater system of regulations governing the operations of enterprises (in effect, the entire national legal framework).

213. State administration of enterprises do not yet refer clearly to implementation and inspection of implementation of business conditions – a central duty of State administration. As a result, related State bodies have encountered substantial confusion, which has even led many in the Government to the inappropriate conclusion that the Enterprise Law itself is to blame for less effective State administration.

[68] The 2003 survey of the Ministry of Labor, War Invalids and Social Affairs indicates that loans are only equal to 8% of the capital of owners of small and medium enterprises, and approximately half of all small and medium enterprises acquire loans for their business (Saigon Times, issue no.31-2004 on 29 July 2004).

214. Although business registration bodies are focal bodies for State administration of enterprises, there has been no clear, specific and systematic direction in terms of their position, legal status, and organizational structure relative to other bodies responsible for State administration. Moreover, there is no single coordinating business registration body at the central level. Therefore, during implementation of the EL, many debates and discussions about a series of issues were left unresolved, proposed solutions have not been consistent and definitive are often incomplete and compromised.

215. Article 117 on inspection of business operations of enterprises may not be necessary because there is a separate system of regulations on inspection, including one decree and various other legal instruments regarding the inspection of enterprise operations.

216. The monitoring of financial statements is one duty of State administration. Article 118 requires that annual financial statements of enterprises must be sent to the competent tax office and the business registration body within 30 days, in the case of private enterprises and partnerships, and 90 days, in the case of limited liability companies and shareholding companies, from the final day of the fiscal year. Where an enterprise has subsidiaries, a notarised copy of the financial statements of each subsidiary for that same year must also be included.

217. The implementation of this provision has exposed some shortcomings. First, there is no difference between financial statements sent to the competent tax office and that sent to the business registration body even though the tax office and the registration body might require different information. The purpose of sending financial statements to the competent tax office is completely different than the purpose of sending financial statements to the business registration body. Second, items in financial statements required by the business registration body have not been specified. Third, there is no provision requiring unified and consolidated financial statements in respect to enterprises with subsidiaries, while only a notarised copy of the financial statements of each subsidiary is required.

218. Experience over the past five years has shown that the number of enterprises sending financial statements is very small and accounts for approximately 20 to 25 percent of all registered enterprises. In a number of localities where the business registration body has allowed simplified forms of financial statements, the number of enterprises sending financial statements is large, approximately 60 to 70 percent of all enterprises in that locality. In addition, information in financial statements are usually incomplete and inaccurate. It may be argued that the provision on financial statements is not appropriate to current conditions. The implementation of this provision is less effective and does not satisfy either the requirements for State administration nor the requirement to publicize the financial results of enterprises to related parties.

219. The provisions on penalties and the methods of dealing with breaches in the Enterprise Law are similar to other laws in Viet Nam. In particular, the EL only lists a number of breaches and the penalties (disciplinary action, administrative penalty or prosecution for criminal liability), depending on the seriousness and nature of each breach. The EL also specifies breaches of persons issuing business registration certificates and persons applying for business registration. During the course of implementation additional penalties were added; administrative penalties have been specified for respective breaches. But specific provisions on prosecution for criminal liability have not been made.

220. There are two types of breaches of persons issuing business registration certificates: (1) issuing business registration certificates to persons who do not legally qualify; and (2) refusing to issue business registration certificates to persons satisfying the conditions stipulated in the EL. Experience has shown that only breaches of the first type are dealt with, while breaches of the second type are ignored. In the past, many relevant State bodies and State employees in breach of this provision (by refusing to issue certificates to qualified persons) have not been subject to any penalties. These breaches are committed by authorized State bodies at both the central and local levels. Meanwhile, provisions and relevant institutions for dealing with such breaches are not available. Further discussion is required regarding this situation where persons

who comply with the EL are forced to deal with State officials who do not uphold regulations and are, themselves, in breach of the EL[69]. This is a point of failure in the Enterprise Law.

221. It can be argued that only two types of breaches of State bodies stipulated in the EL is inadequate. For example, other breaches, such as interfering illegally in business activities or in the internal management of enterprises, and failing to revoke business registration certificates in accordance with the regulations, are common, but not dealt with.

222. Regarding breaches by persons applying for business registration, examples include: forging a file, falsifying declared information for business registration, masquerading as an enterprise (establishing an enterprise not for business purposes, falsifying capital contribution, or failing to contribute capital or contributing capital only after withdrawal from the established enterprise etc.), and the abuse of powers in the management of an enterprise by receiving bribes, misappropriating assets of the company, or embezzling assets of a company. These breaches have not been included in the Enterprise Law. In brief, the EL mainly focuses on breaches relating to business registration, but do not pay appropriate attention to potential breaches during the regular course of business, especially in the management of companies.

223. As mentioned above, prosecution for criminal liability subject to the seriousness and nature of the illegal act has not been clearly outlined. “Prosecution for criminal liability” may not be subject to guidelines provided by company by-laws. “Criminal penalties” are provided only in the Criminal Code. It is likely that certain offences specified in the Criminal Code are not specified in the EL and vice versa. Moreover, some offences specified in the Criminal Code may be incompatible with criminal offences whose seriousness and nature are subject to prosecution for criminal liability in the EL. As a result, while some offences should be subject to prosecution for criminal liability, they are, instead, subject only to administrative penalty, or not even dealt with at all. Experience has exposed this shortcoming that has resulted in a number of offences of the EL that have not been dealt with in a proper and timely manner. This lack of perceived justice is likely to increase doubts about the soundness and rationality of the Enterprise Law.

[69] A number of officials in charge of business registration have been dismissed, removed or transferred to another position because they have disobeyed the order of their supervisor to refuse issuance of business registration certificates in accordance with the conditions stipulated in the Law.

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