New Enterprise Law and Changes Related to State Management Over SOEs

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Overview of SOEs in Vietnam

- State Owned Enterprises play importance roles in Vietnam.
- SOEs still represent a significant part of industrial assets and produce a significant part of GDP (38% of GDP, 50% of country export, 70% of total tax revenue).
- At the end of 2005, Vietnam had around 5,000 State-owned enterprises (SoEs) with a combined capital accounting approximately for 60% of the total capital of all businesses in the country.
- Several SoEs have operated ineffectively with an average growth rate of 10 per cent in the past three years, compared to the private sector's 17 per cent rate.
- SOEs represent a major part of stock market capitalization.
- Equitization process has been speeding up for transforming SOEs in joint stock companies in almost all sector of economy.

Equitization of SOEs

	Total SOE	Equitized SOEs to 2005	SOEs plan to be equtize 2006-2010
1. Number of enterprises	5.175	2.732	2.443
2. Value of Capital (US$ Mil.)	30.000	11.000	19.000
3. Value of share sell to the public (75%)		8	14

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Overview of SOEs Corporate Governance

- The current strategy to improve the performance of SOEs includes: equitization (conversion into a Joint-Stock/Shareholding company), restructuring into a limited liability corporation (LLC), transferring, selling, contracting, and leasing.
- State retains a clear majority share and makes all management decisions. Although equity is available for private purchase, there is little evidence of much change in organizational management.
- Line ministries directly control management decisions through ownership rights, but the system has limitations from unclear responsibility, poor accountability, lack of transparency, and a poor incentive structure for efficiency.

Supervisory Rights Distribution (1)

- A major problem for SOEs is that the State's ownership is poorly defined with respect to direct responsibility and the share of authority.
- The enforcement of supervisory rights run by State organizations over the managers of the SOEs.
- Each of State entities has a specific right to control the management of the SOE, with the total number of rights different for each enterprise. These rights are general controlling mechanisms and not specified by the role of the organization.

Supervisory Rights Distribution (2)

- There is an immediate principle-agent problem with current system. With generalized supervisory rights distributed over several different line organizations, there is no coherent governing structure.
- Firm managers must follow a strategy of universal appeasement. Rather than seeking a resolution between conflicting demands, the mangers must try to make sure that each stakeholder organization feels that their specific interest is served.

Information Distortions

- There are distortions in the incentives to provide accurate information on targets and long-term growth.
- Specific profit targets are determined by managers of SOEs with approval by holding line organizations. With SOE managers having key inside information of the capabilities of their firm, they are able to create safe targets.
- In MPDF/IFC survey, 70% of SOE managers agreed that the approach was “to make no loss, and only a little profit.”

Risk incentive

- With limited possible returns from investment, the risk structure associated with financing production expansion projects or capital improvements is distorted.
- SOE competitiveness drops as equipment depreciates, and managers are unwilling to make investments in the technological advancements required to capture and hold market share.
- The growing technological gap vis-àvis international standards poses a particular problem with respect to SOE viability post-WTO accession.

MPDF's Initial Survey Findings (1)

- SOEs are still very dependent on various government agencies
  - nearly 40% of SOEs said that business targets are imposed from above
  - 62% agreed that SOEs do not have "real" owners
  - 66% said that "ask and give" is still common
  - 87% rated personal relationships with government agencies important
- SOE directors complain they have many responsibilities, but not adequate authority to run their companies according to market principles
- 77% said they experienced situations where the law allowed them to do something, but they could not in practice (eg. laying off workers)
- 70% agreed that the common approach of SOEs is "to make no loss, but only a little profit"

MPDF's Initial Survey Findings (2)

- State still holds a fairly large equity stake in most of equitised firms
- 55% of all equitised firms where the State still has equity. General Directors these firms were representing the government's remaining equity stake in the company
- The state still holds an equity stake has a negative effect on the firm
- Most equitised firms are still following the old (SOE) way of doing things

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Objectives of New Enterprise Law (2005)

- Vietnam currently has separate legal codes for State and private enterprises, known as the State Owned Enterprise Law and the Enterprise Law. These laws currently define Corporate Governance in Vietnam.
- The process of equitizing State Owned Enterprises is causing convergence in the two laws.
- Remove fragmentary and distinct application of the law system on enterprises by economic sectors. (Enterprise Law– 1999; Law on state owned enterprises– 2003 and Law on foreign investment in Vietnam– 1996).
- Set up an unified enterprise law and create an fair and favorable business environment for all kind of enterprise

Scope and Subject of Application

- 4 types of enterprise: Limited liability company, Shareholding company, Partnership and Sole proprietorship regardless of economic sectors (state sector, private sector or foreign invested sector).
- Create a new form of business organization that is sole member limited liability company whose member is an individual
- All State Owned Companies established under the Law on State Owned Enterprises 2003 shall be transformed to Limited Liability Company or Shareholding Company (must be completed in 4 years since July 1, 2006)

Enhancement of Coordination between State Bodies

- Requirement of information exchange between the business registrar and other bodies is enhanced.
- The business registrar is obligated to notify all information contained in the certificate of business registration to relevant state bodies, including the people’s committee at provincial and commune level.

Clear Distinction of Duties between State Management Bodies

- The Government is in charge of unifying state management over enterprises
- The government will appoint an agency with a role of coordinating relevant bodies and exercising state management over enterprises
- Responsibilities of respective ministry and people's committee at all level are clearly defined;
- The provincial people's committee is in charge of organizing and deciding on personnel of the business registrar in pursuant to the Government's regulations.

Reform of Mechanism of Exercising Rights of the Capital Owner

- Function of investor and that of administrative management is clear distinguished and defined
- Execution of rights given to the capital owner and the freedom of doing business of the enterprise is clearly distinguished.
- Rights and obligations of the capital owner is carried out united and centrally.
- Establishment of an agency which will exercise rights and obligations of the capital owner in the enterprise on behalf of the state.

Establistment of State Capital Investment Coporation (SCIC)

- On 20 June 2005, the Prime Minister issued Decision 151 to establish the SCIC as a special state-owned corporation. The State Capital Investment Corporation (SCIC) set to take capital ownership of several types of State-run companies.
- SCIC manage and invest State capital in State-owned one-member liability companies, other liability firms with more than two members, equitised enterprises and newly established joint stock firms .
- The SCIC has the power to make direct and indirect investments in Vietnam or abroad in any form or sectors. It can set up joint ventures with other investors, purchase assets of other enterprises, or trade shares, bonds and other financial instruments.
- The SCIC can mobilise domestic and foreign capital by borrowing, issuing bonds and issuing certain fund investment certificates.
- The SCIC is financially independent, with charter capital of 5 trillion dong (of which 1 trillion will come from the state budget, and the rest from those state-owned enterprises where the SCIC will be the representative of state capital.