

TOP THREE CHANGES OF THE NEW ENTERPRISE LAW DECEMBER 2014



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TOP THREE CHANGES OF THE NEW ENTERPRISE LAW¹

Since 1999, after each revision of the Enterprise Law, the business community and experts always have great expectations for breakthrough improvements in the business environment. Meeting those expectations, the new Enterprise Law introduces three major changes to improve the investment and business environment.

1. Firstly, the Law concretizes the right to freedom of enterprise based on the constitutional principle: Everyone has the right to freedom of enterprise in the sectors or trades that are not prohibited by law²

Under the current Enterprise Law, an enterprise is free to register business lines which must be recorded in its business registration certificate and it may only conduct these business lines. In the process of doing business, if the enterprise wants to expand business activities, it must carry out administrative procedures to change the contents of its business registration certificate. In fact, the enterprise only has the right to freely do business in registered business lines. If it conducts business lines not recorded in its business registration certificate, these business activities are considered illegal.

As a result, an enterprise often registers a lot of different business lines, from tens to hundreds while it actually conducts only one or several business lines. This has led to many negative consequences, such as deviations in statistical data which affect state management work; legal risks facing enterprises in their business activities or their failure to seize ordinary business opportunities.

To overcome the above limitations, the new Enterprise Law clearly affirms the business right of enterprises on the principle of "*freedom of enterprise in the sectors or trades that are not prohibited by law*³".

¹ The new Enterprises Law was passed on 26, 2014, by the National Assembly and will take effect on July 1, 2015. It will replace Enterprise Law No. 60/2005/QH11 of November 29, 2005

² See Article 33 of the 2013 Constitution: Everyone has the right to freedom of enterprise in the sectors and trades that are not prohibited by law

³ Clause 1, Article 7 of the Enterprise Law

Under the Law, business lines are divided into three categories: banned business lines, conditional ones and other business lines. Enterprises are not allowed to conduct banned business lines. They enjoy autonomy and may take the initiative in conducting conditional business lines upon satisfying business conditions and must fully maintain these business conditions in the course of conducting these business lines. Enterprises are free to conduct other business lines.

The enterprise establishment registration procedures are now regarded as enterprise birth declaration procedure, with the enterprise registration certificate regarded as the birth certificate of a new enterprise. Therefore, according to the Law, an enterprise registration certificate no longer contains information on business lines. It only states basic information about an enterprise, such as enterprise code, address of its head office and its at-law representative. An enterprise, at the time of establishment, will declare business lines it expects to conduct and record them in the enterprise registration file. In the course of business operation, it is required to inform new business activities only after conducting them.

These above-mentioned changes are expected to considerably reduce commercial and legal risks, reduce transaction costs and enhance the safety, initiative and creativity for enterprises in their business activities, thus creating favorable conditions for them to make full use of their potential and business opportunities for development.

2. Secondly, the Law better protects the rights and legitimate interests of investors, making enterprises a safer and more attractive business tool and attracting all investment capital sources into production and business activities

According to the World Bank's assessment criteria⁴, investor protection in Vietnam is always rated at low levels compared to other countries in the region and over the world. Among the three assessment indices of investor protection, Vietnam achieves a fairly good rate, 7/10 point, on the disclosure of related transactions, but gains a bad rate on the other two indices, including managers' obligations (1/10 point) and the eligibility of taking legal action against managers (2/10 point). With the following significant changes, the Law has addressed the limitations of the current Enterprise Law and improved the protection of investors and shareholders:

⁴ <http://doingbusiness.org>

The Law heightens the requirement of information disclosure for companies, expands the shareholders' right of access to information and enhances the right of access to information on a periodical basis or upon request for all shareholders regardless of their holding rates, particularly information on management and transactions that are at risk of self-interest seeking. Shareholders are entitled to read or copy part or the whole of the list of affiliated persons and related interests during working hours. Companies must create conditions for shareholders to exercise their right in the quickest and most convenient manner.

The Law articulates more clearly and specifically the obligations and responsibilities of company managers. Accordingly, managers of a company must declare their related interests to the company, including enterprises in which they own capital contributions or shares and enterprises in which their related persons co-own or privately own capital contributions or shares exceeding 10% of charter capital. Managers are responsible for exercising their rights and obligations in an honest, prudent and optimal manner to ensure to the utmost lawful interests of the company and its shareholders. They are not permitted to use business information, know-how and opportunities of the company, and abuse their position, power and use the company's assets for their own benefits or the interests of other organizations and individuals.

Shareholders are offered more favorable conditions to take legal action against a company manager for his failure to duly perform his obligations and acts causing losses to the company and shareholders. If the manager breaches his obligations, individual shareholders or a group of shareholders may initiate a lawsuit in their names or the name of the company against the manager⁵. Expenses for legal action taken in the company's name may be accounted into the company's expenses, except the case in which the lawsuit petition is rejected.

However, whether or not the provisions on protection of investors and shareholders can be effectively implemented in reality depends much on the awareness of investors and shareholders. Realities show that at present, company managers, investors and shareholders do not have a proper understanding of the definition of managers' obligations although it was mentioned in the 1999 Enterprise Law. Many still confuse "*the obligations of managers*" and "*the rights and duties of managers*". Therefore, investors and shareholders themselves must study and thoroughly understand their rights and ways to self-protect their lawful rights and interests.

⁵ Under the current Enterprise Law, shareholders or group of shareholders are allowed to initiate a lawsuit against the manager only after they request the Control Board to initiate a lawsuit but the Control Board refuses.

3. Thirdly, the Law changes the method of state management of enterprises and facilitates supervision by stakeholders of enterprise performance

The Law introduces a new, modern method of state management conformable to the economic development and expansion. Accordingly, although the State is responsible for supervising enterprises according to its functions, it is not the sole entity burdening such duty; stakeholders, including shareholders, partners and customers, are encouraged to participate in supervision for their own interests.

Specifically, the Law adds provisions to promote coordination and information exchange among state management agencies to create a complete, updated and public national database on operations of enterprises after business registration, called the National Business Registration Database.

The State will create conditions for stakeholders to participate in enterprise supervision by providing them with relevant information about enterprises in a timely and convenient manner.

The Law also introduces new provisions to enhance the transparency and publicity of enterprise performance, thus enabling shareholders and company members to implement internal supervision of enterprises.

The above three changes are just some of many reformed provisions of the new Enterprise Law. These substantial changes explicitly express the spirit that the State enacts laws to create and promote development. Finally, it must be emphasized that in order to bring into full play the reforms introduced by the Enterprise Law, not only state management agencies but also enterprises and stakeholders must spare no efforts. Enterprises, investors and shareholders themselves must proactively and actively supervise one another in order to protect their rights and legitimate interests.

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