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## Legal Update – Vietnam’s New Law on Enterprises 2020

The National Assembly of Vietnam recently approved a new *Law on Enterprises 2020 (59/2020/QH14)*, superseding the *Law on Enterprises 2014 (68/2014/QH13)*. As with previous versions, the *Enterprise Law* continues to regulate the establishment, operation, and governance of corporate entities, and exists as the primary legislative instrument in the area of Vietnamese corporate law. The new law will come into effect on 1 January 2021. Directors, shareholders, and prospective investors are encouraged to consider the key amendments discussed below. Critically, companies should also ensure that their charters and internal processes are amended and adapted as necessary to ensure consistency and compliance with the terms of the new law as of **1 January 2021**. If not, they run the risk of taking unlawful corporate actions which could jeopardise validity of transactions and/or give rise to potential disputes and liabilities.

### ***One Member Limited Liability Company – Corporate Owner***

Where a one-member limited liability company is owned by a corporate member, there is now no longer a requirement to appoint official controllers (sometimes called inspectors). Rather, the incoming law provides for the following possible two organisational structures: i) Chairman and Director/General Director; or ii) Council of Members and Director/General Director.[1] Importantly, the company must appoint at least one legal representative who must also simultaneously hold the position of Company Chairman, Chairman of the Members’ Council, or Director/General Director.[2]

### ***Capital Transfers by Foreign Investors***

The *Enterprise Law 2014* provided an express blanket obligation that all foreign capital contributions (as well as dividend repatriations, and the purchase, sale, and transfer of shares) must be routed via an authorised capital account with a Vietnamese bank, except where such transfers were made in the form of assets.[3]

The phrasing under the 2020 law remains unchanged, merely re-stating that all foreign capital transfers must be routed via a capital account, except for transfers in the form of non-cash assets.[4]

In potential conflict with the above position, State Bank of Vietnam regulations under *Circular 06/2019/TT-NHNN* provides that transfers between two non-resident investors need not be routed via a capital account, irrespective of whether or not the transfer was in the form of cash or non-cash assets. [5]

Issues around Vietnamese foreign exchange control laws and the use capital accounts remain highly complex and uncertain, and we intend to produce further publications on such matters in due course. Whilst the 2020 law does touch on the issue, it is still silent as to when foreign investments are categorically deemed to be direct or indirect for the purposes of routing contributions via a formal capital account. It is strongly recommended to seek further legal advice prior to the making of any foreign capital contributions, as non-compliance may result in material transaction delays and prohibitions on the repatriation of future profits.

### ***Bond Offerings***

It has been widely reported that the Vietnamese domestic bond market has recently experienced significant overheating, largely as an indirect consequence of the State Bank of Vietnam imposing credit restrictions, particularly on real estate ventures.

The new law plays a part to address such concerns via the introduction of additional statutory obligations on corporate bond issuers and investors. The new law continues to allow for the issuance of bonds by private joint stock companies, however placement requires satisfaction of numerous complex transparency obligations, including in relation to audit procedures, shareholder approval, stock exchange notification, prudential and debt ratios, amongst others.[6] Such requirements on issuance also overlap with existing stipulations under the *Securities Law 2019* and various guiding decrees, and it is therefore strongly advised to seek legal counsel on such matters prior to considering a private placement. Under the 2014 regime, the placement of private bonds only required the board of management to report on the issuance to shareholders in the next general meeting, including details of bond value, timing, class, and an explanation of the board's resolution.[7]

The new law also allows for multiple member limited liability companies to issue bonds, [8] which was previously restricted to that of only joint stock companies under the 2014 law.

### ***Additional Protections for Minority Shareholders***

The new law allows a group of shareholders (5% or more) of a joint stock company to access important corporate information, including financial statements, resolutions, minutes, and inspection committee reports, amongst others. [9] This is a lowering of the threshold from 10% under the 2014 law.[10]

The group may also seek to convene a shareholders' meeting in specific circumstances (i.e. serious breach of shareholder rights by the board of management). [11] Ordinary shareholders are now no longer required to hold their

shares for a minimum ownership period (i.e. 6 months as under the 2014 law [12]) before being able to exercise general shareholder rights.[13]

Additionally, a group of shareholders (10% or more) now need not wait for 6 months post-investment before being able to exercise their right to nominate a specific director to the board of management. [14] This amendment is crucial, as in practice it had been commonplace for such delay to restrain incoming investors from nominating a preferred director at the time of investment completion.

Of note, the amendment comes on the back of a 2018 controversy, whereby incoming majority shareholder, ThaiBev, was denied the ability to nominate members to the board of management of Sabeco, Vietnam's largest domestic brewer. This occurred due to the fact that ThaiBev had not held their shares for at least 6 months prior to the holding of Sabeco's extraordinary general meeting, which was principally held for the purposes of nominating board of management members post-investment completion.

### ***Rights of Preference Shareholders***

Preference shares are a form of non-voting shares under current Vietnamese law. Significantly, the new law allows for shareholders holding preferred dividends and redeemable preferred shares to have limited participation rights. Such shareholders will be allowed to attend and vote in shareholder meetings where proposed resolutions adversely impact their rights and obligations.[15] In such cases, a resolution will only pass where it is approved by at least 75% of shareholders who hold that specific class of shares.[16] It is important to note that the incoming provision does not provide an express definition of "adverse" should a shareholder dispute scenario arise.

This is a crucial amendment, providing much needed statutory protection to the rights of preference shareholders. In principle, Vietnamese law currently allows ordinary shareholders to alter the substantive terms of a class of preference shares via the passing of a general shareholders' resolution. The above incoming 75% threshold seemingly serves to restrain such adverse action. Of course, the minority 25% shareholding group will nevertheless still be potentially subject to adverse alteration, and it is strongly recommended that appropriate consent rights are negotiated and drafted into the shareholders' agreement at the time of investment.

### ***Pre-emptive Rights***

Where a private joint stock company seeks to issue new shares by way of private placement, the amended law provides that existing shareholders are to be given pre-emptive rights over the subscription of such shares, except in a situation of merger or consolidation. [17]

Accordingly, in practice, a private joint stock company should obtain a formal waiver of pre-emptive rights from existing shareholders prior to undertaking a private placement of new shares. It may also be necessary for a general resolution to pass

where such shares are offered on more favourable terms than those currently in existence. [18]

While this amendment will be welcome to some, it will serve as a potential constraint and unwelcome development for others. This sort of change in the 2020 law also highlights a significant point that has not been addressed: the role and scope of shareholder agreements in which shareholders may reach agreement on points that run contrary to otherwise mandatory terms of the Enterprise Law (e.g. – agreement to be issued new shares in priority to other shareholders). Despite the common use of shareholder agreements in Vietnam, there remains significant question marks over their validity and enforcement in practice. Nothing in the 2020 law suggests a change to this status quo.

### ***Legal Representative Liability***

A joint stock company or limited liability company may now appoint multiple official legal representatives. The specific rights and duties of each appointed representative must be recorded in the charter of the company. [19]

Should the charter be silent as to such allocation of duties, each individual legal representative stands to represent the company before third parties.[20] Under the new law, legal representatives are also now *jointly liable* for any loss or damage related to the company.[21] There continues to be no express indication that companies can agree to insure or indemnify legal representatives against such liabilities.

### ***Shareholder Confidentiality Obligations***

Shareholders of joint stock companies are now under an obligation to keep corporate information confidential and refrain from distribution to third parties (presumably most relevant to substantive financial reports, strategic planning etc). [22]

The provision does not precisely identify the forms of relevant information nor circumstances where distribution would otherwise be permitted. It is also unclear whether such obligations would materially prevent a shareholder from providing corporate information to a prospective purchaser of shares.

### ***State Owned Enterprises – Lower Threshold***

The new law amends the 2014 position, providing that State-owned enterprises (SOEs) are now to be defined as enterprises comprising of a State shareholding of more than 50% charter capital or voting rights. [23] The 2014 law previously defined SOEs as those enterprises with 100% State owned charter capital. [24]

This will have the effect of increasing the number of SOEs significantly. While this may serve a policy position of enhancing State control over use of State capital, it may have an adverse impact, especially when considering the drive to speed up the

equitization process in general. SOEs are, in general, subject to stringent rules on audit, fund raising, and procurement, and such rules may serve to dampen the interest of potential strategic minority investors.

### ***Digital Signatures***

Enterprises are now free to utilise both physical seals *and* digital signatures when executing company documentation. Consistent with the current *Law on Electronic Transactions*,<sup>[25]</sup> digital signatures will be given the same legal weight with that of traditional physical seals. This is particularly relevant due to the current Covid-19 situation, introducing timely flexibility and practicality into corporate administrative practice. <sup>[26]</sup>

### ***Board of Management – Rights and Obligations***

The rights, duties, and liabilities of members of the board of management of joint stock companies remain largely unchanged under the new law, albeit with the following technical amendments.

Firstly, a shareholder holding as little as 1% has standing to commence legal proceedings against a director or member of a board of management who is in breach of their duties, regardless of how long the shareholder has held their shares (previously minimum 6 month holding requirement under the 2014 law).<sup>[27]</sup>

Secondly, where the board of management passes a resolution contrary to law or the charter of the company, a single shareholder now has the right to commence legal proceedings and request that the resolution be suspended or rescinded,<sup>[28]</sup> again with no minimum holding requirement (previously 1 year under the 2014 law). <sup>[29]</sup> This will importantly empower incoming shareholders who would otherwise have limited formal legal recourse against unlawful board action.

Thirdly, a board appointed independent director can now only serve for two consecutive terms. <sup>[30]</sup> There was previously no limit under the 2014 law. <sup>[31]</sup> This amendment will ensure that appointed independent directors are better able to meet their corporate governance objectives, bringing greater transparency and impartial oversight to the management of joint stock companies in Vietnam.

Finally, a board member of a joint stock company which is also a State-owned enterprise (i.e. State shareholding / charter capital of more than 50%), must not have a family relationship with a manager of the company, or with a manager of the parent company.<sup>[32]</sup> Again, such amendment brings greater transparency and governance standards, better protecting shareholders against improper corporate conduct.

### ***Transitional Requirements***

It is highly recommended that all enterprises undertake a thorough review of their existing company charters and proactively identify and amend any clauses which are inconsistent with the incoming law prior to 1 January 2021.

Where a company charter is inconsistent with the new law, board actions based on such outdated clauses (e.g. prohibiting a new shareholder from nominating a specific director until at least 6 months of shareholding has passed) may be legally challenged and potentially deemed invalid at law.

### **Conclusion**

In conclusion, Vietnamese corporate law continues to positively evolve with the approval of the amended *Enterprise Law 2020*.

Significantly, the new law enhances protections for minority and preference shareholders, whilst consolidating pre-emptive rights. Importantly, the law also simplifies organisational structures for one-member limited liability companies, and allows for the use of digital signatures in the execution of corporate documentation.

Finally, the new law seeks to address recent concerns around overheating and transparency in the Vietnamese domestic bond market, introducing greater statutory obligations on private issuers and investors alike.

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[1] Art 79(1), *LoE 2020*.

[2] Art 79(3), *LoE 2020*.

[3] Art 36(3), *LoE 2014*.

[4] Art 35(5), *LoE 2020*.

[5] Art 10(1), *Circular 06/2019/TT-NHNN*.

[6] Art 128(3), *LoE 2020*.

[7] Art 127(4), *LoE 2014*.

[8] Art 46(4), *LoE 2020*.

- [9] Art 115(2)(a), *LoE 2020*.
- [10] Art 114(2), *LoE 2014*.
- [11] Art 115(3), *LoE 2020*.
- [12] Art 114(2), *LoE 2014*.
- [13] Art 115(2)(a), *LoE 2020*.
- [14] Art 115(5), *LoE 2020*.
- [15] Art 148(6), *LoE 2020*.
- [16] Art 148(6), *LoE 2020*.
- [17] Art 125(2)(b), *LoE 2020*.
- [18] Art 125(2)(c), *LoE 2020*.
- [19] Art 12(2), *LoE 2020*.
- [20] Art 12(2), *LoE 2020*.
- [21] Art 12(2), *LoE 2020*.
- [22] Art 119(5), *LoE 2020*.
- [23] Art 88(1), *LoE 2020*.
- [24] Art 4(8), *LoE 2014*.
- [25] *Law on Electronic Transactions 51/2005/QH11*.
- [26] Art 43(1), *LoE 2020*.
- [27] Art 166(1), *LoE 2020*; Art 161(1), *LoE 2014*.
- [28] Art 153(4), *LoE 2020*.
- [29] Art 149(4), *LoE 2014*.
- [30] Art 154(2), *LoE 2020*.

[31] Art 150(2), *LoE 2014*.

[32] Art 155(1)(d), *LoE 2020*.