

**V I L A F****VIETNAM INTERNATIONAL LAW FIRM**

## Vietnam Energy and Infrastructure

### FURTHER LEGAL REFORMS

## A SHIFT OF FOCUS TO LARGE PROJECTS AND ENVIRONMENT-FRIENDLY PROJECTS?

Infrastructure has been a central factor in Vietnam's economic development. The Government aims to raise investment in transport infrastructure from US\$7 billion to US\$120 billion by 2020. ADB experts project that Vietnam will need to invest US\$110 billion in infrastructure development between 2021 and 2025. Likewise, Vietnam will need another 5,000MW in power plant capacity by 2025, which will require about US\$30-45 billion in investment.

The Politburo in Resolution 50/NQ-TW dated 20 August 2019 ("Resolution 50") has directed the policy

of attracting large scale and high-quality foreign investments and targeting at a 50% increase in investments with use of modern or environment-friendly technologies by 2025. In accordance with the above policy, Vietnam has passed a number of new laws which will take effect on 1 January 2021, of which the two laws of paramount importance to investment projects are the Investment Law and the PPP Law.

This article sets out some important changes which will affect project investments.

## NEW INVESTMENT LAW

### New concept of “special investment incentive” introduced

The lowest incentive corporate income tax rate in Vietnam to date has been 10%. Under the new Investment Law, the Prime Minister is empowered to grant any of the following projects a “special investment incentive” of 5% corporate income tax rate for a period which may be 1.5 as long as the maximum tax incentive period under the laws:

- A research and development project with a minimum investment capital of VND3,000 billion, disbursed at least VND1,000 billion within 3 years after being licensed;
- A national innovation and invention center established by the Prime Minister’s decision; and
- A project falling on the list of *especially encouraged sectors* with a minimum investment capital of VND30,000 billion, disbursed at least VND10,000 billion within 3 years after being licensed.

The statutory list of *especially encouraged sectors* is provided in Decree 118/2015/ND-CP on investment, issued by the Government on 12 November 2015. However, note that Decree 118/2015/ND-CP will soon be replaced with a new decree to implement the new Investment Law. Therefore, how this list may be amended should be continually monitored.

### M&A approval required cases

The M&A approval is the approval required to be obtained when a foreign investor (or a local company which is considered a *foreign investor equivalent* under the investment laws) proposes to acquire equity interests in a company in Vietnam in specified circumstances. The M&A approval is designed to certify that the proposed foreign investor is eligible to acquire the relevant equity interests in the target company.

The new Investment Law amends the circumstances in which an M&A approval is required as follows:

Under New Investment Law	Under Old Investment Law
<ol style="list-style-type: none"> <li>1. The acquisition leads to an increase in the foreign ownership ratio in a company engaging in business lines with market access conditions for foreign investors;</li> <li>2. The acquisition leads to an increase in the foreign ownership ratio in a company from 50% or less to more than 50% of the charter capital; or a further increase in the foreign ownership ratio if it has been over 50%;</li> <li>3. The acquisition of a company which has a land use right certificate for frontier land and island, coastal land areas or other areas which may affect national defense and security.</li> </ol>	<ol style="list-style-type: none"> <li>1. The acquisition of a company engaging in conditional business lines applicable to foreign investors;</li> <li>2. The acquisition leads to an increase in the foreign ownership in a company to at least 51% of the charter capital.</li> </ol>

Limb 1) in the new Investment Law column introduces important and favorable changes. The old law required an M&A approval for any transaction with respect to a target company engaging in “conditional business lines applicable to foreign investors” but did not provide guidance for determining such business lines. This led to uncertainties in application of the requirement and investment authorities have required an M&A approval in most cases due to the ambiguities.

The new Investment Law resolves the above ambiguity and reduces the cases where the M&A approval is required in limb 1). In particular, the new law states that the Government will issue the list of business lines with market access conditions for foreign investors. This will bring about more transparency. Additionally, even in case the target company engages in such business lines, the M&A approval is required only if the foreign ownership ratio is increased. As such, if a foreign investor buys shares from another foreign investor, the M&A approval is not required because the foreign ownership ratio is not increased.

Limb 3) is new and is introduced with the objective of strengthening mechanism to protect national defense and security as directed by the Politburo's Resolution 50. This new requirement relates to cases of acquiring frontier land and island, coastal land areas and other land areas sensitive to national security via acquiring shares in a company owning the right to use such land. A direct acquisition of land use rights is subject to registrations and scrutiny under the land laws while an acquisition of shares in a company holding such land use rights could escape such scrutiny under the investment laws. The new Investment Law attempts to address this issue via the M&A approval procedure.

#### State authorities' project termination rights expanded: nominee investments

The new Investment Law introduces another important circumstance where the State authorities are entitled to terminate an investment project: when it is found that the investor has invested in the project in a **simulated transaction** under the Civil Code.

This requirement arose out of the concern raised in the Politburo's Resolution 50 that many projects were approved under companies incorporated by local investors, but actually operated via certain nominee arrangements with foreign investors and involved in businesses which may be sensitive to national defense and security or involved in transfer pricing.

Under the Civil Code, if the parties **simulate a transaction to conceal another transaction**, the simulated transaction is void while the concealed transaction is valid, unless the concealed transac-

tion is also void pursuant to the laws. It is unclear how the above provision of the Investment Law will be linked to the Civil Code in this regard. Monitoring has to be made if any regulatory guidance will be issued in sub-law decrees to provide clarity to implementation. Subject to further guidance, one may be able to construe that, as guided in the Civil Code:

- in case a foreign investor and a local nominee enter into a secured loan transaction to fund the nominee's investment in a local company, but the secured loan transaction is simulated to conceal the foreign investor's equity participation in the local company, then the secured loan transaction could be declared void and the equity participation is valid;
- however, if the equity participation is made in a sector where foreign investment is restricted or prohibited, then the equity participation is also void.

If the equity participation is made in a sector where foreign investment is not prohibited, but due to the nominee arrangement the equity investment does not obtain the required regulatory approvals, will the equity participation be exposed to the risk of being considered void? Likely yes though the risk will be lower.

It is however unclear at what stage the relevant State authorities will have the right to terminate a project. What test will apply to determine if a transaction is "simulated"? Additionally, will the state authorities be required to wait for a court judgment to declare the transactions void pursuant to the Civil Code before their right of termination is triggered?

In the lack of regulatory guidance on how this new provision will be interpreted and implemented, foreign investors should be cautious about contractual nominee arrangements, noting that the risk may be particularly higher with respect to:

- investments in land use rights;
- investments in sectors prohibited of foreign investments or subject to foreign ownership restrictions; and
- investments with the objective of disguising the countries of origin of exported products.



## NEW PUBLIC-PRIVATE PARTNERSHIP LAW (PPP LAW)

The new PPP Law is the first PPP Law passed by the National Assembly in Vietnam. Before this law, PPP regulations were issued as sub-law regulations. The introduction of a legal framework for PPP projects at the law level aims to ensure particular rules intended to apply to PPP projects cannot be unintentionally prevailed by other laws passed by the National Assembly. Although significant effort has been made on the

development of the new PPP Law, there may be reasons to be skeptical that the changes would give a boost for PPP investment interests, unless sub-law regulations actively strengthen the incentives where appropriate.

### Eligible sectors for the PPP framework

The new PPP Law provides for a significantly narrower range of sectors eligible for the PPP framework than the old regulations.

Eligible sectors under new PPP Law	Sectors eligible under the repealed PPP regulation which have been removed in the new PPP Law
<ol style="list-style-type: none"> <li>1. Transportation;</li> <li>2. Power plants and power grids (except hydro-power plants and sub-sectors under state monopoly according to the Electricity Law);</li> <li>3. Irrigation, clean water supply, drainage, sewage and waste treatment;</li> <li>4. Healthcare, education and training; and</li> <li>5. Information technology infrastructure.</li> </ol>	<ol style="list-style-type: none"> <li>1. Public lighting systems; parks; housing and yards for parking cars, vehicles, machinery and equipment; cemeteries;</li> <li>2. Headquarters or offices of state agencies; state-owned housing for government employees; social housing; resettlement housing;</li> <li>3. Vocational training; culture; sport; tourism; science and technology, hydrometeorology;</li> <li>4. Commercial infrastructure; infrastructure of urban zones, economic zones, industrial zones, industrial clusters, and of centralized IT zones; hi-tech technical infrastructure; incubation establishments, technical establishments and common working areas supporting small and medium-sized enterprises;</li> <li>5. Agriculture and rural development; and</li> <li>6. Other sectors as decided by the Prime Minister.</li> </ol>

### PPP contract forms

The new PPP Law recognizes seven types of PPP project structures that are categorized into three groups:

1. Project contracts applying direct fee collection from users or off-takers: Build-Operate-Transfer (BOT); Build-Transfer-Operate (BTO); Build-Own-Operate (BOO); and Operation and Maintenance (O&M);
2. Project contracts applying the state's payment based on the quality of public products or services provided: Build-Transfer-

Lease (BTL); Build-Lease-Transfer (BLT); and

3. Mixed contracts: a contract combining the contract types in 1. and 2.

The new law removes Build-Transfer (BT) projects from permissible PPP models. Although they have been the most popular PPP contract form used to date in Vietnam (according to the Government's Report No. 25/BC-CP in 2019, out of a total of 336 PPP projects, 188 are under BT contracts and 140 under BOT contracts), there have been many shortcomings in the imple-

mentation of BT projects. The public has raised concerns that this form may create opportunities for undervaluation of public assets being transferred to the private sector.

## Capital requirements

### Investment capital

The PPP Law maintains that except for O&M projects, the minimum investment capital of a PPP project in the healthcare or education sector or in areas with difficult socio-economic conditions cannot be less than VND100 billion and in other cases cannot be less than VND200 billion. The Government will determine the minimum total investment scale for each sector.

### Equity capital ratio

The equity capital ratio requirement is simplified under the PPP Law, which stipulates that the investor must contribute at least 15% of the total investment capital, excluding state capital contributions.

### Share or equity transfer

The transfer of shares or equity capital between existing investors in a PPP project is permitted provided that the lead investor retains at least 30%, and each other investor retains at least 15%.

The transfer of shares or equity capital to outsiders is permitted only after completion of construction for the PPP project or, in case of a project without the construction component, after commercial operation.

Any transfer of shares or equity capital in the PPP project must also satisfy the following requirements: upholding of the performance of the executed PPP project contract, compliance with provisions of relevant laws, approvals of the state agency entering into the PPP project contract and of the lender and other investors.

## Selection of investor

Under Decree 25/2020/ND-CP dated 28 February 2020, the selection of investor for a PPP project must be conducted via a public auction, except where only one eligible investor registers to participate or in certain special cases with the objective of protection of national defense or border land.

The PPP Law now broadens the circumstances where other forms of investor selection may be permitted. In particular, the “competitive negotiation” form may be permitted in any of the following cases:

1. No more than 3 eligible investors are invited;
2. The project applies high technology falling on the list of high technologies being encouraged for development under the law on high technology;
3. The project applies new technology under the law on technology transfer.

The PPP Law also grants the Prime Minister the power to determine the selection of the investor as a special case based on evaluation of unique, special conditions of a particular project.

## Risk sharing regime

The PPP Law removes reference to the important government guarantees for obligations of state-owned enterprises which were provided in the prior regulations. It is unclear whether this would mean this mechanism would be removed entirely from the PPP landscape. For reference, to date, BOT power projects in Vietnam have benefited from the government guarantee for Vietnam Electricity’s payment obligations under power purchase agreements.

The PPP Law on the other hand introduces for the first time a “risk sharing regime.” In this regime, if revenue exceeds the agreed financial plan by more than 25%, the PPP project company will share half of the excess with the government subject to cost deductions. On the other hand, if revenue falls by more than 25% from the agreed financial plan, the government will share half of the shortfall with the PPP project company subject to cost deductions and satisfaction of certain conditions.

The risk sharing scheme applies to BOT, BOO and BTO projects, and only when the revenue decrease is due to changes in the laws, policies or master plans. Whether the actual implementation of this risk sharing scheme when it comes to the detail will be desirable to investors remains to be seen when sub-law regulations are developed.

## Governing law and dispute resolution

For many years, the chosen governing law for PPP project contracts involving foreign investors have been Singapore law or English law. The PPP Law for the first time requires the PPP project contract and its auxiliary documents between the project investor or project company and the relevant Vietnamese state agency to be governed by Vietnamese law, except with respect to matters Vietnamese laws do not regulate.

Nonetheless, similarly to the prior regulations, the PPP Law still recognizes the contractual rights to agree on international arbitration for disputes between a Vietnamese state agency and a foreign investor or project company established by a foreign investor. Where there is no agreement on international arbitration, disputes must be resolved by Vietnamese arbitration or Vietnamese court, unless provided otherwise under an international treaty to which Vietnam is a party.

### VILAF UPDATE



Leading law firm VILAF has again won:

**Vietnam Most Innovative National Law Firm of the Year Award** by IFLR Asia-Pacific Awards 2020 in March 2020

**Client Service Excellence Best Firm Award** by Asialaw in May 2020

**Impact Case of the Year Award** by Asialaw in July 2020

This month, the firm has been nominated for the **2020 Project Finance Deal of the Year Award** by Asian Legal Business (ALB) Japan Law Awards for the the following projects:

- The Refinancing of Mong Duong 2 BOT Power Project
- The Financing of Van Phong 1 BOT Power Project

VILAF also continues to be ranked **first tier** in all major practices on IFLR 1000, Legal 500, Chambers Asia Pacific, Asialaw, and Benchmark Litigation.

Legal 500 quotes, *“Ranked in the top tier across the board for financial and corporate work, VILAF is one of the strongest firms in Vietnam. The firm notably boasts the largest teams of English-speaking project development and M&A lawyers in Vietnam.”*

VILAF has advised a number of prominent transactions which have been closed during the first half of the year:

- The merger of VinGroup’s Vincommerce retail chain business with Masan Group
- The US\$240 million sale of all equity stake in Think Phat Cables and Dovina to Stark Corporation
- The US\$650 million investment by KKR’s led consortium of investors in Vinhomes

VILAF team sends to all clients and friends our best wishes for the health of you and your loved ones!

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