Briefs on Foreign Investment

In Vietnam

Eruditus Legal Co., Ltd

A. Overview

Vietnam offers an attractive economic environment for businesses and investors, supported by a modern legal framework. However, operating a business in Vietnam requires highly qualified management and a thorough understanding of the legal and practical conditions.

Foreign investors are free to pursue any business line that is not prohibited or restricted. However, obtaining the necessary licenses and navigating the administrative processes can be challenging.

With sixteen Free Trade Agreements[1] (FTAs) in effect or signed, and an additional three FTAs under negotiation, coupled with its World Trade Organization (WTO) membership since 2007, Vietnam has significantly enhanced its appeal as an investment destination. The recent passage of numerous new laws in 2023 and 2024, along with the strengthening of comprehensive partnerships with several countries, further solidifies Vietnam's position as a rising economic star in the region.

Vietnam's economy is experiencing steady growth, driven by factors such as its strategic geographical location, a young and dynamic workforce, and a favorable investment climate. The country has successfully attracted significant foreign direct investment (FDI), particularly in manufacturing, technology, and services.

Key indicators[2] of Vietnam's economic performance include:

- GDP Growth: Vietnam has maintained a consistent GDP growth rate of around 6-7% in recent years, outperforming many other countries in the region.
- Inflation: The inflation rate has remained relatively stable, contributing to economic stability.
- Foreign Direct Investment: FDI inflows have been substantial, fueling economic growth and job creation.
- Export Growth: Vietnam has experienced strong export growth, particularly in sectors such as electronics, textiles, and footwear.

While there are challenges to address, such as infrastructure development and income inequality, Vietnam's economy is generally viewed as resilient and with significant potential for continued growth.

B. Legal framework

As a member of the WTO and a signatory to numerous FTAs, Vietnam has established a favorable environment for foreign investment. The Law on Investment (LOI) and the Law on Enterprise (LOE) serve as the foundational legal frameworks governing foreign investment activities in the country. These laws outline the general principles that apply

[1] https://wtocenter.vn/thong-ke/13814-vietnams-ftas-summary-as-of-april-2019
[2] https://www.mpi.gov.vn/en/Pages/2024-3-1/FDI-attraction-situation-in-Vietnam-and-Vietnam-s-sh2gfb.aspx#:~:text=%2D%20By%20sector%3A%20Foreign%20investors%20have,which%20the%20processing%20and%20manufacturing; and https://www.worldbank.org/en/country/vietnam/overview

to all domestic and foreign-invested enterprises. Supporting decrees and ministerial circulars provide specific guidance for various industries.

A key consideration for all foreign investments is the potential benefits they will bring to Vietnam's development. This factor is reflected in various regulations pertaining to licensing and tax incentives.

C. Forms of Investment

1. Establishing an economic organization

In ordinary business, a common approach for foreign investors to establish a presence in Vietnam is to incorporate a subsidiary. Prior to incorporation, foreign investors must obtain investment project approval. In this context, the investment project is the company itself.

2. Acquiring capital shares, shares in an existing company

If foreign investors are interested in an existing target company, acquiring capital shares or shares from current such the target's shareholders or owner is also a form of investment under the Law on Investment 2020.

3. Performing investment project

This form is applied to foreign investors for projects selected under the Law on Bidding 2023 or following the legal procedures on investor selection of Law on Investment 2020 and other relevant laws.

4. Business Cooperation Contract and others

A Business Cooperation Contract (BCC) is also a common vehicle for foreign investors to establish a business presence in Vietnam, either among themselves or with Vietnamese partners. To formalize such partnerships, investors must register the BCC as an investment project under the Law on Investment 2020.

Beyond the aforesaid, other investment forms are governed by specific laws tailored to their nature.

D. Forms of company

The Law on Enterprises 2020 outlines various corporate forms, including Limited Liability Companies (LLCs) and Joint Stock Companies (JSCs). Foreign investors typically opt for either an LLC or a JSC to establish their subsidiaries in Vietnam. While JSCs require a minimum of three shareholders, LLCs do not have such a restriction. For companies that do not intend to go public or engage in similar activities, LLCs are often preferred due to their simpler management structure.

E. Branch, Representative Office

Foreign traders can establish a branch or a representative office in Vietnam to conduct trading activities, as outlined in the Law on Commerce 2005. Similarly, the Law on Education 2019 allows foreign entities to set up representative offices in the education sector. However, for other business sectors, it's essential to consult relevant FTAs or commitments of Vietnam to join WTO ("**WTO Commitments**") and specific laws to determine the feasibility of establishing a branch or representative office.

Indeed, there's often confusion between the branches and representative offices of foreign traders and those of existing Vietnamese companies. Their establishment processes and legal implications differ significantly.

F. Licenses to obtain

Depending on the form of investment chosen and the specific business intention, foreign investors need to apply successfully for relevant licenses applicable to foreign investments and businesses in Vietnam. Typically, there are licenses as follows:

1. Investment Licenses

Depending on the form of the investment and scale of the project, forms of investment licenses include the following ones**:**

a) Investment Registration Certificate ("IRC"), or Approval in principle ("AIP")

Unless an investment project falls under categories requiring an AIP, foreign investors can typically proceed with an IRC. The IRC or the AIP shall have details of the project including name, location, capital figure, investor information, scale, objective business, project's implementation process, and its duration, etc.

b) Notice on approval of contributing capital or acquiring capital shares/shares ("M&A Approval")

Foreign investors will need to apply successfully for the M&A Approval if their acquisition of capital shares or shares in an existing target company (i) causes any increase of the foreign ownership of such the target operating in sector(s) with specific foreign ownership restrictions, or (ii) would raise foreign ownership in a company already partially owned by foreign investors to more than 50%. M&A Approval is also required for cases where foreign shareholder buys capital shares/shares in the target company holding land use rights in areas related to national defense or security, such as islands, border regions, or coastal areas[3].

In some cases, authorities may still require M&A approval even if the acquisition doesn't directly increase foreign ownership or fall under the specific conditions mentioned above. For instance, when a foreign shareholder transfers ownership to another entity within the same group but located in a different country, authorities may seek to verify the new investor's financial and legal capacity to fulfill the commitments made in the original investment application.

Even though the M&A Approval is designed for the form of investment on acquiring capital shares/shares in an existing target company, in fact, it does not replace the IRC. It is a necessary step in the process of transferring ownership involved with foreign investors. Once the share transfer is completed, the target company's IRC (if any) will need to be updated to reflect the new investors' information.

[3] Clause 2 Article 26 of Law on Investment 2020.

2. Enterprises Registration Certificate ("ERC")

This ERC is granted by the business managing authority in charge of a company based on an appropriate application the company's owner/shareholders have submitted. The ERC shall have details of such the company, including enterprise code (i.e., the tax code), name, address, charter capital, legal representative(s), and shareholders (if the company is an LLC; a JSC does not have information of shareholders on its ERC). A separate written confirmation attached to this ERC has details of the company's scope of business, its owners' authorized representatives, and management structure.

Within 10 days[4] upon making any changes in the contents of these documents, they must be updated or amended correspondingly.

3. Operation Licenses and others

Certain specialized sectors, such as construction, dental clinics, hospitals, education, and tourism, require specific licenses or certificates beyond standard business registration. These additional approvals are necessary for companies to operate legally and provide services in these regulated industries.

G. Scope of business

When initiating a business in Vietnam, foreign investors should meticulously outline their intended business activities. This detailed approach allows advisors to accurately identify the relevant business codes under Vietnam's Standard Industrial Classification Codes (VSIC) and the Central Product Classification (CPC). As VSIC is Vietnam's domestic classification system, while FTAs often reference the CPC system, the two systems are not directly comparable, leading to potential complexities in aligning business activities with the correct codes.

Misaligning the business scope can lead to significant issues, such as incorrect invoicing and tax deductions. Unlike domestic companies, foreign-invested enterprises (FIEs) face a more complex and time-consuming process for modifying their business scope.

Therefore, it is crucial to carefully consider and specify the business activities to ensure compliance with Vietnamese regulations and avoid potential legal and tax implications.

H. Location of the investment

Typically, the company's registered address should coincide with its primary place of operation. For manufacturing companies, selecting a suitable location within industrial zones, export processing zones, or high-tech parks is crucial. These specialized zones offer infrastructure, utilities, and incentives tailored to manufacturing activities. Non-manufacturing companies, such as service providers or trading firms, are generally established in ordinary areas. Small businesses may opt for virtual or co-working offices to reduce costs. Regardless of the chosen location, a valid lease agreement or a memorandum of understanding for leasing is required as part of the company incorporation process.

[4] Clause 2 Article 30 of Law on Enterprises 2020.

I. Capital Structure

When incorporating a company in Vietnam, it's essential to outline the capital structure. This includes the charter capital, which must be fully paid within 90 days of receiving the ERC, and the mobilized capital, which can be drawn down over the project's lifespan.

For economic organizations, the charter capital directly contributes to the project's equity. However, for other investment forms, the charter capital and contributed capital may differ. In specific sectors like real estate, regulations often mandate that the charter capital must constitute a certain percentage (e.g., 15% or 20%)[5] of the total investment capital.

Charter capital can be contributed to in various forms, including cash, land use rights, intellectual property, and other assets. However, cash payment through bank transfer is the most preferred method due to its simplicity and clarity in accounting, taxation, and foreign exchange control.

Mobilized capital is normally the difference between the project's total investment capital and the charter capital/contributed capital. This is also a limit on foreign loan amounts that the company can borrow from overseas lenders in a period of longer than 12 months. Practically, it is referred to as the "long-term loan capital". For Vietnamese-invested companies, this capital figure is not applicable in cases of capital contribution or share acquisition.

The capital structure should be carefully planned, especially for the initial two to three years of operation. Although it's possible to adjust the capital structure later on, making changes to the company's licenses can be both time-consuming and costly. Therefore, a well-thought-out capital structure is essential for efficient business operations.

J. Legal Representatives

Companies may have one or more legal representatives. At least one legal representative must be a resident of Vietnam regardless of nationality. Normally, the (General) Director should be appointed as the resident legal representative as he/she shall daily manage the company's operating affairs.

K. Investment incentives

The Law on Investment 2020 provides various incentives for eligible investment projects, including:

- Corporate Income Tax (CIT) incentives: lower tax rates, tax reductions, or tax exemptions for specific periods.
- Import duty exemptions: on goods imported to create fixed assets, and materials, supplies, and components imported for production.
- Land use incentives: exemptions or reductions in land use fees, rentals, or taxes.
- Accelerated depreciation and deductible expenses: accelerated depreciation of assets or increased deductible expenses to reduce taxable income.

[5] Clause 2 Article 9 of Law on Real Estate Business 2023.

To avail of these incentives, investors must proactively identify[6] eligible projects and apply to the relevant authorities for certification before commencing the implementation.

L. Investment and Business Managing Authorities

The Ministry of Planning and Investment (MPI) is the central administrative body responsible for overseeing foreign investment activities in Vietnam. Its functions include drafting legislation, formulating policies, providing guidance, and coordinating with other relevant agencies. The MPI also approves and issues licenses for certain large-scale or significant foreign investment projects.

Local People's Committees in cities or provinces administer foreign investment activities under their jurisdiction and issue licenses for smaller projects. In areas with high volumes of foreign investment, the Department of Planning and Investment (DPI) under the People's Committee takes an active role as the licensing authority for foreign investments outside special zones. The DPI also issues enterprise registration certificates.

To attract investment to different regions, Vietnam has established special zones, including Export Processing Zones, Industrial Zones, Economic Zones, High-Tech Parks, etc. to offer preferential treatment, such as reduced tax rates and simplified import procedures. Businesses located in these zones are subject to the regulations of the respective Management Board, in addition to general government and MPI rules.

Other specialized ministries, such as the Ministry of Science and Technology (MOST), may also be involved in foreign investment activities, particularly in developing high-tech industries. The licensing authority often consults with these ministries before approving business license applications.

Disclaimer

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[6] Article 17 Law on Investment 2020.

Appendix A:

No.	FTA	Status	Parties
FTAs in effect			
1	AFTA	Effective since 1993	ASEAN
2	ACFTA	Effective since 2003	ASEAN, China
3	AKFTA	Effective since 2007	ASEAN, South Korea
4	AJCEP	Effective since 2008	ASEAN, Japan
5	VJEPA	Effective since 2009	Vietnam, Japan
6	AIFTA	Effective since 2010	ASEAN, India
7	AANZFTA	Effective since 2010	ASEAN, Australia, New Zealand
8	VCFTA	Effective since 2014	Vietnam, Chile
9	VKFTA	Effective since 2015	Vietnam, South Korea
10	VN – EAEU FTA	Effective since 2016	Vietnam, Russia, Belarus, Amenia, Kazakhstan, Kyrgyzstan
11	CPTPP (previously known as TPP)	Effective since 30/12/2018, came into effect in Vietnam since 14/01/2019	Vietnam, Canada, Mexico, Peru, Chile, New Zealand, Australia, Japan, Singapore, Brunei, Malaysia, The UK (signed the Accession Protocol on July 16, 2023)
12	AHKFTA	Effective in Hong Kong (China), Laos, Myanmar, Thailand, Singapore and Vietnam since 11/06/2019	ASEAN, Hongkong (China)
13	EVFTA	Effective since August 01, 2020	Vietnam, EU (27 members)
14	UKVFTA	Effective since May 01, 2021	Vietnam, The UK
15	RCEP	Effective since January 01, 2022	ASEAN, China, Korea, Japan, Australia, New Zealand
16	VIFTA	Negotiations commenced in December 2015, completed in April 2023. Officially signed on 25/07/2023	Vietnam, Israel
FTAs under negotiation			
17	Vietnam - EFTA FTA	Negotiations commenced in May 2012	Vietnam, EFTA (Switzerland, Norway, Iceland, Liechtenstein)
18	ASEAN – Canada FTA	Negotiations commenced in November 2021	ASEAN, Canada
19	Vietnam – UAE FTA	In the process of initiating negotiations	Vietnam, United Arab Emirates (UAE)

By the Center for WTO and International Trade