TOWARD A WELL FUNCTIONING SECURITIES MARKET IN VIETNAM

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CALE Books

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FOREWORD

This book is a rich product of sincere study executed by Ms. Nguyen Thi Anh Van as a Ph.D. candidate at Nagoya University.

Vietnamese society is now moving fast toward a market-oriented economy. This movement is based on a determined policy of Vietnamese people and government. In order to accomplish that policy all the better, a fully-fledged securities market is needed urgently. Vietnamese people learned quickly what to do for it, having equipped necessary legal frame of securities regulation since 1998. But Ms. Van wants to learn much more about experiences of securities regulations in foreign countries, such as the United States or Japan. She calmly analyzes problems of Vietnamese securities regulations and securities market, having a passionate ideal in mind. Then, she arrives to abundant, realistic law-reform proposals toward a well functioning securities market in Vietnam.

This book is the first comprehensive and systematic legal academic research about Vietnamese securities regulation in the whole world. Ms. Van has had to face extremely difficult tasks---- to digest huge volumes of technical, complex legal texts in the field both inside and outside Vietnam, to draw out meaningful analysis from the standpoint of what is needed in Vietnam, and to compose solid and useful proposals for future Vietnamese law reform---- almost without any preceding academic research in this area. She achieved this task and completed her dissertation because of her exceedingly clear head and her devotion of heart and soul for three years from April, 2000 to March, 2003 at Nagoya University. The faculty of the Graduate School of Law, Nagoya University was happy to confer upon her the Ph.D. degree for this accomplishment in March, 2003.

Now, the Center for Asian Legal Exchange, Graduate School of Law, Nagoya University has decided to publish this Ph.D. thesis written by Ms. Nguyen Thi Anh Van as the first issue in the new CALE Books series.

I believe myself to be very fortunate to have been the academic advisor of such an intelligent, diligent, and charming Vietnamese young researcher. It was an enjoyable experience for me to learn through her study about vital changes in the Vietnamese legal environment. I am very pleased by the Center's decision to publish this Ph.D. thesis as the inaugural volume of CALE books.

I am sure readers of this book can get clear-cut understanding how Vietnamese people are endeavoring to achieve a transparent, fair and efficient securities market.

May, 2004

Michiyo Hamada
Professor of Law,
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I would like to extend my gratitude to the Japanese Ministry of Education, Science, Sports, and Culture (*Monbukagakusho*) for their sponsorship of my research, and to Hanoi Law University (HLU) for giving leave so that I could make a reasonably long stay at Nagoya University and could entirely devote my time to complete the research. I am also thankful to Professor Le Hong Hanh (from HLU), who channeled my research interest in the area of securities regulation as early as the regulation was coming into existence in Vietnam.

I am greatly indebted to the Foreign Student Adviser, Ms. Okuda Saori, for the advice and help I received from her from time to time, so that I could overcome difficulties during my stay in Japan. I am also grateful to the Law Library Staff for their kindness and patience in guiding me as to how to make use of reference materials and other library facilities when I fist came to the Graduate School of Law. Above all, I would like to thank my parents, my husband, daughter, and sisters, without whose continued love and support this thesis would never have been written.

May, 2004

Nguyen Thi Anh Van

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LIST OF ABBREVIATIONS

- ATSs: Automated Trading Systems
- CEO: Chief Executive Officer
- CFO: Chief Financial Officer
- CEPD: Council for Economic Planning and Development (Taiwan)
- CSRC: China Securities Regulatory Commission
- ECNs: Electronic Communication Networks
- EU: European Union
- HCMC: Ho Chi Minh City
- IASC: International Accounting Standards Committee
- IOSCO: International Organization of Securities Commissions
- LSE: London Stock Exchange
- NASD: National Association of Securities Dealers
- NASDAQ: National Association of Securities Dealers Automated Quotation
- NYSE: New York Stock Exchange
- OTC: Over the Counter
- PSE: Philippines Stock Exchange
- SEC: Securities and Exchange Commission (United States)
- SESC: Securities and Exchange Surveillance Commission (Japan)
- SIB: Securities and Investment Board (United Kingdom)
- SOEs: State Owned Enterprises
- SROs: Self-regulatory Organizations
- SSC: State Securities Commission (Vietnam)

TOWARD A WELL FUNCTIONING SECURITIES MARKET IN VIETNAM

INTRODUCTION

In the year 2000, Vietnam witnessed a remarkable event - the birth of the first securities trading center in Ho Chi Minh City.

In fact, the very first legal basis for the issuance of securities was created as early as 1990 by the passage of two legal texts, namely the *Company Act* and the *Ordinance on Banks, Credit Cooperatives and Financial Companies*. These laid the legal foundation for the establishment of shareholding companies and shareholding banks. In the following years, the government has continuously passed other legal rules, in the form of decisions and decrees that permit the issuance of shares and bonds by various legal entities. The texts implied an intention by the Vietnamese Government to erect a securities market for the country in face of the absence of a minimum legal framework for the operation of such a market at that time.

Such an intention was explicitly revealed in 1995 when the Preparatory Commission for the Establishment of a Securities Market was formed.[1] One year later, in 1996, the first market watchdog - the State Securities Commission (SSC) - was founded, with a mandate to establish and foster a securities market in Vietnam.[2] From the outset, the SSC was active in creating a legal framework for the birth of the stock trading centers - an initial step in promoting the formation of formal stock exchanges in the future. Immediately after the government had passed its *Decree 48/1998*[3] - the core legal rules for the operation of a securities market - the SSC issued *Decision 127/1998*[4] to enable the erection of securities trading centers and planned stock exchanges. Since the passage of these governmental level documents, various rules have been promulgated to give further guidance in connection with them. All of these make up the current securities regulation of Vietnam.

Although during the 1990s, a minimum legal basis for the formation and operation of the market had been available, a formal trading center could not be formed. The reasons for that lay in the shortage of commodities for the markets[5] and in the Asian financial crisis.[6] Thus, until the date the first trading center saw the light of day in July 2000, it had

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[1] See *Decree 361-TTg* dated June 20, 1995.
[2] See *Decree 75-CP* dated November 28, 1996.
[3] The full name of this legal text is *Decree 48-1998/ND-CP*, issued on July 11, 1998.
[4] The full name of this legal text is *Decision 127-1998/QD-TT*, passed on July 11, 1998.
[5] See "*Vietnam's First Securities Centre Expected to Open in 1999*" (Nov. 11, 1998) *ASIA PULSE*, <LexisNexis: Non-US News>; see also "*Vietnam to Delay Opening Hanoi, HCM City Stock Exchanges*" (Nov. 25, 1999). ASIA PULSE <LexisNexis: News Group File, All>.
[6] See "*Vietnam Stock Exchange Opening Delayed another Week*", (Jul. 3, 2000) *Deutsche Presse-Agentur* <LexisNexis: News Group File, All>; see also "*Vietnam Legal Update*", Part 4: Equitization Issues, http://www.phillipsfox.co.nz/publications, visited Oct. 5, 2000.

taken almost ten years since the adoption of the first legal bases for the issuance of shares in Vietnam.

To date, although the first securities trading center has only been operating for a short period, rules regulating various aspects of the markets have already been revised several times. A number of issues that need to be taken into consideration can still be found in the current securities regulation. Such issues lie in the information disclosure requirements, in the anti-fraud regulation, in the regulation of securities professionals and in the market structure, as well as in the management apparatus of the markets. Analyzing these problems and proposing possible solutions are the goals of this paper. To achieve such goals, the paper will be divided into seven chapters.

Chapter 1 includes an introductory discussion on the historical development of the economic system in Vietnam before and after the 1986 Open Door Policy in order to argue that a fully-fledged securities market is indispensable to economic development in Vietnam. First, that is because the increasing number of newly established enterprises in the last few years, and even the banking system, all demand a fully-fledged securities market as a means to enable them to be well financed. Secondly, a formal securities market is also required to provide market liquidity for shares, which in turn will speed up the equitization process. Thirdly, such a market will allow Vietnam to mobilize funds from both domestic and foreign savings.

Finally the chapter proceeds to an overall appraisal of the current securities regulations and draws out major problems that need to be dealt with to achieve a well operational market.

Chapter 2 to Chapter 6 have been designed to deal with a number of areas in securities regulations, where both existing and potential problems can be found. Problems that stem from the regulation, and also those that stem from the practical implementation of such regulation, will be carefully analyzed and evaluated in order to find out better forms of regulation for the newly emerging securities market in Vietnam.

Since information disclosure requirements and anti-fraud provisions are the most significant components of securities regulations, these will receive first and second priority amongst the problems needing to be dealt with in detail. Thus Chapter 2 argues that the current information disclosure regulation cannot guarantee that public investors will be adequately informed. The reasons are twofold. One is that the disclosure regime fails in ensuring the availability, timeliness, and adequacy of information. The other is that the regulation leaves a huge number of companies unregulated: companies whose securities offerings do not fall within the purview of the “public offering”, and non-listed companies. These shortcomings have led to the fact that a large pool of public investors has faced the danger of being uninformed.

Chapter 3 argues that the existing anti-fraud regulation cannot foster a fair and healthy market. That is because it cannot avert manipulative and deceptive practices while it deprives the market of instruments that support it well. It also fails to lay down concrete legal foundations for rights of action which would equip company shareholders with necessary measures to protect their own interests and those of their companies.

Furthermore, the sanctions against violations adopted by the regulation are not drastic enough to ensure that the regulation will be well enforced.

Regulation of securities professionals and the legal structure of the exchange market can be seen as the third and fourth most important amongst the said issues and will be discussed in Chapters 4 and 5. Chapter 4 studies the current regulation of securities professionals. It argues that the deficiencies in the regulation of conflicts of interest between securities firms and their customers will put public investors at risk, and that a strict segregation between banking and securities business is not always wise and right.

Chapter 5 examines the legal form of the Vietnamese exchange market in relation to those in other countries and their recent movements. It points out that the ownership structure of the current securities trading centers and the planned stock exchanges might not be appropriate in ensuring an effective market.

The management apparatus over the securities market will be discussed in Chapter 6. This chapter argues that Vietnam lacks an adequate regulatory system to enforce securities law; that in the absence of a self-regulatory system, a single and dependent public regulator cannot ensure that securities regulations will be well enforced.

Finally, Chapter 7 will sum up all the suggestions proposed in earlier chapters for improving the existing securities regulation.

While discussing these issues, a comparative approach will be employed from time to time, in order to find out acceptable solutions for Vietnam. As such, the paper will be presented as a comparative study between the above-mentioned legal issues in Vietnam and those in other jurisdictions such as the United State (US) and Japan. The ways such problems have been dealt with in these countries will be discussed. A question which might arise is that both these countries are much more advanced compared with Vietnam in terms of socio-economic circumstances, and possibly their legal cultures also differ from that of Vietnam, so why should they be chosen for comparison? Justification of this choice can be made, however, on at least the following two grounds.

First, it is well documented that today there has been a tendency towards a convergence of securities laws in various countries.[7] It seems hard for Vietnam to keep

[7] See Mark Gillen and Pittman Potter, "The Convergence of Securities Laws and Implications for Developing Securities Markets" (1998) 24 *North Carolina Journal of International Law & Commercial Regulation* 83, 95 – 109.

In this Article, the authors collect documentary and evidence that there have been a number of similarities between the securities laws of different countries; that a country's securities law often borrows statutory provisions from securities laws of other countries; and that the sources for borrowing seem to be very limited. In justifying such similarities and borrowings, the authors give a number of reasons: (1) the laws employ similar solutions since there are no more practical solutions than these; (2) wherever securities markets operate, similar interest groups that stem from the markets can result in political pressures that lead to similar laws; (3) competitive pressures to attract investment capital can also result in similarities in the laws; (4) pressures from the US regulators with respect to other countries where the US might seek to impose US style securities laws; (5) the geographical proximity of countries, the indifference in language, or close business or educational contacts; (6) and simple coincidences. The authors also maintain that the convergence of securities laws from different jurisdictions is an inevitable tendency, especially in the increasingly globalizing trend of securities markets around the world.

away from such a tendency. That is because the Vietnamese securities market will be isolated from and incompatible with other markets that are ready or approaching readiness for an increasingly globalizing trend if its law and regulation are not standardized and harmonized with the global tendency. This would also mean that the Vietnamese securities market will not be able to compete with other foreign markets in attracting financial resources for economic development in the country. Learning the way to develop a tailored set of laws regulating the securities industry from other countries will thus save time and energy for Vietnam in its law-making process.

Secondly, the two countries, US and Japan, have the most vibrant securities markets in the world.[8] These markets should be models for other countries, especially for those in the process of establishing and promoting a securities market. Here again another issue that might arise is that both the American and the Japanese stock markets are so big compared with that of Vietnam that it might not be appropriate to import regulatory experience from those two countries. However, one might also argue that securities markets, regardless of their size and location, often trigger similar interest groups, which might result in similar problems that need to be dealt with by law and regulation. For example, obviously investors in all big and small markets are all in desperate need of statutory protection from market abuses and fraud. That is because of the fact that, owing to their own interests: (1) issuing companies and listed companies tend to conceal material information that might be harmful to their reputation, which in turn might adversely affect their securities' prices; and (2) corporate insiders and securities firms tend to use their position of advantage in accessing inside information and in having better knowledge of the area, to enter securities transactions to the detriment of outsiders (in the case of insiders) and customers (in the case of securities firms). For these reasons, securities laws in most of countries often contain information disclosure requirements, antifraud provisions, and provisions for regulating conflicts of interest between securities firms and their customers.

Although the American and Japanese law reform experience will be frequently invoked in this paper, that is not its only source. Where it appears relevant to securities law reform in Vietnam, some other jurisdictions such as United Kingdom, Germany, Sweden, and Australia will also be visited. The aim of the comparative study is to contribute to the completion of the legal framework governing the securities market, which in turn can foster a well operational market for Vietnam in the future. Given that aim, more advanced jurisdictions seem to be a better choice for comparison than those that are at the same level as Vietnam. To speed up the improvement of the future market,

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See also Marc I. Steinberg, *International Securities Law: A Contemporary and Comparative Analysis*, (1st ed. 1999) 2-3. The author argues that in an expanding global marketplace, standardization of regulatory requirements among countries would strengthen investors protection; that creating greater harmony in a truly global marketplace is required.

[8] See Michael J. Scown, "Asia's Emerging Equities Markets" (1990), *East Asian Executive Report* 8, 8. In this article, it is reported that: "... before the 1990 market crash, the Japanese stock market was the largest in the world, with 40 percent of world capitalization, compared with 32 percent for the United State."

it may well be that nothing is more useful than learning from the experiences of those who have already succeeded in this area.

CHAPTER I
THE ECONOMIC SYSTEM AND THE NEED FOR A SECURITIES MARKET IN VIETNAM

I. AN OVERVIEW OF THE HISTORICAL DEVELOPMENT OF THE ECONOMIC SYSTEM IN VIETNAM

1. The Economic System before the Open Door Policy

Prior to 1975, Vietnam had undergone different foreign occupations and wartime destruction. Since 1955 the country had been separated into two parts:[9] the North and the South ruled by two opposite governments (Communist Party Government and American Colonial Rule, respectively). Since 1975, although the Country has been reunified, its post-war legacy was little more than the condition of an underdeveloped economy, as observed by economists:

> *For many years, our economy has landed in a serious crisis, a rapidly increasing inflation, a weak infra-structure, a big imbalance in economic structure and various difficulties facing the population in daily life.*[10]

Until 1986 the Vietnam economic system was a centrally-planned one. Production and consumption were subject to detailed plans approved by the government. They were not responsive to market demand. Market participants in the economy included two main components: cooperatives and state enterprises (*doanh nghiep nha nuoc*).

The former were the second most important component in the socialist economy after the latter. They consisted of small-scale saving and credit cooperatives, supply and marketing cooperatives, minor handicraft cooperatives and agricultural cooperatives.

The system of saving-and-credit cooperatives had been in operation since 1945 as a vehicle for collecting savings to support agricultural production. They mainly involved farmers, householders and small cooperatives, and were a means of supporting the population during the revolution of the Vietnamese people.[11] These cooperatives were

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[9] See "Lich su Viet nam" [Vietnam History], http://www.nhandan.org.vn/vietnamese/lichsuvietnam, visited Mar. 21, 2001.

[10] See Nguyen Van Luan, Tran Quoc Tuan and Ngo Minh Chau, *Thi Truong Chung Khoan o Viet nam* [*Securities Market in Vietnam*] (1995) 121. Hereinafter, Nguyen Van Luan (et al.). (All translations of Vietnamese texts quoted from books, articles, bulletin, and legal documents in this paper, unless otherwise noted, are of the author).

[11] Since 1951, when the National Bank of Vietnam (now the State Bank of Vietnam) was established, the system of saving and credit cooperatives has been put under its control. For further information, see Tran Duong, *Ba Muoi Nam: Tien te – Tin dung – Ngan hang 1951 – 1981* [*30 Years-Money-Credit-Banking in Vietnam 1951 – 1981*] (1981).

said to be rather strong during the colonial period and their success continued until the early eighties.[12]

The system of supply and marketing cooperatives was first set up in 1955 under the form of a collective trading enterprise in which farmers invested in shares involving their products. By 1962, this form of cooperatives had become widespread throughout the North of Vietnam. They were used to buy and sell agricultural products from the farmers and they also supplied farmers with products bought from state-trading organizations. At the present time, the number of successful supply and marketing cooperatives is quite small, since most of them have been liquidated or sold to private entrepreneurs.[13]

Minor handicraft cooperatives have been used as a component of government-guided strategies for industrial development since the first five-year plan (1961 - 1965). This kind of cooperative has the same organizational structure as supply and marketing cooperatives.[14]

By the time land reform was introduced, agricultural cooperatives had come into existence with government support. In practice, these were producers' cooperatives established in the place of individual farming.[15]

Later, some other types of cooperatives could be found, such as those engaged in transportation and construction work. It was reported that before the Open Door Policy was initiated, Vietnam had more than 30,000 industrial and handicraft cooperatives, 10,000 trading, 200 transportation and 500 construction cooperatives.[16]

The most important market participant (state enterprises), consisted of enterprises established by the government, and was expected to play a leading role in the economy. Their capital was fully funded by the government from the state budget on a non-refund basis. If any extra capital was needed during their lifetime, they could get loans from state-owned banks. Even with the loans from banks, the enterprises did not have to discharge their debts if they incurred a loss. In addition, they could enjoy many preferential treatments in doing business: they enjoyed a more advantageous tax system[17]

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[12] For more information, see Kirsch, Ottfried C.: "Vietnam: Agricultural Cooperatives in Transitional Economies", *Discussion Paper 59*, http://www.rzuser.uni-heidelberg.de/~t08/DISKUS59.html, visited Mar. 10, 2001.

[13] Ibid.

[14] Ibid.

[15] Ibid.

[16] For more information, see "Unable to Make the Big Leap, Cooperatives Face Extinction", *Vietnam Investment Review* (Hanoi) (January 1, 1995), http://www.hartford-jwp.com/archives/54/111.html, visited Mar. 10. 2001.

[17] Prior to 1990, the state-owned sector and other economic sectors were subject to two different collection regimes. First is a turnover and profit collection regime (the term "tax" was not used for the state-owned sector), applied to state enterprises. For example, the "Profits Distribution and Funds Formation Regime applying to State Industrial Enterprises" [Che Do Phan phoi Loi Nhuan trong Cac Xi nghiep Cong nghiep Quoc doanh] promulgated under *Circular 11.TC/CNA* dated July 22, 1986; the "*State Enterprises' Turnover Collection Regime*" [Che Do Thu Quoc Doanh] promulgated under *Decision 188/CT* dated Jun. 21, 1988. Second is a tax system that consisted of turnover tax, profit tax, agriculture tax, and commodities tax, imposed on non-state sectors. For example, the "Regulation of Industrial-Commercial Tax" was applied to cooperatives and households that engage in commercial and industrial business activities" [*Dieu Le Thue Cong Thuong Nghiep*] promulgated under *Resolution No. 200.NQ/TVQH*, dated Jan. 18, 1966. This Regulation was

compared to other business entities in other economic sectors; they had the right to access scarce resources; to have a priority position in export and import activities; to have monopoly power in a number of industries such as telecommunications, railways, transportation, banking and insurance. Furthermore, production and consumption were conducted according to plans designed by the government. The enterprises did not even have to think of the quality of goods they should produce in order to make their own markets. The government gave them consumers' addresses and they simply sold their products to those customers at a price already decided by the government.[18] Even if the enterprises did not complete the above-mentioned plan, directors did not incur any liability. In such circumstances, there were no incentives for state enterprises to conduct their business effectively. Consequently, loss-making enterprises were inevitable. By 1997, there were 5,800 state enterprises; but only 37% of these were said to be profitable. The unprofitable enterprises had debts about double their capital.[19]

Although state enterprises were expected to play a leading role in promoting economic growth, the management mechanism in a centrally planned economy did not generate expected outcomes.

The same can be said about financial markets, whose principal component was the monetary market. The other minor part of financial markets was the national construction bonds market. The bonds market consisted of issuing markets, which operated only when the government wished to raise more funds to meet budget deficits.

In monetary markets, market participants consisted of the National Bank of Vietnam (now the State Bank of Vietnam),[20] state-owned banks, credit cooperatives and socialist saving funds (*Quy tiet kiem xa hoi chu nghia*).[21]The state-owned banks were specialized banks operating in different areas (indicated by bank's name). For example, at this stage, there were two types of banks, namely the Construction Bank established in 1957[22] and the Foreign Trade Bank set up in 1963.[23]

In the centrally planned economy, the role of the banking system was to fulfill the capital allocation requirements of the economy. As such, there was no separation between the state management functions of the State Bank (the Central Bank) and the trading

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continuously revised throughout 1966-1989; and "Ordinance on Agricultural Tax of 1983" [Phap lenh thue nong nghiep].

[18] See: Nguyen Ngoc Vu, "Chinh sach tai tro doanh nghiep duoi tac dong cua thue va chi phi pha san" [Policy on Enterprise Subsidy under the Impact of Taxes and Bankrupt Expenses] (2000) 8, *Tap Chi Ngan Hang [Banking Review]* 52, 52. In this article, the author also mentions the production and consumption of the state enterprises in the centrally planned economy.

[19] See David O. Dapice (Harvard Institute for International Development), "Vietnam's Economy: Responses to the Asian Crisis", http://ase.tufts.edu/wts/writingfellows-econ, visited Dec. 24, 2000.

[20] In 1951, the National Bank of Vietnam was established under *Decree No. 15/SL* (signed by President Ho Chi Minh) dated May 6, 1951. In 1961 it was renamed the State Bank of Vietnam under *Decree No. 171/CP* dated October 26, 1961.

[21] The system of Socialist Saving Funds was set up as part of the State Bank of Vietnam to collect savings from individuals.

[22] Bank for Construction was formed under *Decree 177/TTg* dated April 26, 1957.

[23] Bank for Foreign Trade was set up under *Decree 155/CP* dated Dec. 30, 1962.

functions of the specialized banks.[24] Because of this feature of the banking system, it has been referred to as the one-tier banking system in Vietnam. In this system, the State Bank worked as a commercial bank and a central bank at the same time. It had branches and sub-branches located throughout the country, from municipal and provincial to district levels. The main tasks of such branches and sub-branches were to prepare and implement credit and cash plans at the direction of the government.[25] The specialized banks were actually mere branches of the State Bank and their operation was subject to direction from the latter.[26] Such direction designed detailed activities for the banks, including the specification of banks' borrowers and the determination of ceiling and floor interest rates. Banks could only provide loans for customers appointed by the government at an interest rate falling within limits also announced by the government. Financial transactions mainly occurred between those banks and other entities, namely state enterprises and cooperatives. Individuals were not allowed to open business accounts at banks, although they could borrow money from credit cooperatives to develop their household economy with a limited amount depending on each individual purpose. Deposit and lending rates varied depending on the purpose of borrowing or the legal form of the borrowers.[27] The lowest rates were often given to state enterprises. Banks' roles and functions, at this stage, were clearly designed to implement the government's economic policies, neither for making profits nor for actually enabling financial flow.

2. The Economic System after the Open Door Policy

In 1986, the *Open Door Policy*, or *"Doi moi"*,[28] was introduced in Vietnam, after the Sixth Communist Party Congress. The reform focused on a number of socio-economic policies. The most notable ones were: (1) ownership should be diversified to encourage non-state ownership and allow the non-state sector to establish businesses. Joint ventures between the state, cooperative and private sectors should also be permitted; (2) state

[24] See "Business Environment - Banking and Finance" http://www.vnn.vn/investment/business/busi_envi/bank_fina.html, visited Dec. 25, 2000.

[25] See *Decree 94 /TTg* dated May 27, 1951. This Decree was replaced by *Decree 171/CP* dated October 26, 1961 (hereinafter, *Decree 171/CP*). Under these two Decrees, the State Bank of Vietnam was responsible for the issuance and management of money and capital mobilizing-lending business.

Decree 163/CP dated June 16, 1977 (hereinafter, *Decree 163/CP*) although deprived of the State Bank of Vietnam's mobilizing-lending function, certified that the State Bank of Vietnam was a legal entity and an economic organization.

[26] See *Decree 171/CP* and *Decree 163/CP*.

After the passage of *Decree 65/HDBT* on May 28, 1986, legal personality of specialized banks was recognized for the first time; this Decree made a first step in separating the state administrative function of the State Bank and the trading function of specialized banks. This new direction was later again adopted in *Decree 53/HDBT* dated March 26, 1988, which gave the first legal foundation for the establishment of a two-tier banking system (see below, Section I.2 of this chapter).

[27] For example, to promote agricultural production, lower-interest-rate loans were often given to enterprises operating in this area - lower compared with those given to enterprises working in other areas; state enterprises could get loans with lower interest rates compared with those applied to cooperatives.

[28] This term means "New Deal".

enterprises should operate according to the so-called 'socialist accounting principles'[29]; (3) foreign investments should be encouraged. Favorable policies and incentives should be applied to Vietnamese living abroad and to foreigners, in order to attract their investment and business cooperation into the country; (4) prices should be liberalized. Under this new price policy, the economic system should be switched from administratively determined prices to market determined prices; (5) the financial system should be fundamentally reformed: central banking functions should be separated from those of the specialized banks; (6) official exchange rates should be adjusted from time to time so that they would closely reflect genuine rates.[30]

Such renovation aimed to switch the economy into a state-oriented market economy in order to promote economic growth. So far, the *Open Door Policy* has generated initially encouraging outcomes. It is reported that the Vietnamese social and political regime has been maintained whilst its economy has quickly been stabilized and restored. During 1993, its macro-economic indicators were stable; inflation had been severe, then dropped as low as 8.4% and the budget deficit was reduced. More surprisingly, Vietnam's economy has even been able to recover from the slowdown that followed the outbreak of the regional financial crisis. Statistics made within the first 6 months of 2000 show that economic growth increased by 6.2%, the highest rate during the last 3 years, industrial production grew up to 14.5%, and agricultural production reached a record of 16.7 million tonnes.[31]

In the law reform area, the departure point was December 29, 1987, when the *Act on Foreign Investment in Vietnam* (*Luat dau tu nuoc ngoai tai Vietnam*; hereinafter, *Foreign Investment Act*) was passed.[32] Under Article 4 of the current Act, foreign investors can do business in Vietnam under three forms: wholly-foreign-owned enterprises, joint ventures and business cooperation contracts. Article 2 of the Act gives definitions of three other types of contract into which foreign investors may enter to do business in Vietnam. Such contracts include Build-Operate-Transfer contracts (BOT), Build-Transfer-Operate contracts (BTO), and Build-Transfer contracts (BT). These contracts can be concluded between an authoritative Vietnamese state organ and a foreign investor.

It was the first time another economic sector - Foreign owners, rather than State and Cooperative ones - has been legally recognized in Vietnam. Shortly after that, the *1990 Company Act* (*Luat cong ty*) and the *1990 Private Enterprise Act* (*Luat doanh nghiep tu nhan*) were passed. These legal documents provided the newly-formed market economy

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[29] The so-called socialist accounting principles require state enterprises to operate on an economically and financially independent basis. In other words, state enterprises have business and financial autonomy.

Previously, state enterprises that made a loss could get further financial support from the government. Under the new socialist accounting principles, they can no longer depend on governmental financial support. Rather, they should make profits and have to be responsible for their own debts.

[30] See *Van kien Dai hoi Dang toan Quoc lan thu VI [Documents of the Sixth National Congress of the Communist Party]*, (1987) 42 – 56.

[31] See "Vietnam's Economic Renovation and its Main Achievements", *Main Macro-economic Indicators*, http://www.mafa.gov.vn:8080/Web+server/Economy.nsf, visited Mar. 17, 2001.

[32] This Act was revised twice, in 1990 and 1992, and then was replaced in 1996. The 1996 *Foreign Investment Act* was also amended in 2000.

some more new types of enterprises, by permitting the private economic sector to set up businesses under the form of shareholding companies, limited liability companies and private enterprises.[33] The *1999 Enterprise Act* (*Luat Doanh Nghiep*), which replaces the above-mentioned two statutes, has broadened market participation even further by the recognition of partnerships and single member limited liability companies. It can be said that since the *Open Door Policy* was initiated in Vietnam, market participants have been enriched by the recognition of a multi-sectoral economy in which all economic sectors are equal before the law. All companies, including state enterprises, now have to compete with each other to make their own markets in order to avoid bankruptcy. Production has been conducted subject to the market's demands, except for a number of state enterprises operating in some vital industrial areas[34] in which the government's control is needed for national security and defense reasons.

In the taxation sphere, a turning point occurred in late 1990 when various tax laws were enacted, such as the *Turnover Tax Act* (*Luat thue doanh thu*), *Profit Tax Act* (*Luat thue loi tuc*), *Special Consumption Tax Act* (*Luat thue tieu thu dac biet*), and the *Import-export Duties Act* (*Luat thue xuat nhap khau*). Since then, a single tax system has been adopted and applied to all business entities coming from different economic sectors.[35] This more or less created an equal business environment for business entities regardless of their ownership. Throughout the 1990s, the tax system had been progressively improved by the passage of a number of new tax laws and ordinances, and by the revision and replacement of other tax laws. [36]

Law reform concerning financial markets occurred in 1988 when *Decree 53/HDBT* dated March 26, 1988 was issued by the Government with the introduction of a two-tier banking system. In this system, the state administrative functions have been given to the State Bank of Vietnam, while the trading functions have been vested in specialized banks; and the specialized banks are no longer components of the State Bank of Vietnam, rather they have become independent legal entities.

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[33] It is necessary to emphasize that in Vietnam, the usage of the term indicating "business entities" has been changed from time to time in legal texts. Before 1990, the term "enterprise" was formally used in both governmental and ministerial legal documents. When the *Company Act* was passed in 1990, the term "company" was first formally used for shareholding and limited liability companies. But recently the National Assembly has gone back to the term "enterprise" when drafting and enacting the 1999 *Enterprise Act*. Thus, at present, all laws governing companies in Vietnam use this term. However, if one scrutinizes the Act, this term is not always used in an individual article, when referring to all types of enterprise. For example, the 1999 *Enterprise Act* uses the terms "limited liability company", "shareholding company" and "partnership company" while it uses the term "private enterprise".

[34] See Appendix No. 1, *Decree 50-CP* dated August 28, 1996 on "The Establishment, Reorganization, Dissolution and Bankruptcy of State Enterprises" for the List of Priority Areas where State Enterprises can be established.

[35] See above n. 17 for the difference between the old tax system and the new one.

[36] For example: the *Ordinance on High Income Earners' Tax* [*Phap lenh thue thu nhap doi voi nguoi co thu nhap cao*], and the *Ordinance on House and Land Tax* [*Phap lenh thue nha dat*] were passed in 1994 and 1991 respectively. The *Turnover Tax Act [Luat thue doanh thu]* and *Profit Tax Act [Luat thue loi tuc]* were replaced by the *Value Added Tax Act [Thue gia tri gia tang]* and *Corporate Income Tax Act [Thue thu nhap doanh nghiep]* respectively.

This Decree also created two other state-owned banks (apart from the Foreign Trade Bank and the Construction Bank, which was later, in 1981, renamed as the Investment and Construction Bank and then, in 1990, the Investment and Development Bank) namely the Industrial and Commercial Bank and the Bank for Agricultural Development (now Bank for Agriculture and Rural Development[37]). A few years later, the Bank for the Poor[38] and Bank for Housing Development in Cuu Long Delta[39] were also established, pushing the number of state-owned banks up to six.

In 1990, *Decree 53/HDBT* was replaced by the *Ordinance on the State Bank of Vietnam* (*Phap lenh Ngan hang nha nuoc Viet nam*) and the *Ordinance on Banks, Credit Cooperatives and Financial Companies* (*Phap lenh ngan hang, hop tac xa tin dung va cong ty tai chinh*). These Ordinances provided the market with more participants by permitting private and foreign sectors, apart from the state and cooperative ones, to carry out banking business. In 1997, these two ordinances were replaced by the *State Bank of Vietnam Act* (*Luat ngan hang Nha nuoc Viet nam*) and the *Credit Institutions Act* (*Luat cac to chuc tin dung*) respectively.

The *Credit Institutions Act* even takes a further step compared with that taken by the *Ordinance on Banks, Credit Cooperatives and Financial Companies* in diversifying the forms of credit organization. Banking business can now be carried out by different economic sectors: state-owned, cooperative-owned, foreign-owned sectors, and private sector[40] under the forms of banking and non-banking institutions.

The monetary market today is no longer confined within financial transactions that occur between banks and entities that belong to state-owned or cooperative-owned sectors. Rather it has been opened to all market participants from different economic sectors. The differentiation in interest rates based on the legal form of the borrower has also been abolished since 1989.[41] However, lending from state-owned banks to state enterprises still accounts for around 80% of all lending in Vietnam.[42] It is also noteworthy that interest rates have continuously been controlled by the government. In other words, credit organizations have to trade within the ceiling and floor interest rates announced from time to time by the State Bank of Vietnam. It is worth quoting the World Bank's observation:

> *In general, Vietnam's credit market is highly distorted as a result of subsidized and directed credit programs, including the priority given*

[37] See *Decision 280/QD-NH5* dated October 15, 1996.
[38] This bank was formed under *Decision 252/TTg* dated August 31, 1995, as a non-profit bank. Its operational purpose is to eliminate poverty.
[39] This bank was set up under *Decision 769/TTg* dated September 18, 1997.
[40] Since private credit institutions are not recognized under the *Credit Institution Act*, the private sector can only establish shareholding credit institutions. For further information, see Art. 12, *Credit Institution Act.*
[41] See Article 1.b, *Decision 39/HDBT* dated April 10, 1989 (promulgating "Policy on Deposit and Lending Interest Rates").
[42] See "Country Commercial Guides - FY 1999: Vietnam", Chapter VII: Investment Climate. http://www.state.gov/www.about_state/business/com_guides/1999/eastasia/viet99_07html, visited Mar. 22, 2001.

> *to loans to SOEs (state-owned enterprises: author added) and to various commodity programs for the purchase of rice and other crops for export.*[43]

This fact, together with the collapse of the system of the People's Credit Funds in the late 1980s and early 1990s, led to a lack of public confidence. It was reported that:

> *[T]he public keeps an estimated 45% of broad money as cash and over 50% of local business transactions are conducted outside of the banking system・・・ At present, there are only 10,000 individual bank accounts for a population of 77 million. Vietnam continues to operate largely as a cash economy.*[44]

In such a situation, public savings have not been able to be adequately mobilized. The banking system has missed a great financial resource which it should use for economic development. Capital needy businesses, in turn, have surely faced obstacles in looking for banking loans.

The other components of the financial market are non-organized credit markets (which have spontaneously been developed in rural areas). These markets have been operating outside the banking system, among individuals, and are often referred to as "underground credit markets".

Griffin and Keith's observation might be useful to sum up the situation of the financial market in Vietnam in the 1990s:

> *It is widely known that the banking system is inefficient and in need of reform・・・ Most domestic investment is self-financed or financed through informal credit arrangements; the capital market is underdeveloped and the commercial banking system plays a minor role in financial intermediation.*[45]

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[43] See "Advancing Rural Development from Vision to Action", http://www.worldbank.org.vn/rep7/visf003.html, visited Mar. 10, 2001.

[44] See "Vietnam Trade and Project Financing", http://www.tradeport.org/ts/countries/vietnam/financing.html, visited Dec. 25, 2000.

[45] See Griffin Keith, "The Management of Structural Adjustment and Macroeconomic reform in Vietnam", *Human System Management*, (1998) (Vol. 17) (Iss. 1). <Database: Academic Search Elite>, visited Nov. 22, 2000.

II. THE NEED FOR A SECURITIES MARKET IN VIETNAM

1. A Securities Market and Long Term Finance for Businesses

From an economic viewpoint, Vietnam is one of the poorest countries in the world.[46] Vietnam has been attempting to move away from this position for more than a decade, since the *Open Door Policy* was first introduced. The economic reform which has been carried out since then allows every economic sector to set up enterprises. As a result, the number of non-state enterprises has been rapidly increased.

It is estimated that within seven years from the passage of the 1990 Company Act, there were more than 35,000 companies and private enterprises[47] established in Vietnam. On average, over 5,000 companies and private enterprises have registered every year.[48] Especially since the day the *Enterprise Act* came into effect, the business climate has been improved. The proof is that the number of newly registered enterprises in 2000 almost equals the total number of enterprises established within the 9 years from 1991 to 1999. Within the first three months of the year 2001, an increasing tendency in the number of newly registered enterprises could still be seen. There were 4000 enterprises founded with a total registered capital of 4,400 billion Dongs. Such an amount of capital increase is 1.5 times the size of that recorded at the same time in 2000.[49] Among enterprises established in 2000, the number of shareholding companies (excluding equitized state enterprises), although accounting for only around 4% (compared with 44% for private enterprises and 51% for limited liability companies), is still bigger than the number of shareholding companies established in the previous 9 years (from 1991 to 1999).[50]

Those figures themselves show that the Vietnamese economy has been in need of a complete capital market to fully meet the financial demands of the newly formed enterprises. The increasing number of shareholding companies recently established once again shows the need for a fully-fledged securities market to enable those companies to raise funds from the public and create liquidity for their shares. This is to ensure that

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[46] See "1998 World Development Indicators CD-ROM", World Bank, http://web.acces.uiuc.edu/faq/faq.pdl, visited Mar. 16, 2001.

See also Norman Brown IV, "The Long Road to Reform: An Analysis of Foreign Investment Reform in Vietnam", (2002) 25 *Boston College of International & Comparative Law Review* 97, 99. In this article the author points out that Vietnam's economic and financial framework remains weak and underdeveloped.

[47] The term "companies" here refers to shareholding companies and limited liability companies which were established and operating under the 1990 *Company Act*.

The term "private enterprises" here refers to one-man-owned enterprises, which were established and operating under the *Private Enterprise Act* of 1990.

Both of the above-mentioned Acts were replaced by the 1999 *Enterprise Act* on January 1, 2000.

[48] See "Developments in Corporate Laws in Vietnam: Overview of Legislative Reforms in Vietnam", (Apr. 21, 2000) (Vision & Associates) *Mondaq Business Briefing*, <LexisNexis: Non-US News>.

[49] See Ministry of Planning and Investment: *"Bao cao tinh hinh mot nam thuc hien Luat doanh nghiep"* [*Report on One Year Implementation of the Enterprise Act*] delivered at the Governmental Meeting (March 28 - 29, 2001), 5.

[50] Ibid.

shares can be publicly issued, and that the repurchase and resale of such shares can be easily effected.

It can, however, be said that prior to July 2000, Vietnam did not have a securities market in a real sense. The principal way for business entities raising more funds was to borrow from banks. But even if the banking system had been very well functioning, its capability in providing long term financing would have been limited. This is because banks' financial resources rely mainly on customers' deposits which can change considerably, depending on customers' demands.

In practice, almost all shareholding banks in Vietnam have been facing financial constraints. They need to increase their charter capital. Some of them have gone public to meet their pecuniary needs.[51] Clearly, not only enterprises but also banks themselves have been looking for a securities market where long term financing can be accessed. In other words, an organized securities market has come to be desired by almost every type of business entity in Vietnam. As stated by Tran Dac Sinh, Deputy Director of the Securities Trading Center, "We needed to set up the stock exchange to mobilize capital".[52]

2. A Securities Market and the Promotion of the Equitization Process

Apart from their role in providing long term financing for enterprises, a full-fledged securities market was said to be necessary to speed up the equitization process since they facilitate the liquidity of shares issued by those equitized enterprises.[53] Faced with the problem of loss-making and ineffective state enterprises, since 1992 the Vietnam government had been conducting an equitization program on an experimental basis by the passage of the two legal texts, *Decision 202/CT*[54] and *Decision 203/CT*.[55] Then, four years later, a large-scale equitization program was carried out under *Decree 28/CP*.[56]

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[51] See Nguyen Tran Que (ed.), *Thi truong chung khoan: Phuong thuc hoat dong va kinh doanh [Securities Markets - Operational and Trading Methods]*, (1996), 234. Hereinafter, Nguyen Tran Que.

[52] See Paul Wiseman, "*Vietnam stock market sees low start, steady growth*", (Nov. 17, 2000) *USA TODAY*. <LexisNexis: US News, Combined>.

[53] See "Vietnam's Finance Minister says SOE Equitizations Must Go Faster", (Dec. 24, 1999) *ASIA PULSE*. <LexisNexis: News Group File, All>. Hereinafter, "Vietnam's Finance Minister says SOE Equitizations Must Go Faster".

[54] This *Decision* was signed on August 6, 1992, by the President of the Ministers' Council. The Decision promulgated "The Regulation of the Conversion of a Number of State Enterprises into Shareholding Companies on an Experimental Basis".

[55] This *Decision* was signed on August 6, 1992, by the President of the Ministers' Council. The Decision promulgated "A List of State Enterprises that will be Equitized". The Decision selected the first seven state enterprises for equitization on an experimental basis.

[56] This Decree was issued on May 7, 1996, promulgating "The Regulation of the Conversion of a Number of State Enterprises into Shareholding Companies".

Decree 28/CP was later revised by *Decree 25/CP* dated March, 26, 1997, and in 1998 both of these Decrees were replaced by *Decree 44-1998/ND-CP* dated June 29, 1998 (promulgating "The Regulation on the Conversion of State Enterprises into Shareholding Companies"), hereinafter, *Decree 44/1998*.

Article 2 *Decree 44/1998* defined the goals of the equitization program: (1) to mobilize capital from the public, transfer technology, create jobs, develop enterprises, enhance competitive capability and reform

The latest legal rules that govern the equitization of state enterprises has recently been released under *Decree 64/2002*.[57] The Decree states the goals of the equitization program. First, the program aims to enhance the effectiveness of and competitiveness amongst enterprises; and to diversify enterprise ownership, and to improve enterprise governance so that enterprise assets and those of the state will both be used effectively. Second, the program aims to mobilize both domestic and foreign savings in order to modernize technology and promote enterprise development. Third, the program is designed to strengthen the oversight of investors over the enterprises and to harmonize the interests of the state, enterprises, and investors.[58]

Decree 64/2002 does not explicitly classify state enterprises for the purposes of equitization as its predecessor, *Decree 44/1998*, did. Rather it defines four ways for equitization, as follows. By the first way, the whole capital the state has invested in enterprises is to be maintained while new shares will be issued to raise more funds for the future equitized enterprises. The second way allows the sale of part of the capital the state has invested in enterprises. The third way permits the sale of the whole capital the state has invested in enterprises. The fourth way combines the second or the third way of equitization with the issue of new shares.

Vietnam has thus been in the process of the equitization of state enterprises for a decade. The equitization might promote the development of the securities market by providing them with more commodities. However, the equitization cannot go smoothly in the absence of an organized market, since there will be no market place that enables the liquidity of such special commodities. The problem would be more serious when a large number of state enterprises is equitized. Then, the absence of a formal securities market will make it even more difficult for shares to continue to be purchased and sold. For the time being, the problem has not yet arisen, because of the modest number of equitized enterprises. It is estimated that by December 1999 the number of state enterprises throughout Vietnam that had been equitized was 167. This figure accounts for only 40% of the 1999 target and shows the slow speed at which the equitization program has progressed.[59]

Of course, a fully-fledged securities market is not the only factor that can promote the equitization program. Some other factors include the government efforts in speeding

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enterprises' structure; and (2) to create opportunities for employees to become the company owners, to reform company management mechanism, and so on.

State enterprises fell into three categories for the purpose of equitization. The first category consisted of not-for-profit enterprises operating in some specified areas shall not be equitized. The second consisted of enterprises to be equitized, but after being equitized, the State must be a controlling shareholder of each enterprise. The third consisted of enterprises that need to be equitized or converted into other types of ownership. In this group, the government need not be a controlling shareholder. For further information, see Appendix, *Decree 44/1998*.

[57] This Decree was issued by the Government on June 29, 2002 and has come into force since the 15th day after the issuing date.

[58] See Art. 1.

[59] For further information see "Vietnam's Finance Minister says SOE Equitizations Must Go Faster", above n. 53.

up the program, the willingness of the incumbent managements of state enterprises in implementing such a program, and so on. However, one cannot deny positive impacts generated by the existence of a formal securities market on the success of the equitization process.

3. A Securities Market and the Mobilization of Funds from Domestic and Foreign Savings

A formal securities market is necessary for the development of a newly emerging market economy. It gives more possibilities for investment projects to be funded, which are, in turn, able to expand the industries. It broadens the chances for local companies to raise funds by having access even to household savings. As noted by economists:

> *As for an underdeveloped economy in Vietnam, economic growth and development mean industrialization and modernization for the country. Capital demand has thus been increasing day by day. This demand calls for medium and long-term financing provided by special institutions, one of which is a securities market. An organized securities market will quickly promote capital mobilization, which in turn will promote the industrialization of the country.*[60]

In addition, such a market can even play a significant role in creating opportunities for the economy to mobilize capital from foreign savings. As early as just after the *Open Door Policy* was initiated, the *1987 Foreign Investment Act* was passed, with generous incentives to attract foreign direct investment (FDI), an external financial resource, into Vietnam.[61] However, the Act and even the current *Foreign Investment Act* can only activate one of the channels through which foreign capital (FDI) can be invested into Vietnam. Another potential channel, a formal securities market, for capital flow into the

[60] See Nguyen Van Luan (et al.), above n. 10, 124.

[61] The *Foreign Investment Act* of 1987 gave generous tax incentives to foreign investors. Enterprises with foreign invested capital could enjoy lower tax rates compared with those applied to domestic enterprises. For example, profit tax rates applying to foreign invested enterprises were 15% and 25% (see Art. 26) (these figures can be contrasted to 30%, 40% and 50% profit tax rates applying to domestic enterprises: see Art. 10, the *Profit Tax Act* of 1990). Where foreign investors reinvested part of profits derived from their business conducted in Vietnam, they were entitled to profit tax refund corresponding to the amount of tax which was already paid for the profits reinvested (see Art. 32). Foreign invested enterprises were also able to enjoy other tax incentives such as tax holidays, tax reduction and so on (see Art. 27).

The current foreign investment law still offers favorable treatment to foreign invested enterprises. The *Foreign Investment Act* of 1996 (as amended in 2000) gives tax exemption and reduction to foreign invested enterprises (Art. 21a). Loss incurred by a foreign invested enterprise in the current financial year can be deducted from the enterprise's assessable income of the following fiscal year (Art. 40). Facilities and machines that are imported to constitute immovable assets of foreign invested enterprises are also exempted from import tax (Art. 47.2). See also *Decree 24/2000-ND/CP* dated Jul. 31, 2000 (guiding the implementation of the Foreign Investment Act) Arts. 55, 57; and see *Circular 13/2001/ TT.BTC* dated Mar. 8, 2001 (guiding the implementation of the regulation of taxes with respect to foreign invested enterprises), Section II.

country from foreign sources had been missing. Obviously, not all foreign investors seek to invest their money by running a business themselves. Rather, many of them look for an indirect way of investment through which their money can generate profits through dividends or interest derived from corporate shares or bonds they own. In such a case, a formal securities market will be an ideal place for them to realize their investment desires, since the purchase, sale, and repurchase and resale of shares and bonds can be effected. In the absence of such a market, the country apparently misses a significant external financial resource, which would otherwise be mobilized for economic development.

III. THE DEVELOPMENT OF SECURITIES REGULATION IN VIETNAM

1. The introduction of securities regulation

The starting point for the development of securities regulation, as mentioned earlier, can be traced back as early as 1990 when the first *Company Act* and the *Ordinance on Banks, Credit Cooperatives and Financial Companies* were adopted, with the recognition of shareholding companies and shareholding banks. Then in 1992, the government made a further effort in issuing *Decision 203/CT*, pursuant to which the first group of seven state enterprises was singled out for conversion into shareholding companies through the sale of equity.

In 1994, a considerable number of legal documents concerning the issuance of securities were passed. Started in July 26 when the government passed *Decree 72/CP*, according to which the issuance of three types of government bonds (treasury bills whose term is less than one year to maturity; treasury bonds which mature after one year; and project-finance bonds whose term is more than 5 years) was initiated. Then in September 17, the government issued a second regulation (*Decree 120/CP*) under which state enterprise bonds and shares could be publicly offered.

In the same year, the State Bank also passed some legal instruments to enable the issuance of State Bank Bills (*Decision 211-QD/NH1* dated September 22, 1994) and the issuance of bonds and shares by commercial banks (*Decision 212-QD/NH1* dated September 22, 1994 and *Decision 275-QD/NH5* dated November 7, 1994, respectively).

In 1995, markets for bidding and for repurchase and resale of Treasury Bills and bank bills were established under *Decision 88-QD/NH9* dated March 28, 1995 and *Decision 89-QD/NH9* (on the same date), issued by the State Bank.

Although, up to this stage, a formal securities market had continuously been absent in Vietnam, nevertheless the primary securities market was broader than that which had been operating before the introduction of the *Open Door Policy*. On such a securities market, the issuance of government bonds, company shares and bonds and bank bonds as

conducted.[62] Although the primary market existed, a number of problems still remained. The principal ones were:

(1) There was a lack of an adequate information disclosure regime. Enterprises that sought to issue shares and bonds had to apply for an issuing license from the Ministry of Finance (MOF). They had to file the following documents with the MOF: a letter of application; the enterprise charter; a proposed business plan; the financial statements of the most recent three years; and the proposal of the issuance. After getting the issuing license from the MOF, they merely had to announce on public media some information concerning the future issuance, such as number of shares or bonds going to be issued, their nominal value, time, and venue for the issuance, and rights of the securities holders.[63] There was no provision saying that either the issuers or the MOF would be responsible for disclosing further information that could affect the securities' price; nor was there any provision saying that continuous and timely disclosure of information was required.
(2) There were neither anti-fraud provisions to prevent misconduct on the market, nor any specific provision to handle violators of the regulation of such a primary market.
(3) There was a shortage of professional intermediaries such as brokers and dealers for offering and distributing securities.[64] Securities were often issued through the State Treasury, commercial banks and financial companies, or were even issued by the issuing enterprises themselves.
(4) Although there were legal bases for the issuance of company shares and bonds and government bonds, as earlier mentioned, it was reported that in practice most of the securities issued were short-term bonds whose terms were less than one year.[65]

The intention of the Vietnamese government to set up fully-fledged securities markets was expressly revealed in the middle of 1995, when the Prime Minister issued *Decision 361/TTg* to form a Preparatory Commission for the Establishment of a Securities Market. The Commission's task was to study and to draft proposals on the establishment and development of a securities market in Vietnam. Then the year 1996 marked an important event, the establishment of the State Securities Commission (the SSC - the public regulatory authority over securities markets) under *Decree 75/CP*.

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[62] Legal bases for this market, as earlier mentioned, had been continuously released since the early 1990s. Recently some of these documents have been replaced. For example: the 1990 *Company Act* was replaced by the 1999 *Enterprise Act*; *Decree 72/CP* was replaced by *Decree 01/2000/ND-CP* dated Jan. 13, 2000, promulgating "The Issuance of Government Bonds".

[63] See *Circular 91-TC/KBNN* dated Nov. 11, 1994 ("Provisional Regulation of the Issuance of Shares and Bonds of the State-owned Enterprises"), Parts I.12, II.12, & II.14. Hereinafter, *Circular 91-TC/KBNN*.

[64] See for example: Art. 9, *Decree 72/CP*: this Article said that government bonds can be issued through the State Treasury and commercial banks, financial companies and insurance companies; Art. 30, *Decree 120/CP*: this Article vested in the State Bank of Vietnam a right to guide commercial banks and financial companies in acting as agencies for issuing company shares and bonds; Parts: I.15.1 and II. 15, *Circular 91-TC/KBNN*.

[65] See Nguyen Tran Que, above n. 51, 232.

Two years later, in 1998, a basic legal framework for the operation of securities markets, *Decree 48/1998*, and a legal foundation for the establishment of stock trading centers and the planned stock exchanges, *Decision 127/1998*, were issued on July 11, 1998. These governmental legal instruments, together with various decisions and circulars issued by the SSC since 1998 to date, have created the current securities regulations in Vietnam.

Decree 48/1998 regulates public offerings and the trade of listed securities. Private offerings and the trade of non-listed securities are not subject to this Decree.

It can be said that all lawmaking activities throughout the 1990s have showned the government's efforts in preparing necessary conditions for the birth of a formal securities market in Vietnam. Those efforts were finally realized on July 20, 2000, when the first Securities Trading Center was put into operation in Ho Chi Minh City.

2. An Overall Appraisal of the Cornerstone of the Securities Regulation: *Decree 48/1998*

The cornerstone of the securities regulation, *Decree 48/1998*, was drafted based on experience learnt from various jurisdictions such as US, Japan, Britain, Germany, France, Hong Kong, Korea, and China.

Because of the complexity of activities conducted in securities markets, usually in countries that have seen a long historical development of such markets, each group of activities is often governed by a separate act. For example in the US, securities laws consist of different acts cover different areas such as *Securities Act of 1933*, *Securities Exchange Act of 1934*, *Investment Company Act of 1940*, *Investment Advisers Act of 1940* and so on. In Japan, various laws compose securities laws: *Securities and Exchange Law of 1947*, The *Law on Foreign Securities Companies of 1971*, The *Law on Trading in Financial Futures of 1987*, and so on.

In Vietnam, the situation seems to be quite different. The highest body of law setting out the general legal framework for the operation of securities markets is *Decree 48/1998*, a governmental legal rule. This Decree covers almost every aspect of securities markets from the regulation of public offerings, of securities professionals and the participation of foreigners in securities markets, to the regulation of abusive market practices and the state management of securities markets. It is necessary to reemphasize that in some areas, the Decree merely gives general principles, and as such, more detailed guidance will be found in subordinate legislation issued by the SSC.

The Decree was designed to embrace four main goals. First is to create a favorable environment for the issue and trade of securities. Second is to promote the mobilization of internal and external long-term financial resources. Third is to ensure that the securities market operates in an orderly way, safely, publicly, fairly and effectively. And the fourth is to protect the lawful interests of investors.[66] With such objectives, the Decree was divided into 11 chapters, covering 83 articles.

[66] See *Decree 48/1998*, second paragraph.

Chapter I, titled "*General Provisions*", sets forth the scope of the regulation and defines terms used in the following chapters. Although the chapter was designed to clarify necessary key terms, definitions of a number of important terms are still missing.

Chapter II, titled "*Public Offerings of Securities*", is expected above all to give a series of requirements concerning information disclosure imposed on issuers before going public for fund raising. However, the chapter has failed to tell issuers that information disclosure is the most important thing to do before a public offering can be conducted. Although information disclosure is mentioned several times in the chapter,[67] the language of such provisions cannot give the impression to the public that information disclosure is significant and should be made before and even after the issue of securities - to disclose information continuously during the time the securities are in circulation.

The chapter concentrates on certifying that all public offerings of securities to be listed on a formal trading center must get approval from the SSC[68] after going through a certain procedure provided by the Decree;[69] that those who seek to make a public offering of securities must meet a number of threshold;[70] and that securities distribution must be done through specified methods in a specified term. The chapter also emphasizes some administrative measures that can be employed during a public offering, such as to postpone a distribution and to withdraw an issuing license.[71]

Chapter III identifies the stock trading centers and the planned stock exchanges. The government clearly reveals its intention first to set up trading centers, later to be replaced by stock exchanges.[72] Some remarkable points in this chapter include: the recognition of a state-owned form of stock trading centers[73] which might exist until they are replaced by the stock exchanges in the future; the uncertain legal structure of the planned stock exchanges;[74] the silence of the Decree on certifying whether or not both the stock trading centers and the planned stock exchanges are self-regulatory organizations.

Chapter IV codifies securities firms. It spells out a number of conditions to be met[75] and the procedure that needs to be followed[76] in order to set up a securities firm. It also lays down criteria imposed on[77] and procedure followed by securities firms' affiliates[78] to obtain a practicing license. Rights and duties of securities firms[79] and some administrative

[67] See Arts.: 12, 13, 18, 19.
[68] See Art. 3.1. The ambiguity of this statutory provision will be discussed in Chapter II, Section III, Sub-section 1 of this paper.
[69] See Art. 11.
[70] See Arts. 6, 8 & 7.
[71] See Arts. 15 - 16.
[72] See Art. 20.
[73] See Art. 21.
[74] Article 23 although provides for the stock exchanges, does not spell out their form of ownership. It is unclear whether stock exchanges will be owned by the state or by public or by exchange members.
[75] See Art. 30.
[76] See Art. 32.
[77] See Art. 40.
[78] See Art. 41.
[79] See Art. 38.

measures that might apply to such firms and their associates[80] are also included in this chapter. Furthermore, the chapter clearly requires credit institutions, insurance companies, and general corporations (tong cong ty) to set up their own subsidiaries in the form of securities firms to trade in securities.[81] Chapter IV, however, does not properly deal with conflicts of interest issues. This is of importance to ensure that public investors are adequately protected.

Chapter V designs a legal framework for the establishment and operation of investment funds and fund management companies. It explicitly states the parties that are necessary for setting up a securities investment fund (a fund management company, a supervisory bank and investors).[82] It also provides for the conditions[83] and procedures[84] for establishing an investment fund, a fund management company and a supervisory bank. Rights and duties of these entities, as well as right of investors, are also stipulated in this chapter.[85]

Chapter VI, titled "*Registration, Clearing and Securities Custody Services*", merely gives general principles for these services, such as the contents of such services; conditions being met by securities firms that provide the services; and the way in which customers' assets are to be managed by those firms.

Chapter VII lays down provisions concerning the participation of foreigners and foreign entities in the securities market. According to this chapter, foreign organizations and individuals can take part in the Vietnam securities market by purchasing, selling, and trading securities. Where they seek to engage in securities business, they will have to establish a join-venture with a Vietnamese partner and obtain a business license from the SSC.[86] Foreign investment funds that are seeking to invest into Vietnamese securities markets can do so after getting an approval from the Prime Minister and then a license from the SSC.[87]

Concerning the percentages of securities that can be held by foreign investors, there are a number of conflicts. Such conflicts will be mentioned while discussing the state enterprise law in relation to the operation of securities markets.[88]

Chapter VIII, titled "*Prohibited and Restricted Activities*", establishes regulation of abusive market practices, takeovers and mergers. Takeover and merger can be effected provided that those who engage in such transactions are subject to some statutory requirements such as reporting to the stock trading center and holding a public tendering in accordance with the SSC rules.[89]

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[80] See Arts. 39 & 43.
[81] See Art. 29.1.
[82] See Art. 44.
[83] See Arts. 45 & 55.
[84] See Arts. 51, 46 & 55.2, respectively.
[85] See Arts. 47, 56 & 57.
[86] See Art. 67.1.
[87] See Art. 67.3.
[88] See Section I, sub-section 3 of the Appendix.
[89] See Art. 74.

Abusive market practices are dealt with in a simple manner. The chapter merely lists prohibited activities. It either does not properly deal with some activities or over-regulates other activities. Short-swing trading, for example, remains unregulated while other activities like short selling and margin trading seem to be over-regulated.

Chapter IX is titled "*The State Management of Securities and Securities Markets*". According to this chapter, the right to manage securities markets is vested in the government. The SSC is a state organ that plays the state management role on behalf of the government. Other ministries, governmental organs and the people's committees at provincial and municipal levels are responsible for cooperating with the SSC in carrying out the state management functions in the field of securities markets and within their own duties and rights.[90]

Although the SSC is authorized to oversee securities market in this chapter, its structure, personnel, and concrete rights and duties are not specified. To have an entire picture of the SSC, one will have to look at Decree 75-CP.

Chapter X gives a legal basis for "*Inspection, Supervision and Sanctions for Violations*". This chapter specifies those who are subject to the inspection and supervision of the SSC.[91] It also specifies the state organs that are responsible for disputes resolution.[92] Concerning sanctions for violation, it merely lists different levels of sanction and seems to leave such sanctions to be dealt with in detail by other governmental rules.[93]

Finally, like any legal document, the last chapter, Chapter XI, contains "*Implementation Provisions*". Such provisions concern the date of effect of the Decree; the responsibilities and obligations of the head of the SSC and those of other ministries in guiding the implementation of the Decree.

More detailed guidance for most of the chapters of *Decree 48/1998* is released in the form of circulars or decisions issued by the SSC. Nevertheless, this does not adequately make up for the above-mentioned weaknesses in the Decree.

Synopsis

In summary, it can be said that the current securities regulations show a significant and initial step in establishing and facilitating an organized stock market in Vietnam. However, since this was the first time when such a regulation was created, deficiencies have been inevitable. A number of issues that lie in both the current securities regulations and relevant laws need to be reconsidered to ensure a transparent, fair, effective and reliable market.

This paper proposes to deal with major problems of the current securities regulations. In the following chapters, the five main themes that will be discussed are:

[90] See Art. 75.
[91] See Art. 78.
[92] See Art. 79.
[93] See Art. 80.

(1) Information disclosure requirements in relation to a transparent market;
(2) Anti-fraud provisions and a fair market;
(3) Regulation of securities professionals in relation to a healthy market;
(4) Legal structure of exchange market and a well organized market; and
(5) Market regulatory apparatus in relation to enforcement issues.

CHAPTER II
WHETHER THE INFORMATION DISCLOSURE REQUIREMENTS PROMOTE GOOD INFORMATION FLOW

Information disclosure is one of the most significant components of the securities regulations and one of the most critical statutory issues for the protection of investors. For those reasons, this chapter will discuss the current information disclosure regime in order to find out what should be done to ensure a transparent market, which, in turn, can strengthen investor protection. It argues that the disclosure regime fails to ensure that public investors are adequately informed.

Before discussing the information disclosure regime, it may be helpful to have a quick look at the public offering process in Vietnam, and also the way in which issuing companies are listed in a trading center. The reasons are twofold. First, public offering and listing procedures adopted in Vietnam are quite distinct. The former can only be done if the issuers obtain an issuing license from the SSC - which sounds stricter than what is adopted elsewhere. The latter seems to be accomplished either in a lenient or in a strict manner depending on the filing date[94] of listing documents with a trading center.[95] Secondly, both public offering and listing trigger company duties in information disclosures. To have a clear idea of what an issuer and a listed company are required to do to discharge such duties, a pre-understanding of statutory public offering and listing is thus required.

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[94] The later filing date seems to be the more difficult procedure an issuing company has to face in order to become a listed company. For further information, see Section I, Sub-section 2 of this Chapter.

[95] Usually in other countries the issuers merely file a registration statement to the state authority in order to execute a public issuance (there is no need for a license) and to have their securities listed on an exchange, the issuers will have to apply at the exchange and must get approval from it. The US and Japan are examples where the requirements are almost the opposite to those in Vietnam.

Pursuant to *Securities Act of 1933* s 5, 15 USC s 77e (2002), no securities may be offered or sold to the public unless registered with the SEC.

Securities and Exchange Law of 1948 (2001 Japan) Article 4 also says: "*A public offering or public selling of a security (・・・) shall not be made unless the issuer has made registration with the Prime Minister for the public offering or public selling of a security・・・*"

However, in order to be listed on an exchange, for example NASDAQ Japan Market, the issuer will have to file a listing application which will go through a listing examination before getting approval. In such an examination, the soundness of corporate management, the adequacy of disclosure of corporate information, and others such as the status of the parent company, status of any business activities which are against public interests, will be looked into. For further information, see *Osaka Securities Exchange: Fact Book 1999*, IV.

I. PUBLIC OFFERING AND LISTING PROCESS UNDER THE CURRENT SECURITIES REGULATION

1. Public Offering

Public offering of securities is the offer for sale of securities that meet some statutory thresholds concerning (1) the amount of equity capital or debt capital of a company held by the public; and (2) the number of outside investors that purchase such amount. According to such thresholds, the issuer has to sell at least 20 percent of the equity capital/debt capital to more than 100 outsiders. Where the equity capital/debt capital exceeds 100 billion Dong, then, at least 15 percent of the equity/debt capital has to be sold to more than 100 outside investors.[96]

Under the current securities regulation, public offerings of securities has to be licensed by the SSC, except for the issuance of government bonds.[97] However, not all of the issuers can be licensed; only those who meet a number of specified criteria are eligible to apply for such a license. These criteria include:

> *(1) The issuer shall have at least 10 billion Vietnamese Dong chartered capital;*
> *(2) The issuer has made profits in the last two consecutive years;*
> *(3) The Management Board's members and director of the issuer must have experience in business management;*
> *(4) The issuer shall have a feasible proposal to use funds raised by the stock issuance;*
> *(5) The issuer shall have at least 20% of equity capital held by more than 100 outside investors;*
> *(6) Founding shareholders of the issuer shall hold at least 20% of the equity capital of the issuer within three years from the date of completion of the issuance;*
> *(7) The issuer shall have an underwriter for the issuance if the total value of issuing shares exceeds 10 billion Vietnamese Dong.*[98]

Issuers that meet the above-mentioned conditions are required to file an application dossier[99] to the SSC for an issuing license. There are two different sets of

[96] Pursuant to Article 2.2, *Decree 48/1998, "[p]ublic offerings are the offers for sales of transferable securities that meet requirements prescribed in Articles 6.5 and 8.2 of this Decree"*. Articles 6.5, and 8.2, *Decree 48/1998* lay down requirements concerning the amount of equity capital or debt capital of a company held by the public and the number of company outside investors.
[97] Ibid, Art. 3.
[98] Ibid, Article 6.
[99] In Vietnam, the term "application dossier" instead of "registration statement" is employed. Probably this is because Vietnamese issuers cannot simply be registered but must get a license from the SSC in order to make a public issue of securities.

dossier required for shares and bonds offerings. To get shares publicly issued, the application dossier must include:[100]

> *A letter of application;*
> *A public-notarized copy of the establishment license/decision;*[101]
> *A public-notarized copy of the business registration certificate;*
> *The company charter;*
> *A general shareholders meeting's resolution approving the stock issuance;*
> *The company-profile notice (ban cao bach);*[102]
> *A list of the members of the management board and director (or general director);*
> *The audited financial statements of the last two consecutive years;*
> *Minutes of the company's asset assessment done by a competent state authority (if the issuer is an equitized state enterprise);*
> *An undertaking to underwrite the issuing shares (if available).*

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[100] See *Decree 48*, Art. 9.1; see also *Circular 02/2001/TT-UBCK* dated September 28, 2001 (hereinafter, *Circular 02/2001*), Section IV. 1.

[101] This document is required by *Circular 02/2001* but not by *Decree 48/1998*. Since the effective date of the *Enterprise Act*, enterprise incorporators have not been required to obtain an establishment license. Nowadays they only need a registration certificate to commence their businesses. Perhaps *Circular 02/2001* refers to issuers that are state enterprises in equitizing process.

[102] The original Vietnamese text uses the term "ban cao bach", whose precise meaning is "prospectus". Because the term "prospectus" employed in the Vietnamese text denotes a component of the registration dossier, filed with the SSC, this might confuse foreign readers. Therefore, in this paper, the term "ban cao bach" will be translated as "*company-profile notice*"; only when "ban cao bach" is made available for public reference, then the term "prospectus" will be used.

In the US, the term "prospectus" means a notice, circular, advertisement, letter of communication, which offers any security for sale or confirms the sale of any security [see *Securities Act of 1933* s 2 (a) (10), 15 USC s 77b (2002)]. A prospectus must contain specified information (but not all the information) found in the registration statement filed with the SEC [see *Securities Act of 1933*, s 10 (a) (1), 15 USC s 77j (2002)]. The prospectus must be available for public investors' reference as soon as the relevant securities are eligible to be publicly offered for sale (or during post effective period) [see *Securities Act of 1933* s 5, 15 USC 77e (2002)].

In the literature, the term "prospectus" is, however, sometimes referred to as a component of the registration statement. Alan R. Palmiter writes: "*The registration statement is typically prepared by company counsel. Part I contains the prospectus; Part II contains supplemental information, signatures, and exhibits.*" For more information, see Alan R. Palmiter, *Securities Regulation: Example and Explanation*, (1998), 88 & 87. Hereinafter, Alan Palmiter.

David L. Ratner also writes: '"*The registration statement" consists of two parts: the "prospectus", a copy of which must be furnished to every purchaser of the securities, and "Part II", containing information and exhibits which need not be furnished to purchasers but are available for public inspection in the Commission's files'*. For more information, see David L. Ratner, *Securities Regulation*, (1998) 34. Hereinafter, David Ratner (1998).

In Japan, the term "prospectus" is also used to denote "*a document containing explanatory statements on such matters as may be prescribed by an ordinance of the Cabinet Office including the business of the issuer of a security and others for delivery to the other party of a public offering or public selling of a securities・・・*": [see *Securities and Exchange Law of 1948* (2001 Japan), Art. 2, Sub-art. 10].

If the issuer desires to have its bonds publicly issued, an even more comprehensive set of documents must be prepared. Although a resolution of the general shareholders meeting concerning the issuance of bonds is not required as it is in the issuance of shares, the dossier must consist of all of the remaining above-mentioned documents, and some extra documents must be added, namely:[103]

> *A resolution of the management board concerning the application for public issuance of bonds; where the issuer is a state enterprise, an approval for the issuance from the state authority that granted the enterprise an establishment license is required;*
> *A commitment of the issuer to carry out its responsibilities with respect to the investors;*[104]
> *A contract signed between the issuer and the bondholders' trustee;*
> *Minutes of the evaluation of the surety, or an agreement document of the underwriter to underwrite the settlement.*

Within 45 days from the date of receipt of the application dossier, the SSC is required to grant or refuse to grant an issuing license. Where a refusal is made, the SSC has to give its reasons in written form.[105]

When seeking to issue extra shares to the public (e.g. to make a public issue of shares for the second time), issuing companies also have to apply for an issuing license from the SSC,[106] providing that, they meet a number of statutory requirements.[107] *Circular 02/2001* provides for the contents of the application dossier filed with the SSC by the issuers. It seems that the application procedure remains the same as what the issuer has to go through to get shares issued for the first time, except for a simpler application dossier filed with the SSC. Some exhibits exempted from submission include the notarized copy of the company establishment license/decision, the notarized copy of the company charter, and the decision on evaluation of the enterprise asset signed by a state authority (where the issuer used to be a state enterprise).[108]

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[103] See *Decree 48/1998*, Art. 9.2; see also *Circular 02/2001*, Section IV. 2.

[104] This commitment seems unnecessary since the bond certificate itself is a contract (1) which contains the responsibilities of the issuer and the rights of the bondholder; (2) under which the two parties have agreed to implement their responsibilities and rights. As such, there is no need for a separate commitment as provided for in this provision.

[105] See *Decree 48/1998*, Art. 11.

[106] See *Circular 02/2001*, Section V.1.

[107] See *Decree 48/1998*, Art. 7; see also *Circular 02/2001*, Sections: II.1 and II.2. According to these provisions: (1) issuers have to meet almost all of the conditions facing them in the first issuance except for the requirement that founding shareholders, by the time the issuance finished, are required to hold at least 20% equity capital of the issuer within the first three years from the date of completion of the issuance; (2) furthermore, the other two new conditions facing issuers are: (a) the second issuance must be effected at least one year after the first issuance from the date the issuer obtained the first issuing license, and (b) total value of shares issued for the second time must not exceed total value of the outstanding shares.

[108] See Section IV.3.

Under *Decree 48/1998* and *Circular 02/2001*, an issuing license seems to be valid for a limited term because the issuers or the distributors must issue securities within 90 days from the effective date of the issuing license.[109] After the 90th day, the remaining securities cannot continuously be distributed, pursuant to *Decree 48/1998*. *Circular 02/2001*, however, goes further in saying that after the expiration of the 90-day period, if there are securities remaining, and if the issuers seek to continue the distribution, then they have to file a letter of application to the SSC. The letter must include reasons for and a proposal of the continuous distribution of the remaining securities.

2. Listing Process

Section V.6, *Circular 02/2001* says that shares and bonds that are eligible for public issuance can be registered and listed at a trading center or a stock exchange. Article 22, *Decision 79/2000*[110] stipulates a number of criteria that issuers have to meet in order to get their securities listed:

1. *Having a charter capital of at least 10 billion Vietnamese Dong;*
2. *Making profits in the last two consecutive years preceding the filing date of the application for being listed or re-listed; having healthy financial conditions and potential prospects;*
3. *Having at least 20% of equity capital owned by more than 100 outside investors; this figure shall be 15% if the equity capital of the issuer reaches 100 billion Vietnamese Dong;*
4. *Having at least 20% of total value of issued bonds held by more than 100 outside investors; this figure shall be 15% if the total value of bonds to be issued reaches 100 billion Vietnamese Dong;*
5. *Having financial statements in the last two consecutive years preceding the filing date of the application for being listed or re-listed, wholly approved or approved with an exception by an auditor;*
6. *Having eliminated the causes for being de-listed (if the issuer was to be de-listed and now applies to be re-listed).*

The first four criteria can actually be found in the conditions a company has to meet to make a public offering. Thus, those who are already eligible for a public issuance will only face one condition, (5), if seeking to be listed for the first time; or will face two conditions, (5) and (6), if seeking to be listed for the second time.

[109] See *Decree 48/1998*, Art. 14; see also *Circular 02/2001*, Section VI.9.

[110] The full name of this document is *Decision 79/2000/QD/UBCK*, dated 29 Dec. 2000. This Decision promulgates the "Regulation of Members, Listing, Information Disclosure and Securities Transaction".

Those who already meet the above-mentioned criteria can become listed companies after completing some administrative procedures at a trading center. It seems that in doing so, the issuers (1) can simply get registered at a securities trading center to be listed companies, or (2) have to apply at a securities center for being listed, depending on the date on which the issuer files the listing dossier with a trading center.

Those who seek to get their securities listed on a trading center for the first time, and within one year after obtaining the issuing license from the SSC, will have to file a listing registration statement with the center. The statement must consist of a letter of listing registration, a copy of the issuing license, a report on the result of public offering, a shareholder or bondholder list, a copy of the company-profile notice and a resume of that notice which was approved by the SSC.[111] After five working days from the date the trading center receives the adequate registration statement, the issuer can get securities listed on the center.[112]

It seems that those who seek to have their securities listed on a trading center for the first time, but one year after obtaining the issuing license from the SSC, have to overcome another application procedure to get their securities listed. Article 16.3, *Decision 79/2000* reads:

> *Where a listing registration is filed with a trading center one year after the date of obtaining the issuing license from the SSC, apart from the documents provided for in sub-article 1 of this Article, the issuer has to file with the securities trading center the financial statements of the last two consecutive years. Such statements must include: the balance sheets, business performance reports, commentary on the financial statements (attached with the comments of an independent auditing company). The securities trading center shall consider and settle within 45 days from the date of receipt of the complete listing application dossier.*

It is clear that where the issuer seeks to have their securities listed for the first time and within one year from the date of receipt of the issuing license, its securities will be listed after five working days. Where an issuer seeks to have securities listed for the first time, but after one year from the date of receipt of the issuing license, it seems to be subject to some discretionary powers of a trading center. In other words, in the latter case it seems harder for the issuer to become a listed company than in the former case. This is, perhaps, because in the later case a longer time has passed since the issuer obtaining the issuing license from the SSC. During that time, the business situation of the issuer might be changed and therefore the relevant trading center needs to investigate more about the issuer to ensure that its current business situation is satisfactory for being listed.

[111] See *Decision 79/2000*, Art. 16.1.
[112] Ibid., Art. 16.2.

II. WHETHER THE CURRENT DISCLOSURE REQUIREMENTS ENSURE THE AVAILABILITY, TIMELINESS, AND ADEQUACY OF INFORMATION

1. Information Disclosure Requirements under the Existing Regulation

A full information disclosure regime has widely been recognized as a cornerstone of securities law to assure a continuous flow of information, which in turn ensures that investors are protected. This position has become embedded, for example, in the IOSCO (International Organization of Securities Commissions) document,[113] and in the US[114] and Japan[115] securities regulation. Having been aware of that fact, the lawmakers in Vietnam created relatively comprehensive disclosure requirements, which seem impressive to foreigners.[116]

The information disclosure regime is quite distinct compared with other components of the current securities regulations because of the fact that it lies in various legal texts regulating both the securities industry and enterprises; and because it has undergone consecutive changes within a short time. The core legal rule of the securities regulations, *Decree 48/1998*, merely gives general principles concerning information disclosure. Principles that are more detailed were created later by the SSC. Three months after the issuance of *Decree 48/1998*, the "Regulation of Public Issuance of Shares and Bonds" promulgated under *Circular 01/1998*[117] was passed. In September 28, 2001, *Circular 01/1998* was replaced by *Circular 02/2001*. This circular, similar to its predecessor, provides a legal basis for public offering disclosures. Continuous disclosures are mainly subject to the "Regulation of Members, Listing, Information Disclosure, and Securities Transactions", which was only released in 1999 by *Decision 04/1999*.[118] In June 12, 2000, *Decision 04/1999* was revised by *Decision 42/2000*,[119] which, in turn, was shortly repealed by *Decision 79/2000* in December 29, 2000. Thus, information disclosure

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[113] See IOSCO, "Objectives and Principles of Securities Regulation - A Report of the International Organization of Securities Commissions: September 1998", Part I.4.2.1: at *IOSCO Document Library*, http://www.IOSCO.org/docs-public/1998-objectives.html, visited Nov. 6, 2001.

[114] See *Securities Act of 1933* ss 5, 6, 7, 8, & 10, 15 USC ss 77e, 77f, 77g, 77h, & 77j (2002): the principal aim of the US Securities Act is to facilitate the availability of reliable information concerning securities that are going to be offered to the public; see also *Securities Exchange Act of 1934* ss 12, 13, & 14, 15 USC ss 78l, 78m, & 78n (2002).

[115] See *Securities and Exchange Law of 1948* (2001 Japan), Arts 5 & 24: the fundamental objective of the securities regulation of Japan is timely disclosure of information.

[116] See Indira A. R. Lakshmaman, Globe Staff, "Vietnam Takes Slow Road Toward Capitalism Stock Exchange Opens to Trade only 4 Stocks", (Nov. 27, 2000) *The Boston Globe*, <LexisNexis: Top News: Most Recent Two Weeks of News Stories>.

[117] The full name of this document is *Circular 01/1998/TT-UBCK* dated October 13, 1998 (hereinafter, *Circular 01/1998*).

[118] The full name of this document is *Decision 04/1999/QD-UBCK1* dated March 27, 1999 (hereinafter, *Decision 04/1999*).

[119] The full name of this document is *Decision 42/2000/QD-UBCK3* dated June 12, 2000. Hereinafter, *Decision 42/2000*.

requirements can now be found in *Decree 48/1998, Circular 02/2001, Decision 79/2000, the Enterprise Act* and other legal texts guiding the implementation of the Act.

The disclosure regime applying to issuing companies requires four types of disclosure:

(a.1.) Disclosure at the time an issuer is seeking to make a public offering (hereinafter, public offering disclosure);
(a.2.) Periodic disclosure (a disclosure made on a quarterly, half-yearly or annual basis);
(a.3.) Timely disclosure (disclosure of newly emerged material facts that might affect the share prices);
(a.4.) Disclosure at the request of either the SSC or a securities trading center.

Securities trading centers are also subject to information disclosure regulation but their duties are confined within the disclosure of market activities.

Apart from these requirements, information disclosure is also required when a tender offer takes place.

a. Disclosures by Issuing Companies

a.1. Public Offering Disclosure

Public offering disclosure is of importance since it provides the public, for the first time, with relevant information about the issuers as soon as they publicly offer securities. Such disclosures enable investors to make wise and right investment decisions in the primary markets. Possibly for this reason, regulations of public offering in most developed countries' securities laws require information to be widely published and distributed by issuers.[120]

In Vietnam, the whole set of statutory provisions that govern public offering disclosures can be found in the regulation of public offering promulgated under Chapter II *Decree 48/1998* and Section IV *Circular 02/2001*.

Under the regulation on public offering, before securities can be sold to the public, the issuer must file an application dossier containing specified information with the SSC to obtain an issuing license, and must provide public investors with specified information. The public offering disclosure an issuer has to make is thus done through this application process. Documents found in the dossier[121] are expected to contain adequate and necessary information concerning the issuer. Among these documents, perhaps the most important ones that provide the public with essential information about the issuer are the company-profile notice and the financial statement.

[120] See James D. Cox, "The Future Content of the US Securities Law: Premises for Reforming the Regulation of Securities Offering: An Essay" (2000) 63 *Law and Contemporary Problems* 11, 14.
[121] The list of these documents is mentioned in Section I, Sub-section 1 ("Public Offering") of this Chapter.

The company-profile notice must contain necessary, faithful, and transparent information that will be helpful in enabling public investors and securities firms to appraise precisely the financial situation, business performance and prospects of the issuer.[122] The company-profile notice must provide the public with the following information:[123]

1. Name, domicile, telephone and fax numbers;
2. Summary of the company's charter and history;
3. Structure of the organization or business group (conglomerate) the issuer belongs to;
4. Company management apparatus;
5. Financial performance analysis;
6. Shareholdings held by the current shareholders; names and addresses of large shareholders (holding more than 5% of equity capital of the issuer), of management board members and of the director, and the chief accountant, and their corresponding equity and debt ownership;
7. Tax liabilities and the way it is intended to discharge such liabilities of the company; pending debts; issuing plans and proposals for the use of the proceeds (capital raised from the public);
8. Outcomes of business performance and of marketing; and principal products/services produced/provided in the last two consecutive years, and so on.

Where the issuer intends to issue shares that give shareholders the right to purchase other shares of stock (*call option*), or intends to issue preferred shares having *call option*, or intends to issue convertible bonds or bonds having *call option*, or secured bonds, the company-profile notice must prescribe the rights and other conditions that relate to such securities.[124]

The financial statement must be presented in conformity with the current accounting regulation.[125] The annual balance sheet and annual business performance report must be audited by an approved auditing firm.[126] Where the issuer holds more than 50% of the

[122] See *Circular 02/2001*, Section IV. 4. a.
[123] Ibid, Section IV. 4.b.
[124] Ibid, Section IV. 4.c. Possibly it is too early to introduce this provision when the Vietnamese securities market is merely in its infancy.
[125] The following Sub-section of this Section will discuss the current accounting regulation.
[126] The *"Regulation of Independent Auditing Firms Selected for Auditing Issuers and Securities Firms"* was promulgated under *Decision 26/2000/QD-UBCK2* dated Apr. 5, 2000 (hereinafter, *Decision 26/2000*). Pursuant to Article 2, *Decision 26/2000*, an approved auditing firm is an independent auditing firm that gets approval from the SSC to audit issuing companies and securities firms. Article 5.1, *Decision 26/2000*, provides for criteria to be met by independent auditing firms that seek to be approved auditing firms.

For more information concerning independent auditing firms, see *Decree 07/CP* dated Jan. 29, 1994, Art. 4 (which defines independent auditing firms); *Circular 22/TC/CDKT* dated Mar. 19, 1994, Section III. 16 (which specifies criteria to be met by those who seek to establish an independent auditing firm).

equity capital of another company, the financial statement of this company must be included in the application dossier filed by the issuer.[127]

After obtaining an issuing license from the SSC, the issuer must get its issuing announcement published in one central and one local[128] newspaper on five consecutive days and in a formal bulletin of a trading center.[129] The announcement must include: the name of the issuer, domicile of the head office, telephone and fax numbers; charter capital; business purpose; public issuing price; types of shares or bonds; total number of shares or bonds permitted to be issued to the public; date and term (*thoi han*) of the issuance; place where shares or bonds will be distributed; place where the prospectus will be available for public access.[130]

The last item in the announcement that concerns the place where the public can obtain the prospectus of the issuer is a new rule introduced by *Circular 02/2001,* compared with *Circular 01/1998*.

After obtaining an issuing license from the SSC, and before distributing securities to the public, issuers have to file with the SSC specified documents such as a resume of the prospectus, an issuance notifying document, and other documents (if any are available), that are to be used for the distribution of securities. After five working days from the date of receipt of the said documents, if the SSC has no refusal, the issuer can use these documents in offering securities for sale to the public.[131] The issuer is responsible for providing a formal prospectus or its resume (if any is available) at the request of investors or securities firms, and in the places specified in the Issuing Announcement.[132] Some other possible ways by which the issuers, underwriters or distributors can directly furnish the prospectus to individual investors such as mailing and facsimile transmission, however, do not seem to be legally required.

a.2. Periodic Disclosure

Issuers are required to disclose information concerning their financial situations and business performance on a periodic basis.[133]

On the whole, *Decree 48/1998* and the *Enterprise Act* merely give general principles concerning continuous disclosures imposed on issuers. More detailed provisions can be found in *Decision 79/2000.*[134]

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[127] See *Circular 0 2/2001*, Section IV.5.
[128] A local newspaper issued in the place where the head office of the issuer is located.
[129] See *Decree 48/1998,* Art. 13.
[130] See *Circular 02/2001,* Section VI. 2
[131] Ibid, Section VI.3.
[132] See Section VI.4.
[133] See *Decree 48/1998,* Art. 18.2; see also the *Enterprise Act,* Art. 93.
[134] This Decision reserves one chapter, Chapter IV titled "Information Disclosure", which applies to listed companies, to fund management companies and to securities trading centers.

Listed companies have to report to the securities trading center and the SSC about their business performance, capital, assets, turnover, profits and taxes on a quarterly basis, and also on half-yearly basis, within the first 15 days of the following month.[135]

They also have to disclose the annual report within 90 days from the date of completion of a fiscal year. Such a report includes a balance sheet, a business performance report, a cash flow report, a commentary on the financial statement (with attached certification by an approved auditing firm) and a general report.[136] The first four items of the annual report are actually components of a financial statement under the current accounting regulation.[137] Thus, the annual report consists of a financial statement and a general report.[138]

Decision 79/2000 also requires listed companies that own more than 50% of the equity of another company, or those having 50% or more equity capital owned by another company, to disclose the financial statement of their subsidiaries or holding companies, respectively.[139]

The annual report must be filed with the securities trading center and the SSC; its contents must be published in the annual releases of the listed companies, and be briefly published in the two consecutive issues of a central newspaper.[140]

Furthermore, such annual reports must be preserved at the Information Disclosure Section of the Securities Trading Center within two years, for investors' reference.[141]

a.3. Timely Disclosure

Timely disclosures are required in a number of specified circumstances. *Decree 48/1998* briefly says that issuers have to report, in a timely way, to the SSC on their own initiative where important information that can affect the prices of their securities is available.[142]

The timely disclosure regime is, moreover, provided for in some detail under *Decision 79/2000*. Listed companies must, on their own initiative, make timely disclosure in a number of circumstances, which can be grouped as follows:

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[135] See *Decision 79/2000*, Art. 32.1.
[136] Ibid., Art. 32.2.
[137] See *Decision 167/2000-QD/BTC* (hereinafter, *Decision 167/2000*) dated Oct. 25, 2000, promulgating the "Enterprise Financial Statement Regime", Part I, Section II.
[138] Although *Decision 79/2000* imposes a duty to disclose financial statements on listed companies, the core of the accounting regulations, *Ordinance on Accounting and Statistic*, does not have any concrete provision laying down such a duty. Thus, public access to enterprise financial information does not seem legally recognized under the current accounting regulation. This fact makes the Ordinance disagree with the *Enterprise Act* and the securities regulations and causes difficulties in implementing the accounting regulation.
[139] See *Decision 79/2000*, Art. 32.3.
[140] Ibid., Art. 32.4.
[141] See Art. 32.5.
[142] See *Decree 48/1998*, Art. 18.3.

(a) Their financial situation has changed, e.g. their bank accounts are to be suspended or blocked; or when such situations have been reversed; their assets have been damaged up to 10% or more; or they go bankrupt;
(b) Their legal structures might be changed: going into consolidation, merger, division or separation; business registration certificate or business operation permission being revoked; facing a dissolution decision;
(c) Their performance does not go smoothly, for example: their business operation has ceased for more than three months, or has been suspended or restarted; or the consumption of their main products has been suspended;
(d) They are threatened by some legal actions such as being prosecuted for violating the listing regulation; being investigated by a tax authority; or receiving a court decision concerning company business performance;
(e) When they make a decision concerning a number of issues such as paying dividends, splitting or adding up outstanding shares or issuing new shares, changing business purpose, expanding business scale up to 10% or more of the equity capital, de-listing and other decisions that might affect stock price or investors' benefit.[143]

A listed company is required to report such information to the trading center in written form, within 24 hours from the time the event occurs. The listed company also has to announce such an event within three days from the date it occurs, in a central newspaper and a newspaper of the locality where its head office is located.[144]

The securities trading center is required to release the above-mentioned information on its own information disclosure facilities. However, when the relevant companies are being investigated by a tax authority, receiving a court decision, or being de-listed, and when companies face events that might affect their securities prices, then the trading center will have to disclose such information in the public media.[145]

Apart from these requirements, under the *Enterprise Act*, shareholders must be informed about the company decision to acquire its own shares within 30 days from the date of approval of that decision.[146] The Act, however, does not specify the way in which such information is to be furnished to shareholders.

a.4. Disclosures at the Request of either the SSC or a Securities Trading Center (hereinafter, disclosures at a request)

Decree 48/1998 merely says that where it is deemed necessary to protect public investors, the SSC can request a relevant issuer to file with it a report on the issuer's business situation.[147]

[143] See *Decision 79/2000*, Art. 33.1.
[144] Ibid, Art. 33.2.
[145] Ibid, Art. 33.3.
[146] Ibid, Art. 65.
[147] See *Decree 48/1998*, Art. 18.4.

Decision 79/2000 further develops the above-mentioned provision. Accordingly, listed companies have to disclose relevant information at the request of either the SSC or a securities trading center if: (a) there is rumor, concerning a listed company, that threatens the price of its security, and it is deemed necessary to clarify such rumor; (b) when the price of a listed security and volume of transactions on such a security have suddenly been changed.[148]

Where such circumstances have occurred, within 24 hours from the time the securities trading center or the SSC makes the request, a listed company has to disclose the relevant information in a central newspaper and a newspaper of the locality where its head office is situated. The listed company has to report to the SSC and the trading center in written form.[149] The concrete contents of the report made by the listed company will be subject to the rules of the trading center where it has its securities listed.[150]

b. Trading Information Disclosure Requirements With Respect to Securities Trading Centers

Securities trading centers have to disclose information concerning: market transactions (securities' prices, volume and value of securities transacted and so on); purchasing and selling orders (the best offering/purchasing prices, number of buying and selling orders); indexes of listed securities; market management and market situation; listed companies and fund management companies, members of the trading center and investors.[151]

The manner in which securities trading centers disclose information includes electronic boards, computer system on the trading floors; printed releases by the centers; and public media.[152] Among these facilities, perhaps, the electronic boards can only provide the public with information such as securities' prices, volume, and value of securities transacted, and indexes of listed securities. Material information that is helpful for appraising the situation of listed companies will thus be disclosed by the remaining facilities.

Securities trading centers are also responsible for furnishing information concerning listed companies to securities firms. Those securities firms will then be in charge of making such information available to public investors.[153] Since the number of securities firms remain poor, it seems hard for public investors to get information directly from the relevant firm.

Furthermore, the computer network among the Securities Trading Center, listed companies and securities firms has not been connected, and so information has been

[148] See *Decision 79/2000*, Arts. 34.1.
[149] Ibid, Art. 34.2.
[150] Ibid, Art. 34.3.
[151] Ibid, Art. 40.
[152] Ibid, Art. 41.
[153] Ibid, Art. 42.1.

transferred mainly by mail, which is often delayed and dependent on the efforts of the relevant parties.[154]

The way in which information reaches the public investors can best be illustrated by the following chart:

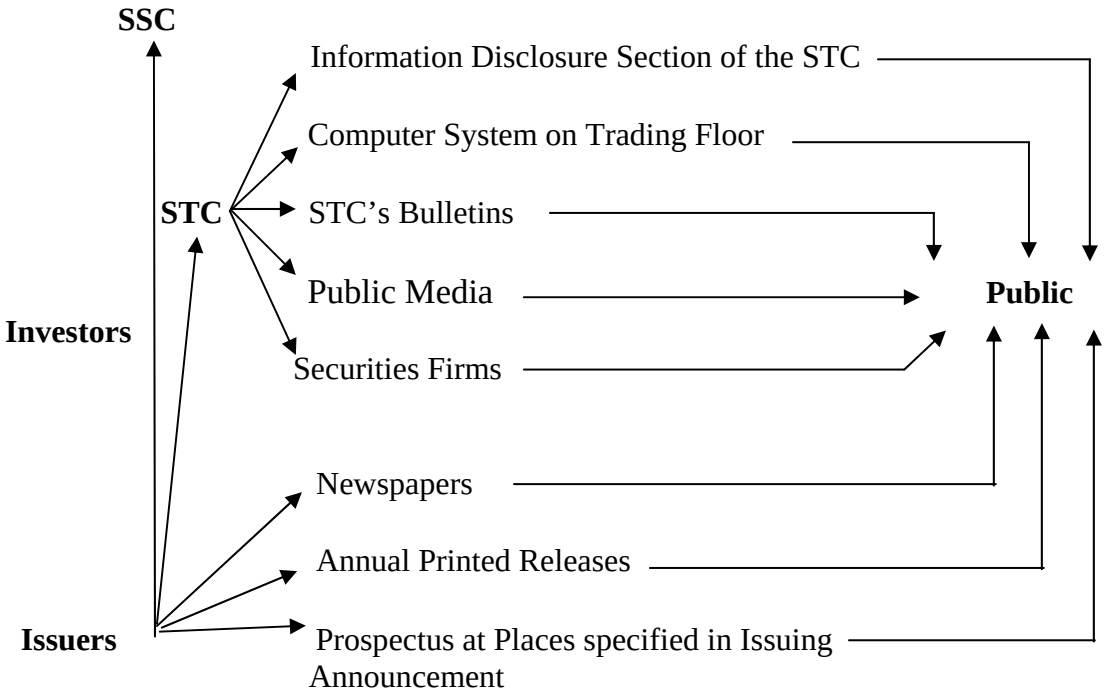

Chart No. 1: Information Flow

c. Information Disclosure in Tender Offers

It is noteworthy that "Corporate Tender Offers and Mergers" are inserted in Chapter VIII, *Decree 48/1998*, under the title "Prohibited and Restricted Activities".[155]

[154] See Kim Chi, "Hoat dong cong bo thong tin tren thi truong chung khoan" [Information Disclosure on Securities Trading Centre], (2001) 2, *Tin Thi Truong Chung Khoan [Securities Markets Bulletin]* (Jan. 6, 2001) 1, 1. Facsimile transmission is not mentioned here; it is unclear whether this facility has been employed in transferring information, hereinafter, Kim Chi.

[155] Although having been titled "Corporate Tender Offers and Mergers", Article 74 gives more weight to regulation of tender offers. Its contents do not embrace what is implied in the title. In other words, the Article does not seem to deal directly with mergers.

The question of information disclosure in mergers will not be discussed here since such disclosure is mainly required and made among the shareholders of the parties in a merger, not among public investors.

Article 74, titled "Corporate Tender Offers and Mergers" comprises two sub-articles. Sub-article one reads:

> *Organization(s) and individual(s) which engage in any transaction that affects the holding or the transferring of 5% or more of voting shares of one issuing company, shall be subject to reporting to the Securities Trading Center or Stock Exchange.*

The language of this provision sounds ambiguous and does not seem to cover the activities that might be expected. First, if the terms "organization" and "individual", employed in the provision, are read in singular form, the scope of this provision does not seem to cover an event that very likely occurs in practice, *viz.* the purchase in collusion of more than 5% of voting shares from one issuer by two or more persons where each of them merely buys, for instance, 4.9% of the shares. If these terms are read in plural form ("organizations" and "individuals"), then it seems that any group of persons whose purchases exceed 5% of the said shares will be subject to reporting requirements regardless of whether or not they have purchased in collusion.

Secondly, the provision merely imposes reporting responsibilities on purchasers of 5% or more of voting shares of an issuer. It does not spell out which kinds of information are to be reported. *Decision 79/2000,* while providing for the types of information that securities trading centers have to disclose, says that the relevant securities trading center shall disclose information concerning the investors that fall within the scope of Article 74 *Decree 48/1998*.[156] It appears that the only information required to be disclosed here concerns the investors making tender offers.

Furthermore, the securities trading center seems to be the only entity that should be reported to, since the provision does not require the purchaser to report either to the issuer or to the SSC. Experience from abroad shows that the issuer and the governmental regulatory agency should also get a report from the acquirer where such transactions occur.

The *Securities Exchange Act* of 1934 of the US also regulates this matter but in a more comprehensive manner. Pursuant to Section 13(d), the acquirers of more than 5% of any equity securities of class/classes registered under Section 12 of the act will be subject to reporting requirements, *viz.* to notify the issuer of such securities; to send to and to file with the stock exchange and the SEC, respectively, statements containing specified information. Section 13(d) even stipulates, in detail, the information that must be included in the statement, *e.g.* information concerning the purchaser, the fund used to acquire such equity securities, the purpose of the purchase, the amount of acquired shares, and other information relating to any contract, agreement or understanding.[157]

The matter is dealt with in a similar manner in Japan, where a holder of more than 5% of share certificates (large shareholder) has to provide a "large holding report" to the

[156] See Article 40.8.
[157] See items (A) - (E) of this Section.

Prime Minister within five days from the date that the person becomes a large shareholder. The report must contain information such as:

> *matters relating to the holding ratio of share certificates, etc., matters relating to the funds used to acquire the share certificates, etc., the purpose of holding the share certificates, etc. and others・・・*[158]

Sub-article two, Article 74, *Decree 48/1998* allows the acquisition of more than 25% of the voting shares of one issuing company, provided that the acquirer makes a public offer. It reads:

> *Organizations, individuals, and relating parties, which intend to acquire more than 25% of voting shares of an issuing company, shall have to hold a public bidding in conformity with rules and regulations of the SSC.*

Since the passage of this provision in 1998, the SSC has not created such rules and regulations. For this reason, to date, uncertainties remain and perhaps public biddings, if available, have been held according to the discretion of the acquirers, which might go against the aim of this provision.

Some Remarks

Looking at the information disclosure regulation, one is impressed by its relative comprehensiveness with various categories of information disclosure: (a) disclosures by issuers/listed companies such as public offering disclosure, periodic disclosure, timely disclosure, disclosure at a request, (b) disclosures by securities trading centers and (c) disclosures in tender offers. In addition, auditing work, which is required with respect to the financial statements of listed companies, ensures that information released by these companies is reliable. This is of importance since it can build up public confidence in the companies' released information, and in securities markets also. Such a good system of information disclosure, if accompanied by sound accounting rules and adequate auditing regulation will, in principle, generate good information flow in the securities market, and the market will gain public confidence. That is because accounting rules are seen as a central part of information disclosure.[159] The quality of disclosed information is greatly dependent on accounting and auditing practices. Only when good systems of accounting and auditing are achieved, can information disclosed by listed companies be reliable and

[158] See *Securities and Exchange Law of 1948* (2001 Japan), Art. 27-23.
[159] See Bernard S. Black, "The Legal and Institutional Preconditions for Strong Securities Markets", (2001)48 *UCLA Law Review* 781, 849.

useful to the public, and securities markets really attract public investors. A thorough examination of the current accounting and auditing regulation of Vietnam is thus needed to clarify whether the current accounting and auditing rules are a support or a hurdle in implementing the existing information disclosure regulation.

2. Whether the Accounting and Auditing Regulations Support Well the Information Disclosure Regime

The core legal instrument regulating the accounting work of enterprises in Vietnam is the *Ordinance on Accounting and Statistics*, which was passed on May 20, 1988. This Ordinance and other subordinate legislation together compose the current accounting regulation. Being issued more than a decade ago and covering the two different areas, accounting and statistics, the *Ordinance* can no longer meet the newly emerging requirements of the young market economy; its provisions are not in conformity with other law regulating enterprises and are not comparable with international accounting standards.

The Ordinance has been supplemented by a number of other legal documents issued by the Finance Ministry. In 1995, *Decision 1141*[160] was issued to promulgate the "Enterprises Accounting Regime". This Regime consists of the regulations of (1) the accounts system, (2) the financial statement system, (3) accounting books, and (4) accounting exhibits. The regulation of the financial statement system (item No. 2) was repealed by the new "Enterprise Financial Statement Regime" promulgated under *Decision 167/2000*. These two Decisions apply to large enterprises. Medium and small enterprises are subject to the regulation of accounting and financial statement promulgated under *Decision 1177/TC/QD/CDKT* dated Dec. 23, 1996. Since listed companies are large enterprises, the following discussion will focus on the statutory provisions promulgated under the *Ordinance*, *Decision 1141* and *Decision 167/2000*.

Although the new regulation of financial statements has been introduced by these two decisions, there are several issues that still need to be taken into consideration. First, the statutory provisions concerning the contents of a financial statement seem to be not entirely consistent. Pursuant to the *Enterprise Act*, a balance sheet and a settlement of account report are components of a financial statement.[161] Meanwhile, a financial statement is composed of (1) a balance sheet, (2) a business performance report, (3) a cash flow report; and (4) a commentary of the financial statement, according to *Decision 167/2000*.[162]

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[160] The full name of this decision is *Decision 1141-TC/QD/CDKT* dated November 01, 1995 (promulgating the *'Enterprises Accounting Regime'*).

[161] See Art. 118.2.

[162] See Part I, Section II (Contents of the Financial Report System). The cash flow report is although included in the list, is not a mandatory item (see Part I, Section III, First paragraph). However, according to Article 32.2, *Decision 79*, the cash flow report is a mandatory item in the financial statement released by listed companies.

Secondly, the form of financial statement that is modeled after the form applied to state enterprises is very different from the international accounting standards.[163] The requirements with respect to financial statements appear to be too complicated, with even excessive and unnecessary items.[164] This observation is borne out by the fact that 90, 60, and 40 different items are required to be included in the balance sheet, the business performance report, and the cash flow report, respectively.[165] Moreover, much of the required information appears not to be necessary to be inserted in the statement *e.g.* the value-added tax, income, and salary of company employees.[166] It is expensive and time consuming to meet these requirements, especially in the current socio-economic circumstance of Vietnam where human resources in the accounting and auditing fields remain poor. As for the cash flow report, even though it is available for investors' inspection, it does not always seem to be helpful. That is because of the adoption of the two statutory methods of reporting, direct and indirect, which causes difficulties to investors when they refer to such reports. Under the direct method, the report reflects amounts collected from, and amounts paid for, various business activities, while according to the indirect method, the report indicates various purposes to which the pre-tax-profits will be distributed to.

SACOM (a cable and communication materials shareholding company) has encountered a problem after its information was released to the public, simply because it followed the direct method to make the cash flow report. One of the items of information disclosed by SACOM, when it announced a proposal on the issue of bonus shares in order to increase its charter capital, was a 50 billion Vietnamese Dong depreciation fund. After the information had been released, investors tried hard to study the cash flow report to find out the concrete depreciation amount, but they failed. This is because the cash flow report was made in accordance with the direct method based on the difference between the total collected and the total paid amounts, which makes it difficult for investors to define the depreciation fund.[167]

Looking at the accounting regulations of Vietnam, one finds that the regulations are far different from those in other countries. A report on the changes in reserved profit is important, as it helps investors to evaluate a company's potential financial resources, but it is not required to be included in the financial statement under the current regulation. Thus, the statement, while in other respects containing too much information, cannot provide public investors with useful information that would enable them to make prudent investment decisions. In practice, investors find it difficult to compare financial

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[163] See "Seeing a Compromise", *SGT Weekly* Dec. 08, 2001, http://www.vneconomy.com.vn/en/finance/finance_taxation/01-0038.htm, visited Apr. 08, 2002. Hereinafter, "Seeing a Compromise".

[164] Ibid.

[165] See *Decision 167/2000*, Form No. B01-DN; Form No. B02-DN; and Form No. B03-DN, respectively.

[166] See "Seeing a Compromise" above n. 163.

[167] See "Nha dau tu mat niem tin vi doanh nghiep khong trung thuc" [Investors Lost Confidence Due to Enterprises' Dishonesty], *Dau tu chung khoan [Securities Investment]*, (Sep. 5, 2002), http://vnexpress.net/Vietnam/Kinh-doanh/chungkhoan, visited Sep. 7, 2002.

performance even amongst a very small number of domestic listed companies.[168] Far worse are the difficulties investors might encounter when they seek to compare such performance between listed companies operating inside and outside Vietnam.

Usually, in other countries, a financial statement consists of (1) a balance sheet, (2) a business performance report, (3) a cash flow report, (4) a report on the changes in reserved profit, and (5) a commentary on the financial statement.[169] In Japan, for example, a financial statement (accounting documents) consists of the following items: (1) a balance sheet, (2) a profit and loss account, (3) a business report, (4) proposals relating to the disposition of profits or the disposition of loss, and (5) the annexed specifications of the above-mentioned documents.[170]

Regulation of financial statements in countries such as Britain, Singapore, Australia and the US, as observed by one commentator, can be very strict or relatively lenient, and can vary in such matters as submission deadlines, business sizes, and so on; but they all have certain common features: (1) financial statements are mandatory for all listed companies and large limited liability companies; (2) the required contents of the statement vary from listed companies to small companies, and differentiate between the scope, size and legal structure of the companies; (3) the statements are to be audited so that they gain public confidence; (4) information contained in the statement is classified into public-disclosure and non-public-disclosure items. Thus the public cannot access all of the information in the statement; (5) there are enforcement mechanisms, including sanctions and education measures. For example, a fine will be imposed for the late submission of financial statements; accounting and auditing staffs must be qualified, and financial disciplines are to be widely disseminated within the business community.[171]

In Vietnam, although the auditing work was not provided for under the *Ordinance on Accounting and Statistics*, it has recently been required in the information disclosure regime, as earlier mentioned, and in the *Enterprise Act*. Under the Act, shareholding companies are to be inspected by an independent auditor. For the purpose of auditing, shareholding companies fall into two groups: those whose annual financial statements need to be inspected by an independent auditing firm and others whose annual financial statements need not.[172] Though the Act does not expressly spell out which companies will be audited by an auditing firm, the answer can be found in *The Regulation of Independent Auditing Firms Selected for Auditing Issuers and Securities Firms*, promulgated under

[168] See Kim Chi, above n. 154.
[169] See Anh Thi, "'Tron' bao cao tai chinh? Binh quan ca nuoc chi co 20% doanh nghiep thuc hien" [Financial Statement Avoidance? On Average, only 20% of Enterprises Nationwide Have Financial Statements Filed]. *Thoi bao kinh te Viet nam [Vietnam Economic Times]* (Sep. 24, 2001), http://www.vneconomy.com.vn/vn/doanh_nghiep/dir.cgi, visited Apr. 08, 2002. (Text is in Vietnamese). Hereinafter, Anh Thi.
[170] See *Commercial Code* (Japan), Art. 281.
[171] See "Seeing a Compromise", above n. 163.
[172] See Art. 92.

Decision 26/2000. The Decision includes an article specifying which companies are required to be audited by an independent auditor:[173]

> *(1) Shareholding companies and equitized enterprises that offer securities to be listed for the first time, and those who seek to further issue securities to the public;*
> *(2) Shareholding companies that used to have securities issued beyond the scope of Decree 48/1998, dated July 11, 1998, issued by the Government (promulgating the regulation of securities and securities market), and now seek to have their securities listed;*
> *(3) State enterprises and limited liability companies that seek to issue bonds to the public;*
> *(4) Securities firms, fund management companies, and other securities investment funds which are established and operate in Vietnam.*

According to the language of the first three provisions, it is unclear whether the relevant companies will be subject to continuous auditing, or merely face auditing requirements when they seek to issue securities to the public or have their securities listed. Although the last provision does not spell out such an issue, it seems to imply that (and its language only makes sense if) the entities mentioned in the provision will be subject to auditing requirements and such requirements will apply to them in the course of business. Possibly the first three provisions also intend to require all those companies to be subject to independent auditing, on a periodic basis, once they seek to make a public offering or to have their securities listed.

In order to avoid conflicts of interest, *Decree 26/2000* also contains some statutory provisions under whereby independent auditing firms must not provide auditing services to an issuing company or a securities firm if they fall into a number of specified positions. For example, if an auditing firm and an issuing company/securities firm have a business relationship (where they subscribe capital to run a business together: to set up a joint venture, or a shareholding company); if an auditing firm and an issuing company/securities firm have, in common, a five percent shareholder; or if the former and one of the latter are, at the same time, subsidiaries of another company, and so on.[174]

Auditors working in these independent auditing firms and the firms' representatives are also to be subject to a number of statutory requirements. For example, they must not be a shareholder eligible to vote or a proxy of that shareholder of the audited issuing company or audited securities firm; they must not be a member of the management board of the audited issuer or audited securities firm, nor may they be a customer having preferred treatment from the audited issuer or audited securities firm; they must not be in

[173] Art. 2.
[174] For more information, see Art. 5.2.

a close relationship (i.e. parents – children, spouse, siblings) with a person who is a director, manager or an equivalent person of the audited issuer or audited securities firm; they must not provide non-audit services such as bookkeeping and making financial statement for the audited issuer or audited securities firm.[175]

To ensure that auditing firms maintain good quality services and to keep them working within statutory disciplines, *Decree 26/2000* also requires those firms to be reselected regularly by the stock market watchdog in order to act as an independent auditing firm. Every two years, the SSC will announce a list of independent auditing firms eligible to audit issuing companies and securities firms.[176] Issuers and securities firms can choose an auditing firm and auditors from the list to audit their accounting books.[177]

In terms of auditing regulation over companies that make a public offering and listed companies, and securities firms, the auditing regulation is rather complete with a number of advanced principles. The auditing requirements do exist, but if they are not accompanied by sound accounting regulation then there will still be a big obstacle in the way of foreign investors accessing Vietnam securities markets. That is because they cannot evaluate the financial performance of Vietnamese listed companies by comparing their financial statements with those of their foreign counterparts. Of course, one might argue that accounting rules vary from country to country and no one country's accounting rules seem to deserve adoption by other countries. That is true and for decade, the harmonization of accounting standards has become one of the operational goals of the IASC (International Accounting Standards Committee) and the IOSCO.[178] For the time being, what Vietnam needs are comparable accounting standards regardless of the absence of international securities offerings, cross-border mergers and acquisitions in the country. Furthermore, in the increasingly globalizing tendency of securities markets in recent years, harmonization of accounting standards and practices is clearly needed. Adopting a comparable accounting system with other countries around the world would thus enable the Vietnam's securities market to attract more foreign investors and also permit such market to be compatible with their counterparts outside Vietnam.

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[175] For further information, see Art. 6.

[176] See Art. 7.

[177] See Art. 8.

[178] For more information concerning the efforts of the IASC and the IOSCO in harmonizing countries' accounting standards, see Marc I. Steinberg, above n.7, 149.

The IASC is an independent, private body that was established with a mandate to create a uniform set of accounting standards to be followed by companies that make cross-border securities offerings. The IASC is an advisory authority, not an official regulator, so it does not have real enforcement authority. In December 1998, a set of core accounting standards was completed by the IASC to be submitted to IOSCO for approval and adoption worldwide. For further information see Joseph J.M. Orabona, "There's A New Sheriff In Town - Will the New SEC Chairman Allow Issuers of American Depository Receipts to Use International Accounting Standards To Satisfy Listing Requirements on U.S. Exchanges?", (2002) 22 *National Administrative Law Judge Foundation Journal of The National Association of Administrative Law Judges* 223, 243. Hereinafter, Orabona.

This is not to say that having internationally comparable accounting standards will ensure the success of information disclosure regulation.[179] Rather, accounting and auditing practices play a significant role toward achieving such success. This has been proven by the recent debacles of some economic giants, Enron and WoldCom, in the US.

The Enron breakdown resulted from conflicts of interest, accounting, poor management, poor public disclosure practices, and auditing failure.[180] The collapse of Enron occurred at a time when the American stock market recoded unprecedented success, but also a time when *"sharp practitioners in business, investment banking, accounting or law appear to have challenged the fundamental tenets of 'full disclosure of material information' or 'fair presentation of accounting results'"*.[181]

However, according to the former SEC Chairman, David Ruder, the primary fault in the Enron failure was poor management, which allowed Enron to engage in extremely aggressive accounting, to overstate its earning, and not to disclose the true nature of its corporate and financial structure and so on. He further stresses that

> *• • • the Enron problems represent a failure in corporate governance. One striking aspect of this failure is Enron's apparent lack of respect for the accounting system that underlines financial reporting. Enron seems to have purposely attempted to avoid disclosure of its true finances. Instead it should have utilized the accounting system as a means of assisting it to make sound management decisions and as a source of information helping it to provide the securities markets with a truthful statement of financial condition.*[182]

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[179] In the US, the SEC has been empowered to establish the accounting standards governing the production of financial statements, a component of the registration statements and periodic reports filed with the SEC under the securities laws [see *Securities Act of 1933* ss 7 & 19(a), 15 USC ss 77g, 77s (a); see also *Securities Exchange Act of 1934* ss 3(b), 12(b) & 13(b), 15 USC ss 78c(b), 78l(b) & 78m(b) (2002)].

However, in history, the SEC has delegated such a power to the private sector, the Committee on Accounting Procedure, later, the Accounting Principles Board (APB). Since the APB did not perform its tasks well, the Financial Accounting Standards Board was set up in 1973 to accomplish the creation of accounting standards, which have come to be known as Generally Accepted Accounting Principles (the term "Generally Accepted Accounting Principles" is a technical accounting term that combines "conventions, rules, and procedures necessary to define accepted accounting practice at a particular time.") Since 1988 the SEC has taken a mandate to establish high quality, comprehensive international accounting standards. [For further information see Ibid Orabona, 239 & 242].

Regardless of those efforts of the SEC in developing accounting standards, recently a number of financial scandals occurred in the US. For more information, see Faith Stevelman Kahn, "What are the Ways of Achieving Corporate Social Responsibility?: Bombing Markets, Subverting the Rule of Law: Enron, Financial Fraud, and September 11, 2001", (2002) 76 *Tulane University Tulane Law Review* 1579, 1635.

[180] See Joel Seligman, "What can We Learn from Enron", (Paper delivered at a special lecture conducted by Professor Joel Seligman on "*Securities Regulation in the United States*", held by Nagoya University, Center For Asian Legal Exchange (CALE), on May 23, 2002), 5 & 16.

[181] Ibid, 3 – 4.

[182] Ibid, 22.

All these problems clearly have a connection to accounting practices rather than to accounting standards.

The WorldCom meltdown, as reported, has its roots in accounting fraud. Compared with the Enron scandal, the WorldCom case is not at all complex but quite simple.[183] Within several years, WorldCom's Chief Financial Officer, Scott Sullivan, improperly capitalized several billion dollars worth of expenses in violation of generally accepted accounting principles. The fraudulent activity aimed to reduce operating expenses and artificially inflated profits, which allowed WorldCom to meet Wall Street analysts' profit expectations and the company's profit margin goals during 2001 and the first quarter of 2002.[184]

Faced with these financial scandals, on July 30, 2002, President Bush signed into law the *Sarbanes-Oxley Act of 2002*. The Act contains a number of statutory provisions that have certain impacts on the accounting profession. The Act establishes the Public Company Accounting Oversight Board, which is in charge of overseeing and investigating the audits and auditors of public companies, of sanctioning both firms and individuals for violations of laws, regulation, and rules.[185] To enhance the quality of information disclosed by listed companies, the Act requires each of these companies to set up an independent audit committee.[186] In John Coffee's view, this provision is the "most important and sweeping revision" of the Act since, although the provision does not strongly affect US corporations, it is a real threat to corporations incorporated outside the US, especially those from European countries. The reason lies in the difference between the corporate governance structure adopted in the US and those adopted in European countries. The latter is characterized by a two tier-board whose managing board (lower one) has no independent directors, and whose supervisory board (upper one) has half of the members being employees' representatives. For this reason, Coffee predicts that this statutory reform might cause foreign issuers who are already listed to de-list, and those who are going to list to decline to list on the US stock exchanges.[187]

To ensure that both public companies and auditors are responsible for all audited reports, the *Sarbanes-Oxley Act* requires auditors to report to and to be overseen by a company's audit committee; and the committee has to approve all services provided by its auditor.[188] Public companies and their auditors are required to be subject to new rules and procedures in connection with the financial reporting and auditing process such as: second partner review and approval of audit reports,[189] management assessment of

[183] See Representative Max Sandlin, "Statement for Financial Services Committee Hearing, - Wrong Numbers: the Accounting Problems at WorldCom" (Jul. 8, 2002), http://financialservices.house.gov/media/pdf/070802sa.pdf, visited Dec. 12, 2002.
[184] Ibid.
[185] See *Sarbanes-Oxley Act of 2002* s 101, 15 USC s 7211 (2002).
[186] Ibid, s 301, 15 USC s 78f(m) (2002).
[187] See John C. Coffee, "Racing Towards the Top? The Impact of Cross-listings and Stock Market Competition on International Corporate Governance" (2002) 102 *Columbia Law Review* 1757, 1824-1825. Hereinafter, John Coffee (2002).
[188] See *Sarbanes-Oxley Act of 2002*, ss 204 & 302. 15 USC ss 78j-1(k) & 7241 (2002).
[189] Ibid, s 103, 15 USC s 7213 (2002).

internal controls, and audit reports having to contain a description of internal control testing.[190] In addition, auditors are forbidden from offering certain non-audit services to audit clients, such as bookkeeping, information systems design and implementation, appraisal or valuation services;[191] auditors are also subject to the so-called "audit partner rotation" which requires leading audit partners and audit review partners to be rotated every five years on public company engagements.[192] To avoid conflicts of interest, the Act puts some limits on audit services providers. Accordingly, an accounting firm must not provide audit services to a public company if the former employs one of the ex-top-officers (CEO, controller, CFO, chief accounting officer, or person in an equivalent position) of the latter.[193]

It can be said that the *Sarbanes-Oxley Act of 2002* is a quick response by the US Congress to the scandals at Enron and WorldCom in order to restore public investor confidence. The Act, however, has been criticized for its hard rules. According to the Chairman of the London Stock Exchange, by its tough statutory provisions, the Act would make the US stock market *"far less attractive and welcoming to foreign issuers"*. In other words, it would cause a number of non-US firms to list their shares in other stock markets outside the US.[194]

Probably, it is too early to judge the potential consequences of the Act to the US economy and its impact on the corporate community. Whether success or failure that will result from such a statutory reform remains to be seen. Valuable lessons that we can learn from the recent American experience are: (1) attention should be paid not only to the completion of accounting standards, but also to accounting and auditing practices, in order to avoid serious corporate financial scandals, which can devastate public confidence in the stock market at an accelerating speed; and (2) the importance of establishing a regulatory body to be in charge of overseeing accounting practices *i.e.* to inspect registered accounting firms' operations, to investigate potential violations of securities laws, accounting standards, competency and conduct, and to impose sanctions for non-compliance or violations of the accounting and auditing regulations. Such a body would play a significant role in supporting a good overseeing mechanism, which in turn would ensure high quality accounting and auditing practices.

Some Observations

It can be said that the existing accounting rules do not well support the information disclosure regulation. For this reason, although the information disclosure requirements are comparable to those adopted in some developed economies such as the US and

[190] Ibid, s 404, 15 USC s 7262 (2002).
[191] Ibid, s 201, 15 USC s 78j-1(g) (2002).
[192] Ibid, s 203, 15 USC s 78j-1(j) (2002).
[193] Ibid, s 206, 15 USC s 78j-1(l) (2002).
[194] See "UK's LSE Chairman Blasts US Corp Reform Act", (Dec. 9, 2002) *Reuters,* http://www.forbes.com/markets/newswire, visited Dec. 10, 2002.

Japan,[195] they might not generate expected outcomes. Moreover, merely having complete statutory disclosure requirements still sometimes cannot assure a healthy market. China adopted its national *Securities Law* in 1998 with a rather comprehensive set of disclosure requirements.[196] Market manipulation and insider trading resulting from non-compliance with the disclosure requirements do occur.[197] Perhaps China is not unique in facing such problems, and it is very unlikely that Vietnam would be an exception. The experience, therefore, should not be ignored in the context of Vietnam, where both the securities industry and its supervision apparatus are merely in their infancy. The question of how to enforce the information disclosure regulation is thus of importance. The following discussion will deal with the practical implementation of the current disclosure regulation.

3. How Has the Existing Information Disclosure Regulation Worked?

So far, two types of practical problem concerning the information disclosure regime can be seen. One consists of those problems relating to non-compliance with the current information disclosures regime; and the other concerns the attitudes of "trading-floor-ready companies" towards that regime.

a. Whether or not the current information disclosure requirements have been adequately enforced?

A general criticism is that there has been a lack of information concerning listed companies; and that the disclosure regime has not properly been implemented, since listed companies often break the regulation on information disclosure.[198] From public investors to securities firms and listed company, all have their own varying observations concerning the question of information disclosure.

Public investors complain about the quality and quantity of information provided by the trading center. They get a bulletin on every trading session from the Securities Trading Center, but the source of information is extremely poor. Market information merely provides some figures concerning the highest or lowest prices, volume of matched orders, totally trading volume of the preceding session, and so on. They further say that all those source of information, they have already self-collected and self-maintained for

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[195] See the *Securities Act of 1933* ss 5, 6, 7, 8, & 10, 15 USC ss 77e, 77f, 77g, 77h, & 77j (2002), and Schedule A; see *Securities Exchange Act of 1934* ss 12, 13 & 14, 15 USC ss 78*l*, 78m, & 78n (2002); see also *Securities and Exchange Law of 1948* (Japan), Arts. 5 & 24.

[196] See Daniel M. Anderson, "Taking Stock in China: Company Disclosure and Information in China's Stock Markets" (2000) 88 *Georgetown Law Journal* 1919, 1932.

[197] Ibid.

[198] See "Dirty Play Drives Market off Course" (Jul. 16, 2001) *Emerging Markets Datafile, The Vietnam Investment Review*, <LexisNexis: Country & Region: Asia Pacific: World Sources Online, Emerging Markets Datafile>. Hereinafter, "Dirty Play Drives Market off Course".

reference.[199] In practice, investors have to self-collect information concerning the trading situation of the center, and concerning interest, speed of economic growth of listed companies, and so on. They also have to self-assess the situation based on their own subjective thoughts.[200] Even at such a self-collecting level, it is clear that not all investors are able do this.

Investors also complain about the lack of transparency and accuracy of both the prospectus and the financial statement made by listed companies.[201] They further say that listed companies do not periodically disclose information as provided by the law; listed companies do not make timely disclosure of information concerning share transactions of company management board's members and of major shareholders; these companies do not make timely announcement of information in the public media and in a number of cases their released information is not accurate.[202] In addition, the financial statements are said to be sparsely prepared, and the commentaries on such statements lack concrete explanations.[203]

Securities firms do not seem happy with what they get from the Stock Trading Center either. Pham Uyen Nguyen, Vice Director of Bao Viet Securities Firm, says that securities firms merely get "crude" information concerning market direction or listed companies from the Stock Trading Center; that the firms are hesitant in processing such information for fear of being reproved for doing so. Thus, investors will have to self-analyze the situation and decide their investment, and the consultative role of securities firms is hardly ever activated.[204]

Listed companies themselves have their own concerns. For them, the shortage of information on the stock trading center mainly stems from the lack of concrete and necessary guidance from either the SSC or the Stock Trading Center. As stated by Nguyen Thi Ngoc Phuong, Vice Director of Lafooco:

> *So far, we merely disclose information on our own initiative since we have been thinking that investors need information. Nobody has told us how to disclose information and to what extent information should be disclosed.*[205]

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[199] See "Thi truong chung khoan thieu thong tin" [Securities Markets Fall Short of Information] (Nov. 29, 2001), http://vnexpress.net/Vietnam/Kinh-doanh/Chung-khoan, visited Dec. 24, 2001. Hereinafter, "Securities Markets Fall Short of Information".

[200] See "Nha dau tu van 'doi' thong tin" [Still Investors in 'Hunger' for Information] (Apr. 27, 2002), http://vnexpress.net/Vietnam/Kinh-doanh/Chung-khoan, visited May 1, 2002. Hereinafter, "Still Investors in 'Hunger' for Information".

[201] See "Securities Markets Fall Short of Information", above n. 199.

[202] See "Nhieu cong ty niem yet vi pham viec cong bo thong tin" [Many Listed Companies Violated Information Disclosure Requirements] (Nov. 22, 2001), http://vnexpress.net/Vietnam/Kinh-doanh/Chung-khoan, visited Dec. 25, 2001. Hereinafter, "Many Listed Companies Violated Information Disclosure Requirements".

[203] See "Still Investors in Hunger for Information", above n. 200.

[204] See "Securities Markets Fall Short of Information", above n. 199.

[205] Ibid.

Even the monthly reports listed companies have to file with the SSC are said not to be useful. According to Pham Thi Loi, the Financial Director of SACOM:

> *[M]onthly reports filed with the SSC tell the public almost nothing, since in order to get accurate figures concerning the business-financial situation of companies, such reports must be made on a quarterly basis.*[206]

Facing these problems, the SSC has its own observation. Bui Thanh Huong, Director of the Department for Securities Trading Management of the SSC, seems to attribute all failure of the implementation of information disclosure requirements to securities firms. She maintains that a number of directors of securities firms have been, at the same time, carrying out too many functions so that they cannot pay enough attention to information disclosure.[207]

Perhaps a report delivered at a symposium on "Improvement of Information Disclosure Regime on Vietnam Securities Markets" held by the SSC in Ho Chi Minh City on November 20, 2001, gives the most objective comments on the implementation of the regime. According to this report, on the one hand, information disclosure is entirely new to market participants, so that most of them often violate the disclosure requirements.[208] They lack experience in dealing with this area. They do not perceive the importance of information disclosure. On the other hand, there has not been a good coordination between different channels of information; a unique form for information disclosure has not been available; and there are many overlaps between statutory documents regulating this area of the securities market.[209]

A Case Study:

In fact, a number of violations of information disclosure regime by securities firms and by issuing companies have been reported.

Hoang Duc Long, chief inspector of the SSC, has admitted that some securities firms have breached the disclosure regulation. These firms give priority to their large customers, with the result that these customers could manipulate share prices.[210] However, it has not been reported which measures, if any, have been taken to deal with such violations.

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[206] Ibid.
[207] Ibid.
[208] The author seems to imply that most of the violators are not aware of the fact that they are violating the law.
[209] See "Many Listed Companies Violated Information Disclosure Requirements", above n. 202.
[210] See "Dirty Play Drives Market Off Course" above n. 198.

One violation by a listed company, HAPACO (Hai Phong Paper Shareholding Company) was publicized on May 28, 2001.[211] HAPACO was accused of breaching the information disclosure regime when it said that it would sell 30,000 shares to raise funds for a project in which a Kraft paper plant was to be built. According to Tran Dac Sinh, director of the Securities Trading Center, *"[T]he information was released before the authorities had approved the project. The move (putting share trading on the alert) is aimed at protecting the interests of stock investors and balancing market stability."* Although the volume of HAPACO shares traded after that was a little bit lower than in earlier sessions, nevertheless the price increased. It was predicted that the price would go up to 150,000 VND (around 10.30 USD) from less than 100,000 VND before the information was released.

Being questioned by the Securities Trading Center's officials, HAPACO's representative maintained that the accusation for violation of the information disclosure regulation was groundless and that they would appeal to the SSC. HAPACO disagreed with the Securities Trading Center's accusation and was concerned that the company share price might be falling, and that the prestige of the company might be degraded.

The Securities Trading Center, however, merely warned HAPACO that if the situation did not improve, they would use harsher measures such as revoking HAPACO's listing rights.

Perhaps the mere administrative measures are not drastic enough to prevent violation of information disclosure.

b. What are the attitudes of the 'trading-floor-ready companies' towards the current information disclosure regime?

Although the current information disclosure requirements are rather comprehensive, the Ho Chi Minh City Securities Trading Center, the first and the only trading floor to date, has experienced very quiet trading sessions, because of the small number of listed companies. It has recently been reported that equitized state enterprises account for around 700, only a 'handful' of them being keen to list.[212] By late December 2001, it was reported that the number of listed companies on the Securities Trading Center was about to touch eleven.[213] This figure can be contrasted with four listed companies at the time the Center commenced its operation in July 2000.[214] Some complain that the listing standards

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[211] See Nguyen Hong, Xuan Son, "Hapaco Stock Up Despite STC Alert" (May 28, 2001) *Emerging Markets Datafile, The Vietnam Investment Review*, <LexisNexis: Country & Region: Asia Pacific: World Sources Online, Emerging Markets Datafile>.

[212] See Nguyen Son, "Listing Sweetener Consider" (Oct. 8, 2001) *The Vietnam Investment Review*, <LexisNexis: Non-US News>. Hereinafter, Nguyen Son.

[213] See "Them hai doanh nghiep nhan giay phep niem yet" [Two More Companies Obtaining Listing Certificate] (Dec. 24, 2001) *Dau tu chung khoan* [*Securities Investment*], http://vnexpress.net/Vietnam/Kinh-doanh, visited Dec. 25, 2001.

[214] See "Profits Hard to Come by for Vietnam Stock Brokers" (Oct. 31, 2000) *Deutsche Presse-Agentur*, <LexisNexis: Non-US News>.

are too strict[215] to be met by many companies.[216] However, statistics shows that among 660 shareholding companies established from the equitization of state enterprises, there have been up to a hundred companies having a chartered capital of more than 10 billion dong.[217] A hundred companies meet the capital requirement while only about a tenth of them are listed on the trading center. Thus the quiet trading sessions in Ho Chi Minh City Securities Trading Center cannot be attributed to high listing standards.

More frequently-mentioned reasons for the hesitancy of trading-floor-ready companies to become listed companies include: (1) companies' fear of facing information disclosure duties, fear of being controlled and threatened by their competitors after being listed; (2) companies' concerns about the changes in the structure of shareholders and of company governance if they are on the trading floor; (3) and companies' poor knowledge about the operation of trading centers.[218]

Among these, the fear of facing information disclosure requirements remains the principal obstacle.[219] Companies are generally afraid of disclosing their financial situation to the public, and of facing transparent reporting standards. As a result, they merely said that they were going to list, but they did not do so.[220]

Equitized enterprises would be a potential source for listing on the trading center. It is said however, that the incumbent management boards are very concerned about their benefits and responsibilities after being listed.

> *Many equitized enterprises remain hesitant towards [sic] joining the official Ho Chi Minh City-base bourse due to perceptions [sic] that the negative aspects of official listing of their stocks, such as forced financial reporting requirements and increased pressure on management, outweighed the limited benefits they would gain from such a move.*[221]

Equitized enterprises are not only in fear of disclosing their secret information, but enterprise managers are also afraid of losing their positions and other privileges they have

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[215] These standards are already mentioned while discussing listing criteria facing issuers at the beginning of this Chapter.

[216] See "Vietnam Stock Exchange Set to Launch Trading", (Jul. 25, 2000) *Deutsche Presse-Agentur*, <LexisNexis: Non-US News>. It is reported that amongst 500-odd state-owned enterprises that were already equitized, fewer than 50 of them have met "Vietnam's relatively strict listing requirements"; see also Vu Long , "Forty Firms Meet Listing Criteria, But All Remain Hesitant", (Nov. 20, 2000) *Emerging Market Datafiles, The Vietnam Investment* Review <LexisNexis: Non-US News>. Hereinafter, Vu Long (Nov). It is reported that one of the main obstacles in the way of companies going to the trading floor is difficult financial situations.

[217] See "Duoc nhieu hay mat nhieu?" [Gain and Loss, Which one Has More Weight?], (2001) 76 *Dau tu chung khoan [Securities Investment]* 13, 13.

[218] Ibid; see also Vu Long (Nov.), above n. 216; and see also Anh Thi, '"Ngai' niem yet chung khoan? Xem xet dieu kien thich hop cho cac doanh nghiep" ["Hesitancy" of Being Listed? Considering Appropriate Requirements Imposed on Enterprises], (May 11, 2001) *Thoi bao kinh te Vietnam* [*Vietnam Economic Times*].

[219] See Vu Long (Nov.), above n. 216.

[220] See Nguyen Son, above n. 212.

[221] See Vu long, "Enthusiasm Sinks for Forced Floats of Equitized Firms" (Aug. 13, 2001) *Emerging Markets Datafile, The Vietnam Investment Review*,<LexisNexis: Non-US News>. Hereinafter, Vu Long (Aug.).

enjoyed if their enterprises have more shareholders, especially large ones. It was also complained that management board members - controlling shareholders - of a shareholding company often enjoy a number of privileges in the form of bonuses and other extra benefits. They also have powers to allocate profits in the company, and to decide the ways in which dividends are distributed.[222] This complaint does not seem to be consistent with the *Enterprise Act*, which vests the rights in the general shareholders' meeting to decide the allocation of annual dividends for an individual type of share.[223] However, it is very likely that in practice the actual decision maker concerning level of dividend to be distributed is the management board rather than the general shareholders' meeting, since it is often the case that minority shareholders cannot attend the shareholders' meeting and so cannot vote. The actual voters therefore are mainly large shareholders. Consequently, the decisions of such a meeting reflect their will.

Another sector that would also be a potential source for listing on the trading floor is the banking sector. However, there seem to be some obstacles as well on the ways banks access the trading floor. It was claimed that the lack of a legal framework setting out clear administrative and capital requirements for commercial banks had prevented banks from listing.[224] In practice, however, although a statutory rule that supports the participation of domestic joint stock commercial banks in stock trading centers has been promulgated,[225] the banks do not seem ready for listing. What has made banks hesitant to list is *"the effect that fluctuations on the fledging market would have on depositors' confidence"*.[226] Of course, it is not absolutely right to say that no banks want to list. Some of them have considered listing. But the minimum capital requirement and other listing criteria are the main obstacles to doing so.[227]

Perhaps most, or almost all, of the above-mentioned reasons result from the fact that trading-floor-ready companies have not been aware of the benefits a listed company will have, or of the benefits that would accrue from diversifying capital sources through securities markets. Such poor awareness of the advantages they would have after becoming a public company seems to be the main reason for their hesitancy. To solve this problem, educational measures might be useful. If the problem truly exists, Vietnam is not the only country experiencing such a problem. It is reported that other Southeast Asian countries have the same experience; that companies in these countries "*need a much*

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[222] See Hoang Quy Vuong, "Giao dich chung khoan trao tay tai Viet nam va nhung van de ton tai" [OTC Transactions in Vietnam Stock Market: Trouble Ahead!" (2000) 8 *Tap chi Ngan hang [Banking Review]* 49, 50, (text is in Vietnamese). Hereinafter, Hoang Quy Vuong.
[223] See the *Enterprise Act*, Art. 70.2.a.
[224] See Vu Long, "Exchange Sets Course for Bank Listings with Legal Framework", (Jul. 9, 2001) *Emerging Markets Datafile, The Vietnam Investment Review*, <LexisNexis: Non-US News>. Hereinafter, Vu Long (July).
[225] See Art. 2, *Decision 172/1999/ QD-TTg* dated Aug. 19, 1999 (promulgating the regulation of "The Rights of Credit Institutions in Establishing Securities Subsidiaries and Becoming Listed Companies"). Hereinafter, *Decision 172/1999*.
[226] Xuan Ha, "Joint Stock Banks Change Minds on Bourse Listing" (Sep. 10, 2001) *Emerging Markets Datafile, The Vietnam Investment Review*, <LexisNexis: Non-US News>.
[227] Ibid.

greater length of time to find out step by step about the true and tangible benefits of going public."[228]

Of course, one might also argue that those trading-floor-ready companies in Vietnam do not have big investment projects that require large finance, and therefore they do not want to go to the trading floor. In other words, for the time being, the Vietnam economy does not have large-scale projects and for this reason, it might not yet be the appropriate time for Vietnam to run a formal securities market. However, earlier in Chapter One, it was well documented that a formal securities market is indispensable to the economic development in Vietnam. The above-mentioned argument can thus be set aside.

4. How Does the SSC React?

As the number of listed companies still remains very modest after more than a year since the first trading center came into operation, a number of commentators think that listing requirements should be adjusted to enable more companies to be listed. However, the SSC has a strong position concerning this issue. The director of the Department for Securities Issuance Management of the SSC, Vu Thi Kim Lien, said that *Decree 48/1998*, especially listing requirements provided therein, would not be altered, at least over the next few years.[229] Pham Trong Binh, deputy director of the said Department, added: *"[i]t is up to the companies to meet the requirements, not for the government to eliminate these public protections, and many companies are able to do so"*.[230]

To cope with the fact that only a few listed companies are listed on the trading floor, the SSC recently revealed its new policy, *viz.*, to appoint companies that meet listing criteria to list. The SSC chairman, Nguyen Duc Quang, said *"besides the voluntary companies which meet listing requirements, some others will be selected and appointed to list"*.[231] According to a commentator, this is a way to force companies *"being bourse-ready"* to list.[232] Perhaps, using a mandatory manner to get more companies onto the trading floor would not generate positive results. In such a circumstance, an OTC (over-the-counter) market operating in its own legal framework would be a solution.

According to another source of information, for the time being the SSC has been consulting different governmental authorities and agencies to reduce listing requirements in order to augment the number of listed companies on the Ho Chi Minh Securities Trading Center.[233] The Commission's recent perception is that "the number of listed firms

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[228] See "Readying the Stock Market for Healthy Acceleration" (Feb. 11, 2001) *Vietnam Economy* http://ww.vneconomy.com.vn/en/stock/dir.cgi, visited Dec 25, 2001.

[229] Xuan Son, "Disclosure Rules Set for 'Tightening'", (Feb. 5, 2001) *Emerging Markets Datafile, The Vietnam Investment Review*, <LexisNexis: Non-US News>.

[230] Ibid.

[231] See Vu Long, (Aug.), above n. 221.

[232] Ibid.

[233] See Nguyen Son, above n. 212.

in the stock trading center is still very small, while existing requirements are keeping potential listers away" - said by a vice chairman of the SSC, Tran Xuan Ha.[234]

A proposal for the birth of an OTC market has also been processed. The Government Office has directed the SSC to finalize a legal framework for such a market by the September 1, 2000.[235] Recently, however Vu Bang, SSC vice chairperson, stated *"[w]e find it necessary to set up such a market but a legal basis is not available"*. He further stressed that *"[t]he requirements for monitoring this market are as strict as those for the official exchange, so we need to take careful consideration"*; and that to run an OTC market, a big investment in equipment to detect fake share certificates is required.[236] These statements imply that the opening of the OTC market in Vietnam is a long term project.

At present, the SSC has two schemes: (a) to create a second "board market", and (b) to adopt an OTC market. The first scheme allows it to set up a second board market in Hanoi, which will be similar to that in Ho Chi Minh City, but will only deal with small and medium-sized businesses that meet lower listing requirements. The proposed requirements include having a chartered capital of 5 billion VND, and having profitable business performance for at least one year. The second scheme legalizes an OTC market, which would be located in the same premises in Hanoi, in which the stock price would be negotiated by sellers and buyers. The SSC hopes to set up a second board market first and to adopt an OTC market later.[237]

It would be quite interesting if the second scheme is implemented. Then perhaps Vietnam would have a unique model of an OTC market compared with others all over the world, distinguished by the fact that it would have a defined physical location with a trading floor. However, all that the SSC has actually done so far in this regard has been to improve, to some extent, the current arrangements for the young securities industry in Vietnam.

III. WHETHER THE SCOPE OF THE INFORMATION DISCLOSURE REGULATION IS ADEQUATELY ADOPTED

1. The Narrow Scope of the Current Information Disclosure Regime

The current regulation of public offerings of securities only binds issuers that seek to make a public offering of securities that will be listed on a trading center. Article 3.1, *Decree 48/1998* providing for "Public Offering", reads:

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[234] Ibid.
[235] See Nguyen Hong, "Equitized Firms Need 'Notarized Trading Facility'", (Sep. 4, 2000) *Emerging Markets Datafile, Vietnam Investment Review,* <LexisNexis: Non-US News>.
[236] See "Regulator to Pilot OTC Stock trade", *Vietnam Economy,* http://www.vneconomy.com.vn/en/stock/, visited Oct. 26, 2001.
[237] See "Opinions Differ on Hanoi Bourse role" (Oct. 1, 2001) *Emerging Markets Datafile, The Vietnam Investment Review,* <LexisNexis: Non-US News>.

> *Public offering of securities to be listed on a centralized market, except for the offering of government bonds, shall be licensed by the State Securities Commission.*

The language of this article is ambiguous. It gives the impression that only those issuers that will have their securities listed on a trading center have to get an issuing license from the SSC for their public offerings. This leads to uncertainty about how an issuer knows that its securities will be listed on a trading center in the future so that it can define, even before the public offering is initiated, whether it will be subject to licensing requirement under Article 3.1.

The first paragraph of *Circular 02/2001* defines the scope of the public offering regulation. It does not, however, make the meaning of Article 3.1 any clearer. It even, once again, confirms that the regulation of public offering is merely applied to the issuance of securities mentioned in Article 3.1:

> *In order to implement Decree 48/1998/ND-CP, dated July 11, 1998, issued by the Government, stipulating securities and the securities market, the State Securities Commission hereby provides the following guidelines on public offering of shares and bonds to be listed on a centralized market.*

Perhaps in order to have an accurate idea of which companies will be subject to the licensing requirements, and thus which companies will fall into the scope of the information disclosure regulation, one should look at the statutory concept of "public offering", which was mentioned at the beginning of this Chapter. Such a concept confines public offerings to those made by issuers, at least 20 percent of whose equity/debt capital is held by outside investors. This figure falls to 15 percent where the equity capital or the total value of bonds to be issued by the issuer exceeds 100 billion Dongs.

Thus it is only those issuers who meet the above-mentioned criteria who will be subject to the information disclosure regime. The remaining issuers, therefore, are not to be bound by the current disclosure requirements.

Furthermore, continuous disclosure requirements, provided for in *Decision 79/2000*, apply only to listed companies. Non-listed companies, therefore, are almost facing no information disclosure.[238] Article 31.1 *Decision 79/2000* reads:

> *Securities trading centers, listed companies and fund management companies are subject to information disclosure requirements provided for in this regulation.*

[238] Except for their duty to file the annual financial statement with a Tax Authority and a Business Registry under Article 93 the *Enterprise Act*.

These provisions might cause public concern since investors that hold securities traded outside a formal trading center - unlisted securities - do not seem to be informed at all. This also means that they remain unprotected under the current regulation on information disclosures.

2. What might be Consequences of the Narrow-Scope-Disclosure Regime?

In practice, regardless of the lack of a statutory regulation, informal stock markets have been operated through a number of cafes and even through some websites.[239] In the absence of an organized market place, shares of equitized state enterprises have been traded on unorganized stock markets since before the time the first trading center was established. Even after the first securities trading center came into existence, such markets remained the places for share transactions of unlisted equitized enterprises. The informal market even seems more attractive to investors than the formal trading center. A recent report reveals that while the stock prices on the trading center tend to decline, those on the free market sharply increase (by the end of October 2002 the prices rose by 15-30% compared with those in March 2002); and that the increasing number of shareholding companies joining the informal stock market has made the market much busier.[240]

Small and medium investors in Vietnam are rather familiar with the Cafe Index X House in Ho Chi Minh City where they can trade via an electronic board updated on a weekly basis. Frequently quoted securities on such a board are confined within around 10 different types. A commentator satirically observes, *"Vietnam seems to follow the way that Britain experienced in the 17th century"*.[241] In such a market place, information concerning traded shares cannot be said to be sufficient, even if not actually poorly provided. Consequently, investors are in danger of being exposed to risks, especially when a minimum legal basis for the performance of the OTC market has not yet been made.

For the time being in Vietnam, the number of listed companies remains poor, because a pool of equitized enterprises does not meet the statutory requirements to have their shares listed, whilst other pools, for some reasons, do not want to be listed on a formal trading floor (as earlier mentioned). *Decree 48/1998* and other legal rules issued by the SSC merely govern transactions over securities issued in public offerings or/and listed securities. Obviously, there have been a huge number of transactions effected beyond the scope of the securities regulations, as well as the oversight of the SSC, and outside the securities trading center. In practice, the unorganized market seems even busier than the organized one.[242] In such a circumstance, an OTC market and a legal

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[239] See Thanh Ngoc, "Thi truong chung khoan co the anh huong toi nganh Ngan hang nhu the nao?" [How Can a Securities Market Affect Banking Industry?] (2000) 12 *Tap chi Ngan hang [Banking Review]* 59, 59.

[240] "Gia co phieu tren thi truong tu do tang manh" [Stock Prices in Free Market Sharply Increase], (Oct. 23, 2002) http://www.vnexpress.net/vietnam/kinh-doanh/chung-khoan, visited Oct. 24, 2002. Hereinafter, "Stock Prices on Free Market Sharply Increase".

[241] See Hoang Quy Vuong, above n. 222, 51.

[242] See "Stock Prices in Free Market Sharply Increase", above n. 240.

framework for its operation has become increasingly demanding, or at least, a system of information disclosure requirements with respect to non-listed companies should be taken into consideration. Perhaps at present, the only statutory provision, concerning such disclosure, which can be revoked, is Article 93, the *Enterprise Act.* This Article requires shareholding companies to file the annual financial statement with the state authorities (including the registry and the taxation authorities) after such a statement was approved in a general shareholder meeting. The Article has three Sub-articles. Sub-articles one and two read:

> *Within 90 days from the date of completion of the fiscal year, shareholding companies have to file the annual financial statement approved by the general shareholders' meeting with a tax authority and a registry.*
> *A resume of the annual financial statement must be furnished to all company shareholders.*

According to the language of this provision, it is not clear when the annual financial statement is to be sent to shareholders, before or after the general shareholders' meeting. This is of importance since, if it reaches shareholders before the meeting, that would help them to cast right and informed votes.

Sub-article three makes the company annual financial statement available to all those who show interest in the relevant company information. In other words, it gives public access to the company annual financial statement. It reads:

> *Every organization and individual can see or get a copy of such a statement in the registry office for a fee.*[243]

Furthermore, organizations and individuals can request the registry to provide them with information concerning company business registration[244] and ordinary shareholders can access the shareholders' list.[245]

According to the language of Article 93, it is clear that all shareholding companies face information disclosure duty, which is good. However, such a duty is merely required to be discharged on an annual basis. Thus, the Article cannot ensure public investors of timely access to material information of the relevant non-listed companies where such companies issue their shares publicly and when their shares are traded outside an organized trading center.

[243] To date, the regulation of the fee has not been created. Accordingly, Article 93.3 the *Enterprise Act* has not been implemented in practice.
[244] See *Enterprise Act*, Art. 20.2.
[245] Ibid., Art. 53.2.c.

IV. WHAT SHOULD BE DONE TO ACHIEVE BETTER OUTCOMES FROM THE INFORMATION DISCLOSURE REGULATION?

The current information disclosure regulation only binds those companies whose securities issuance falls within the purview of the "public offering", and listed companies. In that sense, the regulation is rather complete since it provides for various types of disclosure. However, in practice the market still falls short of information. This shortage is attributed to the intention of listed companies in disclosing information, to the lack of necessary guidance from the SSC and the Securities Trading Center to help listed companies properly to discharge their duties, and to the components and contents of the financial statement. The previous discussion has also revealed that the enforcement of the regulation is not drastic enough to enhance discipline, to prevent violations, and to equip market participants with the availability and timeliness of information. In view of such deficiencies, it is submitted that the following steps (arranged according to chronological priority for law reform) should be taken to achieve better outcomes from the information disclosure regulation.

1. A Call for Improvement of the Disclosure Requirements Applying to those Who Make a Public Offering and to Listed Companies

a. Statutory Provisions laying down the Ways in Which Information is Made Available to the Public should be Revised

a.1. The Need for Concrete Guidance and a Unique Form for Information Disclosure.

One of the problems that arise in the implementation of information disclosure requirements is the lack of concrete guidelines for companies to follow. Companies often disclose information on their own initiative and are not sure of how to do this for the best. The SSC or the Stock Trading Center should therefore release concrete guidance to help listed companies make necessary information available to the public.

The creation of a model form for company information disclosure applied throughout the country is also required. This is of importance since it would give a common standard for disclosing information and help securities firms as well as public investors easily to appraise and compare financial situations and business performance between different listed companies.

Apart from those, the training of corporate information disclosure staff is also required, to ensure that they can follow all guidelines, either from the SSC or from the trading center, without difficulty. This is to produce skillful staff capable of performing their information disclosure duties. In the absence of such well-trained staff, even full sets of guidelines and a unique form might not help to assure good information flow. At present, the securities regulation merely says that information disclosure activities of

listed companies is to be accomplished by the so-called *information disclosure staffs.* It does not, however, spell out any criterion such staffs have to satisfy in order to do the job.

a.2. The Need for More Accessible Ways for Public Investors to Obtain Company Information.

Meanwhile, according to *Chart No. 1*,[246] there are three information providers, namely issuers, securities trading centers and securities firms. However, there is uncertainty as to whether investors can directly get information from these providers. If the answer is "yes", a further question arises: if they are entitled to require a provider to furnish information to them by mail or facsimile, then who will bear such mailing/faxing costs? The current information disclosure regulation does not go into such a detail. For public investors, low cost of obtaining information is of significance. For this reason, in many countries, public investors do not have to pay any fee to obtain information.

Chart No. 1 also indicates various channels for information flow and through which public investors can access information concerning listed companies. These channels include: (1) obtaining annual printed releases of listed companies, (2) getting bulletins issued by the trading center, (3) accessing a computer network on trading centers or (4) going to the disclosure section of the trading center, to securities firms, and to the places specified in the issuing announcement, and (5) reading newspapers.

Obtaining printed releases of listed companies seems to be a good way in which public investors can learn more about the companies. Nevertheless, under the current regulation, such releases are only issued on an annual basis, which cannot guarantee the timeliness of information. This cannot be a good choice for investors. Moreover, it is unclear where such releases are available under the current regulation: in the office of the issuers or at the trading center.

Accessing a computer network on a trading center seems to be a reliable way to get information; getting information directly from securities firms or from securities distributors at specified places is also a good way. However, it is not an easy task, since there might be a long distance between the investors and the trading center, the specified places, or the relevant securities firms, especially when the number of firms remains limited.

Reading bulletins released by a trading center and newspapers seems to be an easy way for public investors to obtain information concerning the listed companies they wish to put money into. However, in remote areas, potential public investors might be available but it is hard for bulletins and newspapers to arrive promptly. Furthermore, the potential investors are not able to access the computer network on a trading center, nor can they easily obtain a printed release of the listed company. In this case, all available ways that can provide information to investors seem to be useless. Here one might argue that farmers, even well off ones, rarely put money in the hands of others (in this case, issuing and listed companies) which they do not know about, or only know very little about; that

[246] See this chart in Section I, Sub-section 1, item b of this chapter.

to build up farmers' confidence with the market is even harder than to do so with other investors. This is probably true in part. However, if and when farmers acquire a better understanding of the securities market and the benefits generated by it, then they might change their minds and desire to invest money in this new area.

A question that arises is how to enrich the manner in which public investors can access information to ensure that they are able to make prudent investment decisions. Even if a comprehensive set of disclosure requirements is available and all companies well meet such requirements, but the ways in which public investors can access information are not adequately provided for, then investors will remain inadequately informed.

In Japan[247] and in the US,[248] the issuers, underwriters, or securities firms are required to deliver to investors a copy of the prospectus that contains information provided in the registration statement filed with the governmental agency in charge of overseeing the securities market. This way of releasing information does not seem to be too complicated for use in transferring information in Vietnam.

Some possible ways to make information reach investors in the future in Vietnam include:

1. Furnishing information (by either mail or facsimile transmission) with an individual investor who shows his/her interest in the relevant security. Securities firms, issuers, or their distributors could easily perform this task and charge investors a fee, which might cover both the costs of the disclosure documents and of delivery. However, the fee, if available, should not be too costly, so that it will not have a negative impact on the investors' desire to obtain information.
2. Making the information available at the office of the issuing companies for investors who can easily access such an office. In both the US and Japan, public investors can get information by themselves at the office of the issuers by seeing a prospectus that has been examined by the stock market watchdog.
3. Making the information available in some other public media, other than newspapers, such as internet. The SSC or trading center should create different websites where the public can easily access information concerning public issuers and listed companies. This would be a useful way for investors to obtain company information, especially in view of the fact that the number of internet subscribers has been increasing in Vietnam.
4. Setting up a computer network among securities trading centers, listed companies, and securities firms, to speed up the transfer of information.

a.3. Company information should be furnished to shareholders before the general shareholders' meeting.

[247] See *Securities and Exchange Law of 1948* (2001 Japan), Art. 15.2.
[248] See Regulation C, Rule 460 of the US.

The *Enterprise Act*, Article 93.2 says that the resume of corporate annual financial statements must be announced to all shareholders. It does not expressly say, however, whether such a resume must reach shareholders before or after the general shareholders' meeting. Article 74 of the *Enterprise Act*, providing for the way in which a general shareholders' meeting is convened, states:

> 1. *The Person who convenes the General Shareholders' Meeting must send a letter of invitation to all shareholders at the latest seven days before the meeting date.*
> 2. *The meeting agenda and other materials necessary for discussion before decisions are approved must be attached with the letter of invitation.*

It is unclear whether the term "decision" embraces the annual financial statement under this Article. If one scrutinizes the *Enterprise Act*, one might become even more confused, since the answer could be both "no" and "yes". "No" can be inferred from the language of Article 80. One of the duties of the Management Board provided for in Article 80 is to deliver the "annual financial statement" at the General Shareholders' Meeting. Article 80 does not use the term "decision" for such a document. "Yes" can be drawn from the language of Article 77 (stipulating the way in which shareholders' meeting's decisions are approved). This Article uses the sole term "decision" to refer to all documents that need approval at a shareholders' meeting. *Decree 03/2000* guiding the implementation of the *Enterprise Act* does not make such provisions any clearer, either.

These uncertainties should be eliminated and there should be a provision explicitly saying that the resume of the annual financial statement must be filed with shareholders before the general shareholders' meeting. This would allow shareholders to study the statement in advance and enable them to cast appropriate and prudent votes.

b. The Gaps in Statutory Provisions on Information Disclosures in Tender Offers should be eliminated

Information disclosures required in tender offers provided for in *Decree 48/1998* are too general, as previously discussed. Meanwhile, the Decree fails: (1) to distinguish the circumstances where a group of persons/organizations constitutes a statutory person that buys more than 5% of the voting shares of an issuer, triggering an information disclosure duty; and (2) to define which information must be disclosed. The revised provisions should therefore: (1) specify the situation where two or more persons/organizations purchase, in collusion, more than 5% of the voting shares of an issuer and impose an information disclosure responsibility on them; (2) define which information is necessary to include in the report. In addition, the Decree merely requires the acquirers to report to the stock trading center. It would be more appropriate if such a report were to be filed with the SSC as well as being furnished to the issuers.

2. The Need for Disclosure Requirements applying to Companies Whose Securities Offerings Do not Fall into the Purview of the "Public Offering", and to Non-listed Companies

The second biggest problem with the current information disclosure regime is, perhaps, the absence of information disclosure requirements applying to companies whose securities issuance does not constitute a "public offering" within the purview of Articles 2.2, 6.5 and 8.2, *Decree 48/1998*, and on non-listed companies.

In practice, the number of companies that meet listing standards is limited, and even amongst companies that already meet listing requirements, not all are willing to list. This leads to a pragmatic problem since non-listed companies seeking pecuniary recourse from the public are numerous, but not subject to either offering disclosure or continuous disclosure requirements prescribed in the current securities regulations.

Obviously, in such a circumstance, a legal framework for the operation of an OTC market with a comprehensive information disclosure regulation is urgently required. Such a regulation should embrace both offering disclosure and continuous disclosure requirements, to ensure that public investors are well informed. It is important that relevant shortcomings of the current disclosure regime applying to listed companies should be examined so as to maximally avoid similar statutory deficiencies in its future counterpart regime applying to non-listed companies. In such a regime, possibly all types of disclosure requirement should also be laid down as binding on non-listed companies.

In Japan, a company, whether listed or not, having more than 500 million Yen of legal capital, and having 500 shareholders or more, is required to report to the Prime Minister.[249] Similar provisions have also been adopted in the US.[250]

3. The Need to Adopt Comparable Accounting Rules and Independent Auditing

a. Accounting rules

As for financial statements, types of information included in the statement should be simplified to enable companies cope well with reporting work, especially when human resources in accounting and auditing in Vietnam remain constrained. The future contents of the financial statement should be redefined to make it useful not only for taxation purposes but also for investment purposes. Attention should also be paid to the components of the financial statement. Possibly, the statement should reflect the changes in reserved profit so that it would become more informative and useful for investors.

These improvements are of importance in bringing Vietnam accounting rules closer to those adopted elsewhere. If internationally comparable accounting standards can be

[249] See *Securities and Exchange Law of 1948* (2001 Japan), Art. 24.1.4; see also *Enforcement Regulation of Cabinet*, Art. 3-6.2.
[250] See the *Securities Exchange Act of 1934* s 12(a) & (g), 15 USC s 78*l*.

achieved in Vietnam, the country's securities market might become more attractive to foreign investors. Foreign investors will refrain from investing in the securities market of a country if they cannot compare the financial conditions of that country's companies with those in other countries because each country adopts a different accounting system. No country should ignore the fact that an internationally comparable accounting law plays a significant role in making up the attractiveness of a securities market.

b. Independent Auditing for All Shareholding Companies.

Under the *Enterprise Act,* independent auditing only applies to a number of shareholding companies, as earlier mentioned.[251] To single out a number of companies whose financial statements need not be audited might give the opportunity for company's officers to commit fraud. A requirement that an independent auditor inspect a company's financial statements is thus a significant protective measure against fraud by the company's officers.[252] In future, discrepancies between different auditing requirements adopted by the *Enterprise Act,* the securities regulations, and the accounting regulation should be eliminated. It may be a good idea if auditing requirements apply to all shareholding companies. For big companies, an audit might be required on a short-term basis while for small companies an audit might be required on a longer-term basis.

c. The Need for a Supervisory Body Overseeing Auditing Practices

Possibly, in order to ensure that the public good in independent auditing receive appropriate consideration at all times, there is a need for a supervisory body overseeing audit practices. That body should be charged with the responsibility of reviewing and evaluating how independent audits of the financial statements of public companies are performed and to consider whether the recent trends in audit practices serve the public good. This body should report to the SSC where it finds weaknesses in and failures of the audit process so that the SSC can act in response to such problems in a timely manner to avoid serious consequences that might occur.

4. Possible Answers to Practical Problems

In Section I of this chapter, two main practical problems were mentioned, namely: non-compliance with the current information disclosure regime; and the hesitance of trading-floor-ready companies to become listed companies.

Non-compliance. On the whole, non-compliance with the law often derives from two facts: a general lack of adequate statutory provisions to enforce the law, and the weakness of enforcement mechanisms. It can be said that both facts have been applicable in the context of Vietnam.

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[251] See Section II, Sub-section 2 of this Chapter.

[252] See "General Principles of Company Law for Transition Economies", (1999) 24 *Iowa Journal of Corporation Law* 190, 287.

So far, sanctions for violation of securities regulation have merely been adopted at the administrative level. Although *Decree 48/1998* provides for disciplinary, administrative, criminal, and civil sanctions, to date the government has only issued one single rule governing administrative violations in the field of securities markets. *Decree 22/2000*[253] provides for rather comprehensive treatment of administrative violations of the regulation of public issuance of securities. Such treatment falls into four categories: fines ranging from 5 million to 50 million Dong (around 300 to 3000 USD); supplementary sanctions (suspending or withdrawing issuing license; confiscating the entire turnover from services provided by the violators); and other sanctions.[254]

Despite the existence of such administrative sanctions, in practice violation of the information disclosure regime do occur. This suggests that sanctions that are more severe should not be ignored as a means of putting market participants under appropriate discipline. Possibly, what public investors need is not many further laws and regulation to protect them, but rather more drastic enforcement of existing laws by the SSC.

Companies' Hesitancies. The problem of negative attitudes of bourse-ready companies towards going public to raise funds can be solved in various ways.

The main reason that triggers companies' hesitancy to become listed is the fear of facing information disclosure duties after being listed. Perhaps a solution for the immediate future would be for information disclosure duties to be imposed on very big shareholding companies with a high number of shareholders and high equity capital, regardless of whether they are listed or not. This could be done by revising the *Enterprise Act* so as to legalize such duties. At present, the *Enterprise Act* merely requires all shareholding companies to disclose information on an annual basis, as earlier discussed. Such a requirement should be broadened by requiring these companies to disclose information on a more timely and frequent basis.

Of course, such a statutory approach might have burdensome implications at governmental authority level, since it would not be an easy task, in terms of human resources, to cope with the screening of information filed with the authority by shareholding companies. Nevertheless, this would be a good measure to eliminate companies' fear of facing information disclosure duties, which in turn can be a hurdle on the way to listing on trading floor.

Another alternative is that the government could intervene with the status of the equitized-state-enterprises as a controlling shareholder. This option is feasible since, in many equitized-state-enterprises, the state holds a block of shares that enables it to keep control of the newly formed shareholding companies.[255]

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[253] This *Decree*, dated July 10, 2000, promulgates the "Regulation of the Treatment of Administrative Violations in the Field of Securities and Securities Markets".

[254] See Art. 4.

[255] *Decree 44/1998* required the State to be a controlling shareholder in a number of shareholding companies converted from state enterprises. Recently, *Decree 64/2002*, although it does not explicitly say so, provides for four forms of equitization. In enterprises that are equitized under the first three forms, the state still remains a shareholder, even a large shareholder, with those transformed into shareholding companies under the first and second forms. For further information, see Section II, Sub-section 2, Chapter I of this paper.

Apart from that, educational measures should also be employed to help the corporate community to understand the benefits of becoming listed companies. Such benefits are no longer confined to listed companies but also extend to public investors. That is because, first they can ensure that the capital demands of listed companies can be met; and secondly, public investors can be maximally protected through transparent disclosures made by those listed companies. To execute such measures, the SSC and the stock trading centers should have websites that can equip the general public with knowledge of securities markets in general and of the benefits of having a transparent information disclosure system in particular.

CHAPTER III
WHETHER THE ANTI-FRAUD REGULATION CAN FOSTER A HEALTHY MARKET

Together with the information disclosure regime, the anti-fraud regulation plays a significant role in protecting public investors and in ensuring a healthy market. This chapter will probe in depth the current anti-fraud provisions in order to draw out statutory gaps that should be filled and regulatory weaknesses that should be eliminated so as to achieve better outcomes from the anti-fraud regulation. It argues that owing to the sparse language of the regulation and the absence of a legal foundation for investors' rights of action, the regulation will fail to prevent manipulative and deceptive practices. It further maintains that the entire prohibition of short sale and margin trading will deprive the Vietnamese securities market of strongly supporting instruments.

In explaining the need for anti-fraud provisions in securities laws, David L. Ratner maintains:

> *・・・since the complexity of securities invites unscrupulous people to attempt to cheat or mislead investors and traders, the securities laws contain provisions prohibiting a variety of fraudulent, manipulative or deceptive practices. These provisions have been applied to a wide range of activities, including trading on "inside information," misleading corporate publicity, and improper dealings by corporate management.*[256]

This observation has been proven by securities regulations in countries all over the world, although the extent to which fraudulent activities are prohibited varies from country to country.

In Vietnam, the core legal rules governing securities and securities markets, *Decree 48/1998*, includes an entire chapter, Chapter VIII specifying activities that market participants are either prohibited or restricted from doing. The prohibited activities include: insider trading, market manipulation, misinformation, short selling, and credit transactions and lending securities.

In contrast to the regulation of abusive market practices and anti-fraud provisions in the securities laws of the US and of Japan, Chapter VIII, *Decree 48/1998* is far simpler. In fact a general lack of definition concerning prohibited activities can be seen in it, and it seems that the chapter merely gives a list of prohibited activities. It is the purpose of the following sections, then, to discuss the most serious problems of the regulation.

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[256] See David L. Ratner, *Securities Regulation: Materials for a Basic Course*, (3rd ed, 1986), 2. Hereinafter, David Ratner (3rd ed, 1986).

I. THE CURRENT ANTI-FRAUD REGULATION AND THE PREVENTION OF MANIPULATIVE AND DECEPTIVE PRACTICES

1. Insider Trading Regulation and the Prevention of Short-swing Trading

Article 70, entitled *"Insider Trading"*, prohibits specified persons from selling and purchasing securities when the information that can affect the securities' price has not been publicly disclosed by the issuing company. It does not, however, define precisely what information can be deemed to have a material impact on securities' price nor does it give a definition of "insider". It simply lists persons (including organizations) who must not directly or indirectly engage in purchasing and selling securities if the relevant information has not been made public by the issuer of such securities. Such persons include:

1. *Issuing organizations and relevant person(s);*
2. *Employees of issuing organizations and relevant person(s);*
3. *Large shareholders of the issuing organizations and relevant person(s);*
4. *Auditors and relevant person(s) of the auditing company that was appointed to audit the issuing organization;*
5. *Officials and employees of the SSC, of the Securities Trading Centers, Stock Exchanges and relevant persons; officials and government employees of other organs that have opportunities to approach inside information.*

Under Article 2.20, *Decree 48/1998*, the term "relevant persons" is construed as either individuals or organizations having been in a relationship of:

a. *Parent and subsidiary companies (if available);*
b. *Company and company managers;*
c. *A group of persons that entered into an agreement to takeover a company or to take control of the decision making of the company;*
d. *Parents, spouse, offspring and siblings.*

From the public servant's perspective, Article 70 seems rather broad since it includes all governmental officers and employees who can access inside information as persons that are not eligible for trade when such information has not been made public. A similar provision can be found in Article 6 (3), the *Provisional Measures on Prohibiting Securities Fraud* of China. Perhaps Vietnam has learnt from China's experience in this

respect, since China is also a country where *"administrative agencies are especially powerful and can directly affect a company's policy and activities"*.[257]

From the shareholders' perspective, it can be claimed that this provision is, to some extent, relatively narrow, since it merely prohibits large shareholders from trading on inside information; other shareholders, by implication, do not seem to be prevented from so doing. Large shareholders, pursuant to Article 2.26, *Decree 48/1998*, are those who hold 5% or more of voting shares of an issuer.

Article 53, the *Enterprise Act* while providing for the rights of ordinary shareholders in general, confers some important rights on shareholders or groups of shareholders who have owned more than 10% (or a smaller amount as prescribed in the company charter) of the company's common shares in the six consecutive months. Such rights include: nominating candidates to the Management Board and Supervisory Board; convening a General Shareholders' Meeting; seeing or getting a copy of the list of shareholders that are entitled to attend the General Shareholders' Meeting; and other rights as provided for in the *Act* and the company charter.[258] Although Article 53 does not use the term "large shareholder" to refer to such persons, it makes a distinction between 10% shareholders and others. As such, only 10% shareholders have the privilege of intervening in the company management apparatus and in the management of the company. Other shareholders, whether they hold 9.9% or less than 1% of voting shares, accordingly – and equally – do not have such a privilege. Thus, there seems to be no reasonable ground to impose a restriction on 5% shareholders in dealing with company shares while excluding the under-5% shareholders from subjection to that restriction.

So far, the regulation of insider trading, while at a first glance appearing expansive, merely lists the persons who are forbidden to trade. A definition of insiders and of information that can affect the securities price is still missing. For that reason, it cannot distinguish between insiders and non-insiders, and therefore it is difficult to impose liabilities on a non-insider who has obtained inside information by improper means, but has not directly traded, and has merely recommended others to trade on that information. *Decree 48/1998* has also failed at defining prohibited activities done by insiders, such as leaking inside information and making it possible for others to trade on inside information, or tipping, or recommending others to trade on a basis of inside information. *Decree 22/2000* seems to go further compared with *Decree 48/1998*, although it merely governs the administrative treatment of violators of the securities regulation. It imposes sanctions on any person who either uses or discloses inside information to another person so that either the former (insider) or the latter (tippee) can purchase or sell or make a purchase order or a sale order of such securities. Article 5.1.c. imposes administrative sanctions on the following activities:

[257] See Jay Zhe Zhang, 'Securities Markets and Securities Regulation in China', (1997) 11 *North Carolina Journal of International Law & Commercial Regulation* 557, 602.
[258] See Sub-Art. 2.

> *Using inside information to trade, or providing information to (or tipping) another person to make a purchase or to put a purchase order; or to make a sale or to put a sale order;*

Regulation of insider trading is a complicated matter. More detailed provisions are needed to ensure that the regulation at least covers those activities that need to be regulated. The current provisions under *Decree 48/1998* deal merely with part of insider trading. In practice, insider trading can be executed in various and sophisticated ways. With such simple language in Article 70, it is hard to impose sanctions on people engaging in insider trading transactions.

The American and Japanese regulations on insider trading might be useful to examine. In the US, both the *Securities Act* of 1933 and the *Securities Exchange Act* of 1934 do not explicitly mention insider trading. Two provisions, Sections 10(b) and 16, were inserted in the 1934 Act to deter fraud in the sale of securities and to achieve full and fair disclosure of the character of securities.

Section 10(b) proscribes the use of manipulative and deceptive devices to defraud in the purchase and sale of securities. The Section makes it criminal to trade *"in contravention of such rules and regulations as the Commission may prescribe"*. The said rules and regulations, which were created by the Commission, the SEC, have been known as *Rule 10b-5*. This *Rule* generally lays down sanctions against purchases or sales by persons who have accessed information that is not known by those with whom they deal or by traders in general. *Rule 10b-5* makes it unlawful for any person

> *(1) to employ any device, scheme, or artifice to defraud,*
> *(2) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of circumstances under which they were made, not misleading, or*
> *(3) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.*

The US case law has also accepted a theory of insider trading which is composed of two elements: *"(i) the existence of a relationship affording access to inside information intended to be available only for a corporate purpose, and (ii) the unfairness of allowing a corporate insider to take advantage of that inside information by trading without disclosure."*[259] From the US Supreme Court's position, any securities transaction bearing these two elements will be deemed guilty under *Rule 10b-5*.

Section 16(a) requires 10% shareholders, officers and directors of listed companies having shares registered under Section 12 of the 1934 Act to file a report with the SEC no

[259] See *Chiarella v United States*, 445 US 222, 227 (1980).

later than ten days after the end of the month the acquisition or disposition of their company's shares occurred. Recently, the time in which such filings must be made has significantly reduced under Section 403 of the *Sarbanes Oxley Act of 2002*. Pursuant to the new provision, Section 16 insiders must file reports within two business days following the execution of a securities transaction.

Where the sale and purchase of securities by such persons were effected within a period of less than six months, their company is entitled to confiscate the profits (short-swing profit) derived from such sale-purchase transactions.[260]

In Japan, views on whether insider trading regulation has been adopted since the passage of the *Securities and Exchange Law* of 1948 is not unanimous. A number of commentators think that insider trading provisions have been codified in the *Securities and Exchange Law* almost as long as the United States, i.e. since 1948, when Japan first enacted the Law. The evidence is that Article 58 of the Law is much like the US Rule 10b-5. Most of commentators agree that the provision is best interpreted to cover insider trading practices.[261] Another view, however, says that prior to 1988, a proper insider trading regulation had not been available in Japan, and that only the 1988 amendment of the *Securities and Exchange Law* has effected considerable changes in this area.[262]

The current Law, as amended in 2001, explicitly governs insider trading by the four articles: 166 and 164 entitled "Prohibited Acts of Corporate Insider" and "Restitution of Undue Profit Made by Officer or Major Shareholder", respectively; Article 163 requires the filing of a report on trade in specified securities; and Article 167 prohibits insider trading in tender offers.

Article 166 while prohibiting insiders from sale, purchase, assignment and acquisition of specified securities of listed companies, explicitly defines insiders,[263] and tippees,[264] and also construes the meaning of the relevant terms used in the article, such as "material fact", "made public", "parent company".[265]

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[260] See *Securities Exchange Act of 1934* s 16 (b), 15 USC s 78p (2002).

[261] See Louis Loss, Makoto Yazawa and Barbara Ann Banoff (eds), *Japanese Securities Regulation*, (1983), 192. Hereinafter, Louis Loss *et al* (eds).

See also Ramzi Nasser, "The Morality of Insider Trading in the United States & Abroad" (1999) 52 *Oklahoma Law Review* 377, 382. Hereinafter, Ramzi Nasser.

Article 58 reads: "*No person shall (1) employ any fraudulent scheme or artifice with respect to buying, selling or other transactions in securities; (2) obtain money or other property by using documents or any other representations which contain a false statement with respect to a material fact, or omit representation of a material fact which is necessary in order to make such statements made not misleading; (3) make use of any false quotation for the purpose of inducing the purchase or sale or other transactions in securities.* "

Lately, for the first time in history, in February 1999, the Japanese Supreme Court ruled on an insider trading issue. For further information, see Masanori Hayashi, "Japanese Insider Trading Law at the Advent of the Digital Age: new Challenges Raised by Internet and Communication Technology" (2000) 23 *Hastings Communication & Entertainment Law Journal* 157, 159.

[262] See Hiroshi Oda, *Japanese Law*, (1st ed, 1999), 288.

[263] See items (1) - (5) of Sub-article 1.

[264] See Sub-article 3 of this article.

[265] See Sub-article 2, 4 and 5.

Article 164, similar to Section 16 of the American *Securities Exchange Act*, discourages officers and major shareholders of a listed company from taking advantages of confidential information they obtained by their positions. If such circumstances do occur, profit gained from the relevant transaction will be confiscated for the company.

Article 163 requires corporate officers and shareholders owning 10 percent or more of shares to file with the Prime Minister a report on his/her purchase/sale of the said shares. Filing must be made within the first 15 days of the month following the month of purchase/sale. This Article and Article 164 are made to prevent short-swing trading.

Article 167 was almost designed in the same pattern as that of Article 166, but its scope is confined to the regulation of insider trading in tender offers.

2. Market Manipulation Regulation and Stabilization Transactions

Similar to other articles, Article 73 also fails to define the term "manipulation", even though it is used in the title of the Article: "Market Manipulation". It specifies that organizations and individuals are prohibited from engaging either directly or indirectly in a number of activities. It reads:

> *Organizations and individuals must not directly or indirectly carry out the following activities:*
> 1. *Purchasing, selling a security in collusion with another person in order to create an artificial supply, demand in such security;*
> 2. *Engaging in purchasing or selling transactions without delivering title to the securities;*
> 3. *Continuously purchasing securities with high prices, or continuously selling securities with low prices;*
> 4. *Re-purchasing or re-selling their own securities (in the case of issuing companies) in the absence of SSC permission.*

According to the language of the Article 73.1, the two transactions, purchasing and selling, do not seem necessarily to be simultaneously effected. Rather the fact that the transaction is done *"in collusion with another person in order to create an artificial supply, demand"* seems to decide the unlawfulness of the transaction.

Article 5 *Decree 22/2000*, while providing for sanctions to be imposed on persons who violate securities regulation, lists a number of violation activities. Sub-article 1.a, although mentioning the same activities as those under Article 73.1 *Decree 48/1998*, seems to give a different meaning. It reads:

> *Simultaneously purchasing or selling a security on one's own initiative or in collusion with another person in order to create artificial supply, demand or artificial prices.*

The term *"simultaneously"* does not agree with the word *"or"* in the language of the provision. Perhaps this provision should read: *"Simultaneously purchasing and selling a security・・・"* Regardless of that, this provision clearly mentions "wash trading", while Article 73.1 does not.

Anti-manipulation is a complicated task, and it demands a corresponding complex regulation. Sometimes it is hard to draw the line between manipulative and legitimate transactions, especially when such transactions are entered into by some specific groups of people in stabilization transactions and in contested takeover bids. The US securities regulation appears to have detailed rules dealing with these two areas.

Stabilizing activities are often performed by participants in a public offering if at the same time they bid for or purchase the same securities. Stabilizing activities are also employed by issuers in repurchasing their own securities on the market to influence the price of such securities.

In the US, activities in the former case are deemed unlawful if they are conducted in contravention of rules and regulations prescribed by the SEC.[266] Such rules[267] are enshrined in *Regulation M*. The regulation focuses on the bidding and purchasing activities of persons that have connection with a public distribution (the purchase of the securities being distributed). *Regulation M* makes it unlawful for issuers, selling security holders, underwriters and other distribution participants, directly or indirectly to bid for or to purchase any unit of the distributing securities in an attempt to induce any person to bid for or to purchase such securities during the applicable restricted period.[268] The Regulation also forbids any person who purchases securities from any distribution participant to cover a short sale occurring during a specified period of time.[269]

There are, however, some exceptions under which two types of conduct can be permitted: (1) broker-dealers may engage in market making transactions in NASDAQ securities without violating Rule 101;[270] (2) syndicate members may conduct stabilization transactions to prevent or retard a falling market price of a security, provided that such transactions are effected in conformity with pricing requirements.[271]

Activities in the latter case (issuers repurchasing their own securities) are subject to Rule 10b-18. Pursuant to this rule, an issuer and its affiliates are not prohibited from repurchasing during any trading day, provided that the purchase meets the four conditions concerning the number of brokers or dealers that effect the purchase, time of the purchase, price of the purchase and volume of purchase. Such conditions include: the purchase is made through only one broker or one dealer on one single day; the purchase is not the opening transaction nor is it made during the last half hour of the trading day; the purchase is not effected at a price exceeding the highest current independent sale price;

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[266] See *Securities Exchange Act of 1934* s 9 (a) (6), 15 USC s 78i (2002).
[267] There are six rules, numbered from 100 to 105.
[268] See *Regulation M*, Rules 101 & 102.
[269] Rule 105.
[270] Rule 103.
[271] Ibid, Rule 104.

and the total of such purchases is equal to or less than 25% of the average daily trading volume for the preceding four weeks.[272]

In contested takeover bids, manipulative activities are very likely to be conducted. Dealing with this problem, the US law makes it unlawful for any person who misrepresents or omits any material fact in connection with any tender offer.[273] The two criteria, namely misrepresentation and omission, are of importance in defining whether or not a manipulative device was employed in a tender offer. In the absence of these two elements, even if the offer occurs in a way that affects the price of the target shares to the detriment of the target company shareholders, it will not be deemed a manipulative transaction.[274]

Going back to the case of Vietnam, the current anti-manipulative provisions are far simpler than those dealing with such complicated circumstances in the US legislation. Stabilizing activities in a distribution of securities seem to have no room in the regulation except for the vague language of Article 73.4, *Decree 48/1998,* pursuant to which issuing companies are prohibited from repurchase or resale of their own securities in the absence of SSC permission. It is unclear whether this provision refers to the purchase by issuers in a public distribution of securities or in a secondary market.

The latter case, repurchases in a secondary market, or share buybacks, is provided for in the *Enterprise Act,* but in a sparse manner. Shareholding companies are eligible to buy back maximally 30% of common shares, or maximally 100% of other kinds of shares, provided that the purchase of more than 10% of the total number of the outstanding shares of each kind is decided by the General Shareholders' Meeting; the purchase of a lower amount is to be decided by the Board of Management.[275] In buying back shares, the amount of shares companies purchase from individual shareholders must correspond to the stock ratios the shareholders hold in the companies.[276]

The *Enterprise Act* does not say that such companies have to get permission from either the SSC or a Securities Trading Centre to buy back their outstanding shares. However, pursuant to *Decree 48/1998* and *Decision 79/2000,* it seems that the companies in question will have to get an approval from the SSC or the Securities Trading Centre. The Decree and the Decision do not seem to agree with each other in defining a unique authority that is in charge for granting such permission.[277] Thus, when a listed company desires to buy back its shares, it will have to get the approval from (1) either the General

[272] Rule 10b-18.
[273] See *Securities Exchange Act of 1934* s 14(e), 15 USC s 78n (2002).
[274] *Schreiber v. Burlington N., Inc.,* 472 US 1, 7, (1985).
[275] See the *Enterprise Act,* Art. 65.
[276] Ibid, Art. 65.3. It can be said that company shareholders are equally treated in share buyback. This principle is also adopted in Japan.
[277] Article 73.4, *Decree 48/1998* merely implies that companies have to get permission from the SSC in such a case. Article 54, sub-articles 1, 2 & 3, *Decision 79/2000* states that the authority responsible for approving buyback of shares is the Securities Trading Center. It is unclear whether buyback of shares needs approval from both the SSC and the Securities Trading Center or from only one of the two organs.

Shareholders' Meeting or the Board of Management, depending on the repurchased amount; and (2) the SSC or/and the Securities Trading Centre.

Decision 79/2000 goes further than the *Enterprise Act* in that it lays down some limits on company repurchase. That is, listed companies can only put one order to purchase at least 3% and at most 5% of the total approved amount. In special circumstances, they can put an order to buy back more than 5%, provided that they get permission from the relevant securities trading centre.[278] Where a listed company buys back more than 25% of its voting shares, it has to do so by making a bid.[279]

Decision 79/2000, however, does not set out any limit on the repurchase price, nor does it lay down any requirement on the time the repurchase order can be made. These criteria are vital to the prevention of manipulation by listed companies in share buyback transactions. In the absence of such criteria, listed companies might have potential opportunities to manipulate shares prices under the form of share buyback.

The current laws seem merely to deal with share buybacks. As such, participants in a public distribution cannot bid for or purchase the offering securities in order to stabilize the securities' price. In practice, stabilization transactions in a distribution are important to underwriting companies, since such transactions are sometimes required to support the purchases of securities to mitigate risk that might be incurred by the underwriter of such issue. When revising the antifraud provisions, the law makers might have to think of making a more detailed regulation to cope with new and even conventional manipulative activities that have been found in other securities markets outside Vietnam.

3. Misinformation Regulation and the Prohibition of Omission of Information

Article 71, entitled "Misinformation", proscribes the improper dissemination of information. Under Sub-article 1, "*[o]rganizations and individuals must not announce or circulate untrue information*". This provision, however, is too simple to make it clear whether it refers only to a false statement included in an application dossier filed with the SSC, or whether any false statement made in any form (either oral or written) will fall into the scope of the provision.

Furthermore, Sub-Article 1, while prohibiting false statements, does not seem explicitly to forbid the omissions of material facts in a statement concerning the issuance or trade of securities that would affect the investment decisions of public investors. Since a true statement does not necessarily mean a full statement, it is very likely that the person in question can make a true statement and yet omit a number of items of material information. As such, the statement could lead other persons to purchase or sell a security at a price misleadingly affected by such a statement. Clearly the provision inadvertently leaves room for such statements to be made.

[278] Ibid, sub-article 2.
[279] Ibid, sub-article 3.

It might be useful to look at the way the Americans deal with this issue. Section 18(a) entitled "Liability for Misleading Statements", the *Securities Exchange Act of 1934* of the US, reads:

> *(a) Any person who shall make or cause to be made any statement in any application, report, or document filed pursuant to this title or any rule or regulation thereunder or any undertaking contained in a registration statement as provided in subsection (d) of section 15 of this title.... shall be liable to any person (not knowing that such statement was false or misleading) who, in reliance upon such statement, shall have purchased or sold a security at a price which was affected by such statement, for damages caused by such reliance, unless the person sued shall prove that he acted in good faith and had no knowledge that such statement was false or misleading.*

This section explicitly prescribes: (1) liability imposed on any person that makes statement on which another person buys or sells a security at a price affected by the statement; (2) a statement must be inserted in documents filed with the SEC under the *Securities Exchange Act of 1934*. It does not use the term "false or untrue statement" in the first place. Rather the term "any statement" is employed, provided that it has connection with the purchase or sale of a security at a price affected by such a statement. In that way the term "any statements" can cover both material misstatement and omission of material facts.

Sub-article 2, Article 71, *Decree 48/1998* refers to some organizations, namely the issuer, the underwriter and relevant persons, but it puts them in a narrower context compared with those in Sub-article 1. These organizations are banned from doing things that might mislead investors even before the issuer obtains an issuing license. It reads:

> *During the time the application dossier for securities issuance is being considered by the SSC, the issuer, the underwriter and relevant persons must refrain from advertising, offering and having other advertising-characterized activities that might result in investors' misunderstanding the securities to be issued.*

So, in relation to the purpose of advertising, offering and other related activities performed before the attainment of an issuing license from the SSC, the statutory prohibition of misleading activities only applies to the issuers, underwriters and relevant persons. Thus, the prohibition does not apply to a number of potential organizations that are very likely to be able to make misleading statements concerning the issuing or trading of securities, such as securities trading centers, appraisal agencies, law firms and accounting firms. None of these organizations fall within the meaning of the term "relevant person".

II. THE EXISTING ANTIFRAUD REGULATION AND THE PROMOTION OF A LIQUID AND HEALTHY MARKET

1. Should Short Sale be totally Prohibited?

The term "short sale" is not defined by *Decree 48/1998* either. Article 69, entitled "Short Sale", makes unlawful any sale of securities if the seller does not actually have title to the securities at the time of selling. It reads:

> *Organizations or individuals are prohibited from selling any security in any form if the organizations or individuals do not own such security at the time the transaction is effected.*

Owing to the failure in defining the term "short sale", this provision cannot explain in which situation the seller can be deemed to own securities.[280] It simply prohibits all persons, not only securities firms, from selling short in any circumstance. According to a government official, an entire prohibition of short sale is an innovative creation of Vietnam in order to prevent speculative short sales, the sort of activity that resulted in the East Asian financial crisis of 1997.[281] A question arising here, of course, is whether speculative short sale was the only or even the main cause that led to that crisis.

Economists seem to attribute the financial crisis to two main factors: (1) domestic policies and practices, and (2) the development of the global financial system, currency speculation and the behavior of large institutional investors.[282]

The former derives from a number of issues such as: weaknesses of financial institutions, and of regulatory or overseeing systems; a high number of risky investment projects conducted in the field of real estate and in the stock market; ineffective corporate governance and supervision; a credit boom by which corporations incurred high dollar-

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[280] See Rule 3b-3 issued by the US SEC, for example. This Rule gives a definition of "Short Sale": *"The term 'short sale' means any sale of a security which the seller does not own or any sale which is consummated by the delivery of a security borrowed by, or for the account of, the seller. A person shall be deemed to own a security if (1) he or his agent has title to it; or (2) he has purchased, or has entered into an unconditional contract, binding on both parties thereto, to purchase it but has not yet received it; or (3) he owns a security convertible into or exchangeable for it and has tendered such security for conversion or exchange; or (4) he has an option to purchase or acquire it and has exercised such rights or warrants: Provided, however, that a person shall be deemed to own securities only to the extent that he has a net long position in such securities."*

[281] See Vu Ngoc Nhung, "Hoan thien thi truong chung khoan Viet nam nham thiet lap nen tai chinh vung manh va hieu qua" [Completion of Vietnam Securities Market in order to Establish a Strong and Effective Financial Foundation], (Paper presented at the conference on *"Finance and the Development of Vietnam Securities Market"*, held by the Financial Research Institute, Finance Ministry, in Ho Chi Minh City, on May 22, 2001), 3. See also the appendix of the above-mentioned paper "Thu gui ong Andy Gent, Tong giam doc Ngan hang Hong Kong & Thuong Hai tai Vietnam" [Letter to Mr. Andy Gent, General Director of Hong Kong & Shanghai Bank in Vietnam], 9.

[282] See Noeleen Hezer and Martin Khor, "The Asian Financial Crisis: Causes, Consequences and Ways Forward" http://www.worldbank.org/devforum/speaker_heyzer.html, visited Nov. 4, 2002.

denominated short-term private debt, and weaknesses in legal structure as well as political accountabilities.[283]

The latter factor is said to have its root in the combination of deregulation and liberalization of the financial sector in most of the countries that were worst affected by the crisis; the increasing interconnection of the market and speed of transactions through computer technology; the development of large institutional financial players; and the speculation or short term investment that could move in and out very quickly across national borders.[284]

Here, causes of the crisis are classified into domestic and international ones and as such, problems with financial sector can be found in both areas, in parallel with other non-financial problems, and under various forms. Although risky investment projects in the stock market are mentioned, similar risky projects in real estate can also be seen. Furthermore, risky investment projects in the stock market were not the single financial problem. Others such as the credit boom, corporate high debts, and the combination of deregulation and liberalization of the financial sector in relevant countries, can also be found. As such, it is unclear whether speculative short sale, which was only one of the financial problems, dominated.

For the purpose of our study here, perhaps the interim report of the *Emerging Markets Committee, IOSCO,* gives a clearer picture of causes that led to the financial crisis. The report observes such causes from a different approach, by which all problems concerning financial market are grouped into one of the three main causes of the crisis. These three main causes are: (1) macroeconomic issues, (2) structural issues, and (3) financial market issues.[285]

The first cause refers to (a) capital flow surges that could generate benefits to developing countries, but could also bring along with them significant risks, especially in the absence of necessary pre-conditions to ensure the sound deployment of private capital flow; (b) the fact that large capital inflows received by many emerging markets in the early 1990s, along with the credit boom, enabled rapid and sustained economic expansion, which, in turn, led many of these countries to run significant current account deficits; (c) the loss of competitiveness arising from exchange rate policies adopted by most of the afflicted countries, which is also found to have been a crucial factor that caused the crisis; and (d) the confluence of all the above-mentioned factors.[286]

The second cause (structural issues) consists of (a) the deregulation and liberalization of the financial sector in the economies worst afflicted by the crisis; (b) the underdeveloped debt markets that caused the worst-afflicted economies to over-rely on banking finance; (c) the failure in regulating and supervising financial institutions; (d) the inadequate disclosure and weak corporate governance that resulted in significant

[283] Ibid.
[284] Ibid.
[285] See "The Causes of the Asian Financial and Economic Crisis", extracted from an interim report "Causes, Effects and Regulatory Implications of the Financial and Economic Turbulence in Emerging Markets" by the Emerging Markets Committee, IOSCO. http://risk.ifci.ch, visited Nov. 4, 2002.
[286] Ibid.

problems in the financial and corporate sectors of the worst-afflicted countries; and (e) distorted lending decisions as a result of a confluence of the above-mentioned factors.[287]

The third cause (financial market issues), as pointed out in the report, is composed of the three following factors: (a) the currency market activity or the sharp currency devaluation experienced by the South East Asian countries; (b) the use of OTC instruments, especially derivatives and off-balance-sheet items, that very likely triggered the crisis most severely; and (c) the financial contagion that resulted from an increasingly global and integrated financial system.[288]

According to the report, the crisis was clearly a consequence of various factors. If speculative short sales lay in the so-called "use of OTC instruments", it was merely one of the issues that occurred in the financial market, and the financial market issues were, in turn, merely one of the three principal causes that led to the Asian financial crisis. Therefore, speculative short sales were obviously not the only cause – indeed not even one of the principal causes – that triggered the financial crisis in Asia in the late 1990s.

Concerning the benefits generated by, and harms resulting from, short sales, there have been contrary schools of thought. It might be useful to quote the Report of the US Senate Committee on Banking and Currency:

> *The proponents of short selling contend that it is a necessary feature of an open market for securities; that in a crisis short sellers are useful in maintaining an orderly market; and that their activities serve as a cushion to break the force of a decline in the price of stocks. Its opponents assert that short selling unsettles the market, forces liquidation, depresses prices, accelerates declines, and has no economic value or justification.*[289]

The US SEC, while proposing rules and seeking public opinion on short sale regulation, points out two important benefits which short sales provide for the market, namely market liquidity and pricing efficiency.[290]

Market liquidity: when market professionals effect short selling transactions, they are offsetting temporary imbalances in the supply and demand for securities and thus are creating substantial market liquidity. Through securities professionals, short selling activities enrich the trading supply of stock, which in turn lessens the risk when investors might have to pay an artificially high price owing to a temporary shortage in supply.[291]

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[287] Ibid.
[288] Ibid.
[289] See Stock Exchange Practices, Report of Senate Comm. On Banking & Currency, S. Rep. No. 1455, 73d Cong., 2d Sess. 50 (1934). Quoted in Louis Loss & Joel Seligman, *Fundamentals of Securities Regulation*, (4th Ed. 2001), 797. Hereinafter, Loss and Seligman.
[290] See *"Proposed Rules"* (SEC), (Action: Concept Release; Request for Comments. Oct. 28, 1999), 17 CFR Part 240, [Release No. 34-42037; File No. S7-24-99] RIN 3235-AH84, Short Sales. 64FR 57996. <LexisNexis>. Hereinafter, *"Proposed Rules"* (SEC).
[291] Ibid.

Pricing efficiency: in an efficient market, prices fully manifest all interests of purchasers and sellers. When entering into a securities transaction, both the purchaser and the short seller expect to profit from the difference between the buying and the selling price. Usually a short seller in a security trusts that the security is overvalued and so its price will fall. By engaging in short sale transaction, that seller informs the market of his/her evaluation of future securities price performance, which in turn, contributes to securities pricing efficiency. By employing short sales to gain profit from price divergence between a stock and a derivative security (e.g. a convertible security or an option on that stock), arbitrageurs also add to pricing efficiency.[292]

The US SEC, although recognizing the above-mentioned benefits generated by short sale, has stressed that short sale can also be utilized as a manipulative tool on securities market.

Loss and Seligman, while considering opposite schools of thought over the advantages and disadvantages of short sale, also conclude that it is impossible to find out where the truth lay between these extreme views.[293] Regardless of such a controversy over short sale, in practice, the Dutch, French, Germans, British, and even the Americans, have all more or less eliminated the prohibition of short sales.[294]

Today short sales are often controlled rather than prohibited. Both the Japanese and the Americans seem to follow this approach. The *Securities and Exchange Law* of Japan reads:

> *No person shall do the acts set forth below in violation of the provisions of a Cabinet order.*
> *(1) To make the sale of, or the placement or acceptance of an order for the sale of, a security without owning, or by borrowing, such security (including such case as may be prescribed by a Cabinet order as one comparable thereto), or*
> *(2) To make the placement of an order to buy a security forthwith when the price of such security has risen from that at the time of the placement of such order and is equal to or above the limit price set by himself/herself, or to sell a security forthwith when the price of such security has fallen from that at the time of the placement of such order and is equal to or below the limit price set by himself/herself.*[295]

Pursuant to this provision, in Japan, short selling is only prohibited where the price of the relevant security drops (that is when the security can be sold at a price lower than the previous preceding selling price).

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[292] Ibid.
[293] See Loss and Seligman, above n. 289, 797.
[294] Ibid, 795 – 796.
[295] Art. 162: items (1) and (2).

In the US, short sale regulation has been adopted since 1930s under the *Securities Exchange Act of 1934* and the SEC's Rules. The short sale regulation is twofold: regulation of short selling by corporate insiders and that by others. Corporate insiders are prohibited from selling short their corporate security if the seller or his/her principal does not own the sold security; or even if he/she does own the security but does not deliver it within 20 days from the selling date, or does not deposit the security in any usual channel of transportation within 5 days after the sale is consummated.[296]

The second part of the short sale regulation even reaches every person who engages in a short-selling transaction.[297] However, such a transaction will only be deemed unlawful where the prices of the relevant securities are falling.[298] In other words, short sales only become illegal in a declining market; in an advancing market, they are permissible. The purposes of short sale regulation in the US were mentioned in an SEC report in 1963, including: (1) to permit short sale in an advancing market; (2) to eliminate the use of short sale in driving the exchange markets down; (3) to avoid short selling in accelerating a downward trend in stock price.[299]

The controversy over positive and negative aspects of short sale has continued. Recently, in the US, the SEC has sought public comments on the necessity of short sale regulation and the extent to which short sale should be regulated. By this open request for comment, the SEC aims to find out the most appropriate regulatory structure for short selling. One of the eight proposed concepts related to the regulation of short sale of securities is the elimination of Rule 10a-1.[300]

2. Should Extension of Credit and Lending Securities (Margin Trading) be Entirely Banned?

Article 72 makes it unlawful if securities firms and their associates engage in credit transactions and lending securities. This Article is too brief to give a clear meaning of "extension of credit" and "lending securities". It reads:

> *Organizations that engage in securities business and persons who practice in the area of securities trade must not extend credit and lending securities.*

This might be an equivalent to the provision concerning "Purchasing Securities on Margin" under the US *Securities and Exchange Act* of 1934. However, in the US, the

[296] See *Securities Exchange Act of 1934* s 16(c), 15 USC s 78p (2002); see also Rule 16(c).
[297] See *Securities Exchange Act of 1934* s 10(a), 15 USC s 78j (2002).
[298] See the US SEC rule: Rule 10a-1.
[299] See "Report of Special Study of Securities Markets of the Securities and Exchange Commission", H.R. Doc. No. 95, 88th Cong., 1st Sess. (1963), at Pt.2, 251.
[300] See *"Proposed Rules"* (SEC), above n. 290.

term "margin transactions" refers to securities purchased on credit.[301] In that sense, Article 72 has failed to define the prohibited activities, since it cannot make any connection between "extension of credit" and "lending securities". It simply bans specified persons from engaging in two such areas of business: (1) extending credit and (2) lending securities. As such, its meaning cannot be construed as the prohibition of extending credit for the purchase of securities, although that might have been the intention of the lawmakers.

In practice, in other countries, the purchase of securities on credit is not usually prohibited but is put under control. That is because margin trading, to some extent, has a good impact on market liquidity and promotes a healthy market. As observed by some economists:

> *margin trading must be defended not on the grounds that it efficiently and ingeniously assists the speculator, but rather that it encourages the extra trading which changes a thin and anemic market into a thick and healthy one.*[302]

However, there are a number of reasons why margin trading cannot be totally deregulated. According to the US SEC report, an entire freedom in the extension of credit for purchasing securities has been found detrimental to the exchange.[303] Loss and Seligman also give three reasons for control of margin trading under the American law. The first is to prevent a situation where the nation's credit resources, which would otherwise have been available at normal interest rates for more desirable uses of local commerce, industry, and agriculture, could be drained by much higher rates into loans for securities speculation in the stock market. The second is to protect the margin purchaser from a risk the purchaser might encounter by purchasing securities mainly on credit. And the third is to achieve a stable economy and to avert over fluctuation in the market.[304]

The US securities regulation thus does not ban margin trading but allows such a trading within certain thresholds.[305] A margin requirement of 50% of the market value of the purchased securities has been maintained for years. A purchaser can thus enter a margin transaction by borrowing up to 50% of the market price of the securities he/she is

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[301] See Thomas Lee Hazen, *The Law of Securities Regulation*, (1985), 285. Hereinafter, Thomas Lee Hazen.
[302] See J. Patrick Raines and Charles G. Leathers, *Economists and the Stock Market*, (2000), 112.
[303] See Dean Furbush, Annette Poulsen, "Symposium on the Regulation of Secondary Trading Markets: Program Trading, Volatility, Portfolio Insurance, and the Role of Specialists and Market Makers: Harmonizing Margins: the Regulation of Margin Levels in Stock Index Futures Markets", (1989) 74, *Cornell Law Review* 873, 876.
[304] See Loss and Seligman, above n. 289, 803.
[305] *Regulation T* of the Federal Reserve Board governs the extension of credit by securities market intermediaries like broker-dealers. *Regulation U* of the Federal Reserve Board governs the extension of credit by banks.

going to buy. In extending credit to a customer in a margin transaction, broker-dealers are required to disclose initially and periodically the credit terms in margin transaction.[306]

A similar provision to that of the US is adopted in Japan, where margin trading can only be effected by a securities company if its customer deposits a specified sum of money. Article 161-2, *Securities and Exchange Law* reads:

> *A securities company shall, in connection with such transaction as may be prescribed by an ordinance of the Cabinet Office including a margin transaction and others, receive from its customer in accordance with the provisions of an ordinance of the Cabinet Office the deposit of a sum of money no smaller than an amount arrived at by multiplying the market price of the security by such ratio as the Prime Minister may fix by taking into consideration the assurance of fairness of the sale or purchase of , or any other form of transaction in, a security.*

III. THE LACK OF LEGAL BASES FOR INVESTORS' RIGHTS OF ACTION AND FOR MEANINGFULLY DETERRENT SANCTIONS AGAINST VIOLATIONS

1. No Concrete Legal Bases for Rights of Action against Wrongful Conduct

To ensure that public investors are adequately protected, other jurisdictions often adopt a legal basis for three kinds of action: private action, class action and derivative action. Concrete provisions concerning these rights do not appear to be available in the Vietnamese securities regulation and enterprise laws.

A legal action against market participants like Securities Trading Centers and their staff, securities firms and their employees, issuing companies and their officers, and other persons who violate the securities regulation are not mentioned in *Decree 48/1998,* nor are they stipulated in the *Enterprise Act*. Article 79 *Decree 48/1998* merely provides for the settlement of disputes arising in the issuance and trading of securities and in other securities transactions. However, this provision is inserted in Chapter X, namely "Inspection, Supervision and Treatment of Violation", following the two Articles, 77 and 78, which provide for inspection and supervision by the SSC. This fact seems to imply that disputes mentioned in Article 79 are only those found by such inspection and supervision, and do not include disputes instituted by public investors. As such, it is unclear whether or not public investors have rights of action under the current securities regulations.

[306] See *Rule 10b-16* of the SEC: under this Rule, both initial and periodic written disclosures of the credit terms of margin loans are required.

Article 79.1 says that disputes over securities transactions are to be initially handled by the relevant parties on a negotiation and mediation basis. Stock Trading Centers, Stock Exchanges and the SSC can act as a third party in reconciliation of such disputes. Where parties fail at self-handling the dispute, they can bring the case to an economic arbitrator or a court of law for settlement or trial, respectively.

Sub-article 2 of Article 79 goes on to provide for the settlement of disputes involving a foreign party. If these disputes cannot be handled by the relevant parties on a negotiation basis, and cannot be settled in conformity with an international treaty to which Vietnam is party, then the disputes will be solved in conformity with the law of Vietnam.

Nowhere in the Article or in Chapter X are rights explicitly vested in investors to sue the securities law offenders on their own initiative, to protect themselves.

Decree 22/2000 merely provides for the rights of individuals to make accusation regarding administrative violations to the state competent authorities.[307] Accusation regarding other violations not of an administrative nature cannot be made by individuals since there is no concrete legal basis for doing so. Possibly, in order to institute legal action against a wrong doing where the violation is not of an administrative nature, investors have to rely on general statutory provisions found in the *Ordinance on Procedure for Settlement of Civil Disputes*[308] and the *Criminal Procedure Code*.[309]

Rights to take legal action are of importance. Such rights, if adequately adopted, can usefully cooperate with the market watchdog in preventing insider trading and other deceptive practices. It might be helpful to learn from the Japanese experience. For a long period of time, private rights of action were not legally recognized under the *Securities and Exchange Law* in Japan. The old Article 58 of the Law does not give a direct legal foundation for civil remedies. The remedies, however, can be found in Article 709, the

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[307] See Art. 19. 2.

[308] See Art. 1. This Article empowers citizens and legal entities with the rights to institute legal proceedings against wrong doers to protect their lawful interests.

On August 2, 2002, for the first time, a company was sued by workers for depriving them of several billions Vietnamese Dong by not paying social insurance fees and workers' salary. This legal action was taken by seven workers, on behalf of another 260, working at the First Branch, Thien Ho Production Ltd. Co. The case was brought into Thu Duc District Court (located in Ho Chi Minh City). For more information, see "Cty TNHH Thien Ho (TPHCM) chiem doat tien BHXH: Cong nhan khoi kien Cty ra toa!" [Thien Ho Ltd. Co.: Usurping Social Insurance Fees – Workers Sue at a Court of Law!], *Bao Lao dong [The Labour]*, Issue No. 205, Aug. 6, 2002.
http://www.laodong.com.vn/, visited Aug. 6, 2002.

This case although it has not yet been heard, shows that the language of Article 1, the *Ordinance on Procedure for Settlement of Civil Disputes*, is very broad. Perhaps, shareholders can similarly take a class action against the company where the class interests are injured. However, it is unclear whether a derivative suit can be brought into court under this Article 1.

[309] Article 84 of the Code vests in citizens the right to accuse a criminal offender. Article 87 imposes criminal prosecution obligations on a number of state competent authorities such as investigation organs and the People's Prosecutors' Office. Where the crimes occur within their own jurisdiction, Border Defending Army, Naval Force, and the Forestry Office can also institute prosecutions. Courts can also institute prosecution if during a trial they find a new crime or a new criminal offender.

Civil Code.[310] Unfortunately, the provision has never been used to prosecute insider trading in Japan.[311] More precisely, there was only one insider trading case, but it merely appeared in the press, not being reported in any official case reports.[312] A number of reasons for that have been found: (1) most Japanese did not think insider trading to be wrongful conduct,[313] (2) Japan is an inherently non-litigious society;[314] (3) Japan lacked provisions for class actions and effective discovery procedures; (4) Japan has extremely expensive litigation fees for taking a civil action.[315] Although legal action can be initiated under Article 709, the *Civil Code*, it is maintained that *"any tort action places the burden of proof on the plaintiff, and Japan's discovery procedures make proving a violation of insider trading laws extremely difficult"*.[316]

Possibly the absence of direct statutory provisions on private right of action and class action in the *Securities and Exchange Law*, as well as other aspects of social and legal culture, have resulted in the failure to detect insider trading in Japan. In the literature, an often-seen observation is that Japan is a heaven of insider trading.[317] While in the US, the number of actions against insider trading taken by the SEC alone amount to 300 per year, in Japan there have only been three cases brought to trial.[318] This fact, however, shows that the small number of cases brought to court in Japan cannot be attributed only to the dearth of concrete legal bases for rights of action in the securities regulations. It also indicates that the Japanese market watchdog does not seem to have made a real effort in detecting insider trading. This is probably the case, since in a number of circumstances, even when concrete legal bases for rights of action are available, there might still be a dearth of litigation since investors themselves cannot detect or do not know whether this or that transaction actually constitutes insider trading.

In the US, to answer the question whether Congress allows a private right of action under Section 10(b), one will have to look at the language of that Section, which does not seem to explicitly specify such a right. However, aside from statutes enacted by the legislature, the US case law is another important source under which a private right of action against violators of Section 10b can be found. In *Kardon v. National Gypsum Co.*,

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[310] See Louis Loss *et al* (eds.), above n. 261, 192.

[311] Ibid, 192 – 3; see also Ramzi Nasser above n. 261, 328; see also Curtis J. Milhaupt, "Managing the Market: the Ministry of Finance and Securities Regulation in Japan", (1994) 30 *Stanford Journal of International Law* 423, 454. Hereinafter, Curtis Milhaupt.

[312] See Louis Loss *et al* (eds.), above n. 261, 192.

[313] Ibid, 191- 192; see also Ramzi Nasser, above n. 261, 384.

[314] Cutis J. Milhaupt, above n. 311, 455; see also George F. Parker, "The Regulation of Insider Trading in Japan: Introducing a Private Right of Action", (1995) 73, *Washington University Law Quarterly* 1399, 1414. Hereinafter, George Parker.

[315] Ibid (George F. Parker), 1414 - 5; see also Larry Zoglin, "The Global Securities Market: Insider Trading in Japan: A Challenge to the Integration of the Japanese Equity Market into the Global Securities Market", (1987) *Columbia Business Law Review* 419, 422.

[316] Ibid (George F. Parker), 1422.

[317] See Ramzi Nasser, above n. 261, 382 - 383; see George F. Parker, above n. 314, 1403; and see also Shen-Shin Lu, "Are the 1988 Amendments to Japanese Securities Regulation Law Effective Deterrents to Insider Trading?", (1991) *Columbia Business Law Review* 179, 193.

[318] See George Parker, above n. 314, 1403.

the plaintiff shareholders sued the defendant shareholders for violating Section 10(b), the *Exchange Act* when purchasing shares from the plaintiffs without disclosing material information. The US District Court for the Eastern District of Pennsylvania held that the defendant shareholders entered deceptive transaction and that the plaintiff shareholders were entitled to a private remedy without proving whether or not the defendants profited from the transaction.[319]

2. Only Administrative Sanctions against Violations

Article 80, *Decree 48/1998* provides for the "Treatment of Violations". It merely gives the levels of sanction borne by violators. Depending on the nature of the violation and the extent to which the securities regulation is breached, disciplinary, administrative or criminal sanctions can be imposed on the violator. Although civil sanctions are not mentioned here, Article 80 goes on to say that where the violation has caused damages to other parties, compensation for damages will be applied. So it can be said that civil sanctions are also adopted in this Article.

For the time being, the statutory sources dealing with such violations are mainly found in Article 80, *Decree 48/1998.* There are no further rules expanding the language of Article 80 apart from *Decree 22/2000*. However *Decree 22/2000* merely deals with administrative violations. Other violations remain poorly regulated. Since securities law offenders in general, and securities crimes in particular, are relatively new in Vietnam; the current *Criminal Code* has no concrete article regulating these newly emerging crimes. In the absence of such provisions in the *Criminal Code*, the simple language of *Decree 48/1998* and the limited scope of *Decree 22/2000* cause general concern as to whether Vietnam has enough remedies to protect public investors. And that is not to mention whether or not the available remedies are well enforced.

As long as public confidence in securities markets is maintained, the markets can attract customers. Failure in doing so will result in ineffective markets, which goes against the goal of Vietnam in creating a market place where capital demands can be increasingly and widely met to support economic development in the country.

IV. THE FUTURE OF THE ANTI-FRAUD REGULATION

Looking at the anti-fraud regulation as a whole, one can easily recognize a number of deficiencies that need to be eliminated. First are the statutory gaps in the regulation and in its enforcement mechanism. Second is the failure of the regulation to employ supporting instruments to promote a thick and healthy market. Third are technical deficiencies in the regulation. To consolidate the regulation, enhance its validity, and promote a healthy market, the following steps should be taken:

[319] See Kardon v. National Gypsum Co., 69F Supp. 512, 514 - 515 (E. D. Pa.) (1946).

1. Strengthening the Anti-fraud Regulation and Enhancing the Enforcement Mechanism

a. Short-swing Trading Should be put under Control

The regulation of insider trading has no provision requiring company officers and large shareholders to report their sales or purchases of securities to the state authority. Such a provision is of significance in detecting short-swing trading and in confiscating short-swing profit for the company. *Decree 22/2000* does have a rather general provision on which the whole amounts derived from law-breaking activities and the relevant securities can be expropriated (*sung cong quy*).[320] This provision gives the impression that even if profits that have derived from insider trading transactions (for example, short-swing profits) were detected, the relevant company is not entitled to disgorge such profits. Rather the profits will be transferred into the state budget.

The future regulation of insider trading therefore needs concrete provisions to impose reporting duties on any person who, by the acquisition of shares, becomes a large shareholder, and on company insiders who engage in transactions to purchase and to sell shares. Such duties should be discharged at the time the acquisition occurs and at the end of the month the purchasing or selling transactions are effected. A concrete period of time, within which a purchase that can be matched against a sale at a higher price so that the transactions can be deemed as short-swing trading, also needs to be defined. In addition, a legal basis, on which a company can recover short-swing profit derived from the purchase and sale of shares effected within a short period of time, as specified by the law, needs to be created.

b. Stabilizing Activities Should be Legalized

The language of the anti-manipulative provisions - Article 73, *Decree 48/1998*, is rather general. As such, it seems to cover too broad an area, while lacking necessary details to deal with a number of specific issues. For example: in a number of circumstances, where stabilization of market price of a security during the issuance is required, there is a need for purchase or bid for such security by an underwriter or issuer. The current regulation gives no legal basis for such transactions to be effected.

There should be statutory provisions clearly distinguishing between bidding and purchasing activities done by securities distributors to induce others to purchase the distributing securities, on the one hand, and activities that are actually done to stabilize the securities price in order to avoid risk that might be incurred by the underwriters, on the other hand. Such provisions should explicitly require issuers to set out their proposal on price-stabilizing activities, if they plan to do so, in the application filed with the SSC

[320] Art. 15, sub-art. 2, paragraph d.

before the commencement of a public offering. When stabilizing operations are actually done during a distribution, underwriters should be subject to reporting requirements to the SSC.

In the absence of such provisions, on the one hand, there will be no legal basis for detecting manipulative transactions conducted under the form of stabilization. The problem becomes more serious once legal action is taken since it will take time and energy for courts to discern manipulative and stabilizing activities during the time of hearing. On the other hand, where it is necessary, actually stabilizing activities could not be performed. This obviously causes difficulties for securities distributors in preventing and retarding the falling trend of securities prices during a public offering.

Concerning the repurchase of outstanding shares by listed companies, at present, although there are up to three provisions - Article 65 of the *Enterprise Act*, Article 73.4 of *Decree 48/1998*, and Article 54.2 of *Decision 79/2000* mention the issue - uncertainties still remain. All of the Articles say rather little about the conditions for share buyback except for the requirements by which the buyback must be approved by the general shareholders' meeting and then by the Securities Trading Center, and the minimum, and maximum amounts that can be repurchased on a once-a-day basis. Possibly, there should be concrete provisions laying down more detailed limits companies have to meet in share buybacks. Such limits would include the maximum purchase price a listed company might offer and the time such transactions could be effected. These would reduce the possibilities for listed companies to manipulate their share prices.

c. Omissions of Material Information should be Prohibited

The mere prohibition of false statements under Article 71.1 is not enough to avoid public investors being misled. It is therefore, necessary to insert a provision that makes unlawful the omissions of material facts in a statement. In addition, the forms (oral or written or both) in which statements are to be made within the scope of the provision also need to be specified.

Another legal loophole also lies in the "misinformation provisions". Article 71.2 merely proscribes issuers, underwriters and relevant persons from advertising, offering and carrying out other activities having an advertising character before obtaining the issuing license from the SSC. As earlier discussed, the provision leaves room for so doing to many other persons such as securities trading centers, appraisal agencies, law firms and accounting firms. In practice, it is not beyond the abilities of such persons to accomplish the prohibited activities under Article 71.2. So this gap should be eliminated.

d. Concrete Rights of Action and Meaningfully Deterrent Sanctions for Violations should have Legal Bases in the Securities Regulation

Rights of action (including private right, class and derivative) and legal sanctions are of importance in ensuring compliance with the law. Both these issues have not been

properly dealt with by the current regulation, as earlier discussed.[321] More concrete provisions embodied in securities regulations conferring private rights of action on investors to institute proceedings against wrong-doing are thus necessary. Such provisions could be adopted in an individual article dealing with individual fraudulent activities or could be combined in the form of articles specifically dealing with such rights of action. Regardless of what forms they might take, such provisions should expressly set out the private right of public investors against violators of any nature (civil, criminal or so on) in a court of law. The *Enterprise Act* also needs concrete articles providing for class and derivative actions to ensure that company shareholders have adequate legal remedies to protect their own interests as well as those of the company.

These provisions will, in part, build up public confidence with the newly emerging securities market, as investors would know that they could take legal action against the wrong-doer on their own initiative when necessary.

To enable such rights of action, especially derivative action, to be realized, litigation fees in general, and court fee in particular, should also be reasonably provided for, since high fees might minimize the number of suits brought to court. This is because in contrast to a suit instituted by a private action or class action, in a derivative suit, the plaintiff will not receive any compensation, event if eventually successful.

Merely recognizing the rights of action for public investors is not enough to assure compliance with the law, in the absence of an adequate and proper system of statutory sanctions. As pointed out earlier in this Chapter,[322] at present, only administrative sanctions have been adopted, and on a rather detailed basis. Sanctions for violations having criminal and civil natures are still missing. Even with a full system of legal sanctions, if adequate levels of penalty are not adopted, the success of law reform would still be in doubt.

In the late 1980s, Japan had experienced a reform in securities law, by which the *Securities and Exchange Law* was adopted with more detailed standards. But for various reasons, concerns about the success of the Revised Law still remain. One such reason is "the relatively minor penalty threatened by the law".[323] It is said that both maximum fine and imprisonment sanctions applied to those "reaping enormous profits" (a maximum fine of 500,000 Yen and imprisonment of at most six months) provided in the revised Law at that time are not sufficient.[324]

In Vietnam, the maximum fine level under *Decree 22/2000* is merely 50 billion VND (around 3000 USD), which is not drastic enough. There is thus an urgent need for Vietnam to introduce adequate criminal sanctions, appropriate fines and proper compensations for damages caused by frauds in law and in practice.

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[321] See Section III of this chapter.
[322] See Section III, Sub-section 2 of this chapter.
[323] See Harald Baum, "Japanese Capital Markets: New Legislation", (1989) 22 *Law in Japan an Annual* 1, 24.
[324] Ibid. The author compares such levels of punishment in Japan with those adopted in the United State (a fine of 1 million USD and 10 year imprisonment) and in Switzerland (3 year imprisonment and up to 40,000 Swiss Francs or in some specified cases, an unlimited fine).

2. Providing the Market with more Useful Instruments

a. Short Sale should not be totally prohibited

The current securities regulation bans short sales entirely. As earlier discussed, short sales, whilst they can be employed in manipulative transactions, can also benefit the market by providing liquidity and pricing efficiency. A strict prohibition as has been adopted in Vietnam will deprive the young securities market of a useful instrument.

The lawmakers should pay more attention to this problem and possibly create a new short sale regulation under which: (1) only short sales effected by company insiders should be strictly proscribed; (2) short sale transactions entered into by other public investors should only be banned in a falling market to prevent free falls in stock prices.

b. Margin Trading should be allowed Within a Certain Threshold

The prohibition of purchasing securities on margin under Article 72, *Decree 48/1998* should be discussed more thoroughly, since margin trading, as earlier discussed, to some extent has a good impact on market liquidity and promotes a healthy market. For these reasons, an approach in which margin trading is not totally prohibited, but can be carried on within certain limits, has often been adopted elsewhere. Usually the law sets some thresholds on the amount of credit that can be obtained by investors who purchase securities using such loans, as earlier discussed.

In the history of the stock exchange in the US, margin requirements were first set by the exchanges and individual brokers. In 1913, the NYSE adopted a rule based on a theory of "proper and adequate" margin requirements. The theory generally says that if margins are not set properly and adequately, they might be harmful to the exchange. The theory used to be followed by exchange members in setting their own margin requirements.[325]

The stock market crash in 1929 pushed the US Congress to take a decisive step in granting to the Federal Reserve Board the power of regulating initial and maintenance margins.[326]

Perhaps this should be a lesson for Vietnam in revising the regulation of margin trading. The problem is to find an appropriate credit limit within which investors could purchase securities for speculation, rather than to ban margin trading entirely.

3. Eliminating Technical Deficiencies

a. Providing Definitions of a Number of Significant Terms

[325] Ibid. 877.

[326] Ibid. 877 - 878; see also *Securities Exchange Act of 1934* s 7(a), 15 USC s 78g (2002). Pursuant to this Section, the Federal Reserve Board has the right to "prescribe rules and regulations with respect to the amount of credit that may be initially extended and subsequently maintained on any security".

Precise definitions of the terms that refer to the prohibited activities such as "insider trading", "market manipulation", "misinformation", "short sale", and "credit transaction, lending securities" should be provided. This is essentially important to ensure the feasibility of the regulation. In the absence of such significant definitions, it is hard to know in practice which activities fall into the scope of the relevant provision.

b. Eliminating Inconsistencies in Different Legal Texts

Decree 48/1998 has failed to define activities that are deemed as unlawful such as tipping or recommending other persons to trade based on inside information. While tipping is not prohibited by *Decree 48/1998*, it is deemed illegal and subject to administrative sanctions under *Decree 22/2000*. It seems that the two Decrees do not agree with each other about this issue, although that might not have been the intention of the lawmakers. Of course the later rules often overrule the earlier rules, but this should be taken into account while revising *Decree 48/1998* to maximally eliminate undesirable discrepancies between these two documents.

Another discrepancy is found between Article 73.1, *Decree 48/1998* and Article 5.1.a, *Decree 22/2000*. These two Articles refer to the same manipulative activity but do not seem to be successful in the way they are expressed. Both have failed to describe the prohibited activity – wash trading – adequately as earlier discussed. For these reasons, both Articles should be reworded to assure their transparency and to clarify their intention as well as to eliminate the inconsistency between them.

CHAPTER IV
WHETHER SECURITIES PROFESSIONALS ARE ADEQUATELY REGULATED

In parallel with the information disclosure regime and anti-fraud provisions, the regulation of securities professionals is also critical to investor protection. That is because in many cases conflicts of interest between customers and broker-dealers are inevitable. In the absence of an adequate regulation of such conflicts, broker-dealers might take advantage of their superior knowledge in the area over their customers to make profits to the detriment of these customers.

Furthermore, a suitable regulation of market professionals can even contribute to market development. In the case of Vietnam, defining the proper extent to which banks can act as securities professionals or can enter securities business is of importance in creating competitive force in the market, which, in turn, will foster market development.

This chapter studies the current regulation of securities professionals in Vietnam and argues that the regulation is not adequate. It contains weaknesses which will threaten investors' protection and be hurdles on the way Vietnam promotes market development.

I. REGULATION OF CONFLICTS OF INTEREST AND THE SAFETY OF PUBLIC INVESTORS

1. Securities Firms in General

Decree 48/1998 refers to all securities professionals as securities firms. Securities firms can engage in one or more of the following business activities: (1) brokerage; (2) dealing; (3) portfolio management; (4) underwriting; and (5) securities investment advisory services.

Securities firms must be shareholding or limited liability companies having an operating license granted by the SSC.[327] This means that, like any company, securities firms must be established under the *Enterprises Act*[328] and doing business in conformity with that Act. To trade in securities, they must obtain a license from the SSC.

In order to avoid risks incurred by future securities firms and by the public at large, the lawmakers created various statutory conditions that firms have to meet before and after obtaining a business license from the SSC. Such conditions relate to future business

[327] See *Decree 48/1998*, Art. 29.

[328] This Act was passed in 1999; under the Act four forms of enterprise are recognized, namely limited liability company, shareholding company, partnership, and private enterprise.

proposals, the material and technical conditions of the future firm, minimum capital requirements,[329] and qualification of the staff.[330]

Depending on the kinds of business activities carried out, securities firms have to meet different levels of minimum capital requirement. Firms that provide brokerage, portfolio management and investment advisory services must meet a minimum capital of 3 billion Dong. Such a figure applied to dealers is 12 billion Dong, and to underwriters 22 billion Dong. Where a firm carries out more than one business activity, it has to meet the total minimum capital requirements for each such activity,[331] for example, 37 million Dong if each of the above activities are carried out.

Since securities firms operate in a very special field, where specialty is highly required and where fraud and risk are very likely to occur, they have to meet a number of statutory requirements that are not necessary to be met by other companies. This fact thus makes securities firms differ from most other business entities. The fundamental differences between securities firms and other companies are: (1) the staff in a securities firm consists of securities trading staff. Apart form the clerks, accountants and cashiers, other staff working in securities firms, including directors, must have a practicing license from the SSC;[332] (2) the statutory representative of a securities firm must be the firm's General Director (or Director), who is responsible for the day-to-day operation of the firm in the stock trading centers.[333] The firm representative must have a bachelor's degree in law or economics, and a practicing license granted by the SSC as for other staff of the firm; he/she must not be a member of the management board or a general director (or director) of a previously bankrupt company, nor can he/she be a securities trading staff member whose practicing license was previously revoked by the SSC; and he/she must have at least three year experience in financial, banking or insurance business.[334] It is

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[329] It should be noted that *Decree 48/1998* uses the term "legal capital" (von phap dinh) instead of "minimum capital requirement". Although *Decree 48/1998* does not construe this term, the meaning of "legal capital" can be found under the *Enterprise Act*.

Article 3.7, the *Enterprise Act* defines: *"Legal capital (von phap dinh) is the minimum capital enterprise incorporators have to meet, pursuant to the law, in order to set up an enterprise."* Thus the concept of "legal capital" in Vietnam denotes a minimum amount required by the law or a "minimum capital requirement". It is not similar to that in use elsewhere, where "legal capital" means "stated capital": see Bayless Manning and James J. Hanks, Jr. *"Legal Capital"*, (3rd ed 1990), 30 - 34.

[330] See *Decree 48/1998*, Art. 30.

[331] Ibid.

[332] See *Decision 04-1998/QD-UBCK3* dated 13 October 1998 (hereinafter, *Decision 04/1998*), issued by the State Securities Commission, promulgating the Organization and Operation of Securities Firms, Art. 12 as amended under *Decision 78/2000/QD-UBCK* (hereinafter *Decision 78/2000*) dated December 29, 2000 by the SSC, to amend and supplement the "Regulation of Organization and Operation of Securities Firms" promulgated under *Decision 04/1998*.

[333] See *Decision 04/1998*, Art. 18.

[334] Ibid., Art. 19. The terms "finance", "banking" and "insurance" in Vietnamese are "tai chinh", "ngan hang" and "bao hiem".

Under the *Enterprises Act*, the statutory representatives of enterprises other than private enterprises can either be the president of the management board (in shareholding companies), the president of the members' assembly (in limited liability companies) or the general director of these companies. The *Enterprises Act* does

interesting that Article 19. 5, *Decision 04/1998* does not include the term *"securities"*, and as a result it inadvertently excludes from the post of a representative of a securities firm, persons who have had three years, or even more, of experience in the securities business. Of course, at the time this Decision was issued in 1998, there was no one who had three-years experience in securities business since at that time no securities firms existed in Vietnam. However, this provision will soon be outdated, especially since the first Stock Trading Center has already been operating since July 2000 with the first six securities firms[335] getting licenses to do securities business. Moreover, the term *"finance"* itself covers all three areas *"banking"*, *"insurance"* and *"securities"*. Possibly the term *"finance"* alone is enough to cover all the three areas in one of which a securities firm representative is required to obtain experience.

Individuals holding a practicing license granted by the SSC are not permitted to work for or invest in two or more securities firms, or to occupy the position of director, company manager, or shareholder owning more than 5% of voting shares of an issuer.[336] By this provision, Vietnam has taken a relatively careful step in avoiding potential conflicts of interest. That is necessary because both company law and securities law in Vietnam are in their infancy.

The *Enterprise Act*, although it puts self-dealing under control, merely deals with transactions between company board members and the company itself.[337] In spelling out the duties of company managers, the Act generally says that company management boards, directors and other officers must not misuse their powers for their own interests or those of other persons.[338] Self-dealing, however, can basically be divided into four groups of transactions: (1) those entered into by a company and its directors or officers; (2) those entered into by a company and a business entity in which the directors or officers have a significant direct or indirect financial interest; (3) those entered into by a subsidiary and a parent company; and (4) those entered into by companies having common or interlocking directors.[339]

The *Enterprise Act* has thus not yet covered all necessary areas requiring regulation, nor can it provide adequate legal bases for governing transactions occurring between companies with a common director/officer. The situation will become worse when those companies have relationships involving a subsidiary securities company and a holding bank or the like. Such a relationship might well give rise to opportunities for bad dealing to occur. In the absence of a comprehensive regulation of conflicts of interest, the prohibition of interlocking directorates can thus be deemed wise and right.

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not specify any criteria to be met by the statutory representative of an enterprise as *Decision No. 04/1998* does with respect to such a post in a securities firm.

[335] See "Profits hard to come by for Vietnam Stock Brokers", above n. 194.

[336] See *Decision 04/1998*, Art. 17.1 & 17.2.

[337] See Art. 87.

[338] See Art. 86.2.

[339] See Robert Charles Clark, *Corporate Law*, (1986) 159.

Such prohibition can be found in both Japanese and American laws. In Japan, common directors and auditors between a securities firm and its parent bank or its subsidiary bank are forbidden.[340] Even a director who performs an executive duty in a securities company must not perform the same duty in any bank, trust company or any other financial institution.[341] The US had also prohibited interlocking directorates between securities firms and banks.[342] Recently, such prohibition was eliminated under the *Financial Services Modernization Act*.[343] However, it can be argued that the elimination of interlocking directorates in the US is justifiable because of the extensive US regulation of conflicts of interest. Most of the state corporation statutes in the US have special provisions regulating conflict of interest transactions.[344] Conflict of interest provisions can also be found in the *Revised Model Business Corporation Act*.[345] Or one could even argue that whether or not such elimination is appropriate remains to be seen.

2. Brokerage and Dealing Activities can be combined in one Securities Firm in the Absence of Necessary Regulation of Conflicts of Interest

The statutory permission under which one firm can act as both a broker and a dealer is not something new. However, this combination of business activities often results in serious conflicts of interest between securities firms and their customers if there is no statutory measure to avoid them. *Decree 48/1998*, *Decision 04/1998* and even *Decision 78/2000*, all have no definition of either broker or dealer. Article 2, *Decree 48/1998* merely defines brokerage and dealing. It reads:

> *Securities brokerage is an intermediary business of buying or selling securities on behalf of customers for a commission.*[346]
> *Dealing is activities of securities firm in buying and selling securities for the firm itself.*[347]

[340] See *Securities and Exchange Law of 1948* (2001 Japan), Arts. 32 & 32.2.
[341] Ibid., Art. 32.3.
[342] See *Banking Act of 1933* s 32. (Richard W. Jennings, *Federal Securities Laws: Selected Statutes, Rules and Forms*, 1999 ed).
[343] Section 101 b.
[344] See Franklin A. Gevurtz, *Corporation Law*, (2000) 324.
[345] Since 1984, conflict of interest transactions have also been covered by Section 8.31, the 1984 *Revised Model Business Corporation Act*. The 1988 revision creates four provisions: from Section 8.60 to Section 8.63. Subchapter F, Section 8.60 (1) (ii), for example, says that a conflict of interest exists when a transaction is entered into by two corporations sharing a director and if "*the transaction is brought (or is of such character and significance to the corporation that it would in the normal course be brought) before the board of directors of the corporation for action*".
[346] See Article 2.6.
[347] See Article 2.7.

In practice, where a securities firm acts as a broker, it engages in the business of effecting transactions in securities for the account of others; where it acts as a dealer, it engages in the business of buying or selling securities for its own account.

Jonathan R. Macey and Maureen O'Hara make a rather clear distinction between brokers and dealers by defining the economic functions each of them performs. Dealers in acting as market-makers provide a liquidity function; in purchasing and selling securities, they carry out an arbitrage function. Brokers while acting as agents for customers or as distributors of newly issued securities perform a distribution function, while simply implementing the sale and purchase orders of customers is an executive function.[348]

When these functions are performed by one securities firm, conflicts of interest are very likely to occur, since *"what is the best for the broker-dealer is not always best for the customer"*.[349] Cheryl Goss Weiss, while considering the liability of broker-dealers for breach of fiduciary duty to their customers also maintains:

> *Broker-dealers face conflicts in many areas: between their own and their customers' interests; between the conflicting interests of different customers; and between their customers' interests and the public interest... A conflict of interests exists when a fiduciary is faced with a choice between his beneficiary's interests and any other interests.*[350]

To prevent such conflicts, some measures which have often been employed include: prohibition of broker-dealers from trading ahead of a customer's order, withholding and maintaining accounts for employees of other broker-dealers without notifying such broker-dealers. Aside from those, disclosure requirements with respect to broker-dealers can to some extent mitigate such conflicts. However, such requirements are usually very constrained and even if all of these measures are in use, this cannot avoid the fact that customers often refrain from dealing with firms that act as brokers and dealers at the same time.[351]

The securities regulations of Vietnam while allowing one securities firm to carry out more than one securities business activity, also provides for a number of operational principles securities firms have to follow, as well as statutory limitations imposed on those firms.

Securities firms have to follow seven statutory principles while doing business.[352] These principles are made up of ten sub-articles. The last three sub-articles were

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[348] See Jonathan R. Macey and Maureen O'Hara, "Regulating Exchanges and Alternative Trading Systems: A Law and Economics Perspective", (1999) 28 *The Journal of Legal Studies* 17, 44. Hereinafter, Macey and O'Hara.

[349] See David L Ratner (3rd Ed. 1986), above n. 256, 748.

[350] See Cheryl Goss Weiss, "A Review of the Historic Foundations of Broker-dealer Liability for Breach of Fiduciary Duty", (1997) 23 *The Journal of Corporation Law* 65, 69 - 71.

[351] See Macey and O'Hara, above n. 348, 45-46.

[352] See *Decision 04/1998,* Art. 20: these principles were drawn from this article.

introduced by *Decision 78/2000*. The ten sub-articles can be grouped into three categories:

Principle of acting for customers' interests: this requires securities firms to act with fidelity and fairness and for the customers' interests.[353] Firms have to trade skillfully and responsibly and they must not trade ahead of customers' orders.[354]

Since the passage of *Decision 78/2000*, this principle has been widened by the insertion of three other sub-articles: 8, 9, and 10 into Article 20, *Decision 04/1998*. Under the amendments, (1) securities firms have to fully, timelily and honestly provide information to customers; (2) business of a firm's owner and that of the firm itself must be separated in order to avoid conflicts of interest between the firm, its staff and its relevant organizations and its customers, and conflicts amongst its customers; (3) the three business areas of brokerage, dealing and investment-portfolio-management must be separated.

Principle of anti-manipulation: securities firms must not have any activity that misleads customers or the public on the securities' price, value and nature, nor can they act to their customers' detriment.[355]

Principle of good financial, internal control and manning capacity: securities firms have to ensure the adequacy of financial resources while trading with their customers; must have good internal control to ensure that all activities conducted by them and their staff are in conformity with the law; must have enough qualified staff that have been adequately trained and recruited.[356]

Apart from those principles, securities firms are subject to certain statutory limitations.[357] For example, a securities firm must not own more than 20% or 15% outstanding shares of a listed or a non-listed company, respectively; its capital subscription in a limited liability company must not exceed 15% subscribed capital of that company. Some other limitations include a limit on the amount a firm can underwrite, a limit on the percentages of liquid asset a firm has to maintain, and a limit on the charter capital a firm can use to purchase facilities and immovable assets. Apart from these, a securities firm must not purchase shares issued by its parent company.[358]

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[353] Ibid., Art. 20.1.
[354] Ibid., Art. 20.3.
[355] Ibid., Art. 20.7.
[356] Ibid, Art. 20.4 - 2-.6.
[357] Ibid, Arts: 22, 23. Article 23 was revised under *Decision 78/2000*.
[358] Articles 22 and 23 (as amended under *Decision 78/2000*) do not specify sanctions applied to securities firms that breach the above-mentioned limitations. Article 32, *Decision 04/1998* generally says securities firms and their securities trading staffs that (1) violate provisions prescribed in the securities business license and practicing license, respectively, or (2) breach statutory provisions provided in *Decree 48/1998*, shall have sanctions imposed on them in conformity with the current law.

Article 2, *Decree 22/2000* provides for sanctions and other statutory measures applying to administrative violations in the field of securities and securities market. The Article lay down two principal sanctions, namely warning and monetary sanction. Other supplementary sanctions are also provided for, such as: revoking business license or practicing license; confiscating the amounts derived from unlawful activities; and compensation for damages.

Firm - customer relationships are also subject to statutory regulation under the language of Article 21, *Decision 04/1998*, which was replaced by a new Article 21 under *Decision 78/2000*. The new article has eight sub-articles compared with four sub-articles under the old one. Under the new article, a firm and its customer must enter into a written contract when the firm, with the agreement of the customer, is about to open and manage a customer's account, or to provide investment-portfolio-management service to the customer; a firm's security assets and those of its customer must be separately managed; firms must choose a bank for settlement and transfer all customers' fund into a bank account and must use customers' funds according to the agreement or direction of customers; firms must not disclose information concerning a customer's account without customer's consents; firms must immediately inform customers where there is any unusual change in the price of securities in their investment portfolios.[359]

While providing statutory principles that securities firms have to follow and putting some restrictions on the activities conducted by these firms, neither *Decree 48/1998* nor *Decision 04/1998* has a concrete article regulating the conflicts of interest between securities firms and their customers. This deficiency has been partly eliminated by the passage of *Decision 78/2000*, which creates the three new sub-articles earlier mentioned, especially Sub-article 8 of Article 20, stipulating information disclosure duties by firms to their customers. However, this *Decision* does not concretely specify what kinds of information securities firms must provide to their customers. In addition, the new Article 21, although it has been broadened compared with the old one, merely requires of securities firms timely notification of customers about changes in their investment portfolios. Such provisions cannot ensure that conflicts of interest between the firms and their customers will be avoided.

Article 27, *Decision 04/1998* provides for information disclosure requirements that securities firms have to follow. It reads:

> *Securities firms are responsible for reporting honestly, precisely and fully to the State Securities Commission all information concerning their trading activities.*
> *Public information disclosure by securities firms must be done in conformity with the regulation of public information disclosure issued by the State Securities Commission.*
> *Aside from reporting to the State Securities Commission, securities firms that are members of a stock trading center or a stock exchange must report to the center or the exchange as provided for in Articles 28 and 29 of this Regulation.*

Article 38, *Decree 48/1998* provides for duties and rights of securities firms. Sub-article 2, although it requires securities firms to collect full information about financial situations and investment goals of customers, does not explicitly say that firms have to

[359] The same can be said about sanctions applying to violators of these statutory provisions. See Ibid.

give investment advice based on such findings. *Decision 79/2000,* while preserving one article - Article 5 - stipulating concrete duties of member firms of a securities trading center, also does not mention duties of securities firms to their customers. It has no requirements for securities firms concerning their responsibilities in ascertaining their customers' financial situation and ability to assume risk before determining which securities should be recommended to them. Securities firms are not required to investigate the nature and risks of securities that will be recommended to customers, nor are they required to have an adequate basis for trusting that the securities they recommend are suited to the customer's needs.

Article 5 mainly concentrates on duties of securities firms in relation to stock trading centers. Pursuant to such provision, firms have to be subject to the center's rules, control, and supervision; they have to pay a membership fee and other subscription to form the so-called "settlement support fund"; they have to periodically and timelily report to the trading center the following issues:

a. *Operating and financial situations in conformity with the Regulation of the Organization and Operation of Securities Firms;*
b. *Monthly securities transactions in accordance with Form 02-TV attached to the said Regulation within the first five days of the following month;*
c. *The merger, consolidation, division, separation and establishment of branches; member firms wholly or partly stopping operation; restructuring of the firms (where any of these occur);*
d. *Other information concerning the operation of member firms as requested by the securities trading center;*
e. *When activities that have violated securities law are detected.*[360]

Apart from these, member firms have to report to the securities trading center within 24 hours from the time the following events occur:

a. *Increasing or decreasing registered capital;*
b. *Going into bankruptcy or dissolution;*
c. *Applying for bankruptcy announcement;*
d. *Being a plaintiff or defendant in a court case;*
e. *Member's bank account being suspended or blockaded, or when decisions to suspend or blockade its bank account are lifted.*
f. *Moving the head office, opening, closing or moving the main branch office;*

[360] See Sub-article 5.

g. Director or other trading staff of the member firm being under the investigation of a governmental authority or having been on trial by a court.[361]

Although these Articles impose rather detailed disclosure requirements on securities firms, there is still be something missing here. Securities firms are not explicitly required to disclose their conflicts of interest to customers when they recommend securities of their own, or if they have some interest in recommended securities. This might give an impression that, to some extent, they do not differ from coffee house stock exchanges very much, which in turn might trigger fears among the public about investment safety. Furthermore, if a securities firm can act both as a dealer and a broker, it might put its own interests over the customers' interests. Even though a new regulation on conflicts of interest between customers and securities firms has been introduced, as previously discussed, nevertheless it does not seem strong enough to eliminate conflicts.

Moreover, as securities professionals, securities firms obviously have superior knowledge concerning securities transactions compared with that of their customers. It is not beyond their ability to take unfair advantage of this superior knowledge in dealing with their customers. Thus, it is necessary to set forth some statutory standards of conduct for their business activities.

It might be useful to examine the ways in which conflicts of interest have been dealt with in some other countries. In the US, the *Securities and Exchange Act of 1934*, while providing for the registration and supervision of broker-dealers, keeps silent on the duty of broker-dealers to their customers. However, regulation of conflicts of interest can be found in case law[362] and in the rules of conduct issued by the Securities and Exchange Commission (the SEC),[363] the National Securities Dealers Association and the stock exchanges themselves.[364] Together, these set out a series of duties to be carried out by broker-dealers: (1) broker-dealers must have a good understanding of their customers' financial situation, ability to assume risk and investment holdings; must well understand the securities they recommend to their customers; (2) they must assure that their recommendations are suitable for their customers' financial situation and needs; (3) they should fulfill their customers' investment objectives, and customers' orders must be executed correctly and promptly; (4) they may not engage in excessive trading of securities in the account in order to generate commissions; (5) they must not overcharge customers in providing service nor may they effect securities transactions at an unreasonable price.

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[361] See Sub-article 6.

[362] See *Charles Hughes & Co. v. SEC*, 139 F2d 434 (2nd Cir. 1943); *Hanly v. SEC*, 415 F2d 589 (2nd Cir. 1969); *SEC v. Capital Gains*, 375 US 180 (1963); *Chasins v. Smith, Barney & Co.*, 438 F2d 1167 (2nd Cir. 1970), for example.

[363] See the *Disclosure Order Execution and Routing Practices*, Exchange Act Release No. 43,590 (Nov. 13, 2000).

[364] See NASD Manual 2152; NASD Rules of Fair Practice; NYSE Rule 405, for example.

In Japan, the *Securities and Exchange Law,* Article 38 imposes on brokers a duty to specify the form of trading in advance. It reads:

> *A securities company shall, in case where it has accepted from a customer an order for the sale or purchase of a security or for trade in over-the-counter derivatives contract on a security, give an explicit indication to the customer in advance whether it will consummate such sale or purchase or such trade by acting as a principal, or as a finder, broker, or agent.*

Article 42 even further prevents securities companies from making a decisive judgment and from soliciting customers to trade in over-the-counter derivatives contracts. The Article details the prohibited activities in nine sub-articles and clearly distinguishes them.

In addition, Article 43 proscribes securities companies from doing business in a way that would make the companies adopt a condition that could undermine the protection of investors. Relevant statements include:

> *(1) The state which undermines or is liable to undermine the protection of investors by making solicitation of customers deemed inappropriate in the light of their knowledge, experience or assets, for the purchase or the sale of a security or placement, ect. of an order therefore, placement of an order for trade in futures contract on a securities index, etc., trade in options contract on a security, or trade in foreign market futures contract on a security, or for trade in over-the-counter derivatives contract on a security, or placement, etc. of an order therefore, or*
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> *(2) Such state as may be prescribed by an ordinance of the Cabinet Office as that which is liable to impair the public interest or undermine the protection of investors, otherwise than the state set forth in the preceding item.*

These should be a good lesson for Vietnam in revising the current regulation of securities firms business.

II. REGULATION OF THE INVOLVEMENT OF BANKS IN THE SECURITIES MARKET

Before judging the Vietnamese regulation of banks' involvement in securities markets, it might be useful to examine how the issue has been dealt with elsewhere.

1. The Involvement of Banks in Securities Markets: Overseas Experience – Lessons for Vietnam

a. The US Experience

Prior to 1900, although in the US there had been no statutory provisions prohibiting commercial banks from carrying out securities business, such a prohibition was made by case law.[365] With the adoption of the *McFadden Act* in 1927, the US has adopted a universal banking system in which commercial banks can carry out securities activities.[366]

Owing to the stock market crash in 1929, a large-scale reform of the financial system was initiated. Causes of the market crash of 1929 were attributed to the speculative abuses in securities that infected commercial banking; unsound loans given by banks to their affiliates; and the combination of investment and commercial banking.[367] As a result, commercial and investment banking has been separated. A strict segregation between banking and securities business has been entrenched in the *Banking Act of 1933* (the *Glass-Steagall Act*).

Such a segregation includes: (1) the proscription of banks from acting as underwriters of any issue of securities or stock, from dealing in securities or stock;[368] (2) prohibition of a member bank from being affiliated with an organization that is principally engaged in underwriting securities and in certain other securities activities;[369] prohibition of securities firms from doing banking business such as receiving demand deposits;[370] prohibition interlocking officers, director or employee between securities firms and member banks.[371]

In practice, before the market crash, banks could carry out various business activities. Many banks, especially national banks, invested heavily in speculative securities; they entered the business of investment banking by buying original issues for public resale. Banks lent their affiliates money to shore up securities' prices or to secure the financial position of the affiliates. Banks even advised their customers to purchase securities which the bank needed to sell for the pecuniary sake of the bank itself.[372] These facts gave rise to potential risk of loss to depositors and were subject to failures that in turn took away public confidence in the banking system. Furthermore, when banks

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[365] See Jennifer Manvell Jeannot, "An International Perspective on Domestic Banking Reform: Could the European Union's Second Banking Directive Revolutionize the Way the United States Regulates its Own Financial Services Industry?", (1999) 14 *American University International Law Review* 1715, 1723.
[366] Ibid, 1724.
[367] See George J. Benston, "The Separation of Commercial and Investment Banking", (1990), 11 - 14. Hereinafter, George J. Benston.
[368] See *Banking Act of 1933* s 16, (Richard W. Jennings et al, *Federal Securities Law: Selected Rules and Forms*, 1999 ed).
[369] See Ibid, s 20.
[370] See Ibid, s 21.
[371] See Ibid, s 32.
[372] See George J Benston, above, n. 367, 11.

provide investment banking services and mutual funds, they face conflicts of interest between themselves and their customers, as well as other abuses.[373]

In addition, the 1933 Act has taken account of the fact that commercial banks could enter the business of investment banking was deemed as a cause of unfair competition. Commercial banks have market power since they can access cheap deposit funds. Thus they have an unfair competitive advantage over non-bank competitors; if they were permitted to provide investment banking services, or own corporate stock, they would be dominant and could take over securities brokers and underwriters.[374]

However, a number of studies conducted before and after the enactment of the *Glass-Steagall Act*[375] have shown that the above-mentioned problems were not the cause of the financial crisis in 1929. The failure of the Bank of United States[376] has been examined thoroughly and no evidence shows that failure of the bank or its use of affiliates had any connection to securities operations. Rather it was due to the bank's heavily lending money to affiliates; because it used acquisitions as a measure for rapid expansion, which was money-consuming and beyond its ability; and to avoid criticism by bank examiners and depositors, it removed bad loans from the bank's books to affiliates.[377] Also, among more than 200 banks engaged in securities operations, only 15 banks failed. Their securities trading amounts, however, accounted for a very small percentage of their total assets. The actual cause for the failure was found to be the bad banking situation.[378] Neither securities activities nor securities investment (regardless of whether or not purchased from bank securities affiliates) was a cause of bank failure. Rather, the causative factors include: demographic changes, over-banking, fraud and mismanagement, and poor farming conditions.[379]

Jordi Cannals seems to have a clear observation concerning the cause of the market crash of 1929:

> *It cannot be concluded from the results we have just presented that the cause of the 1930s banking crisis in the United States was the stock market activities carried out by some banks. Some results even seem to indicate that the losses could have been higher if the banks had not been able to count on the gains from the operations in financial assets.*[380]

All the findings thus tend to argue against the belief that banks' securities activities or investment caused the collapse of the financial system. In practice, the firewall

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[373] Ibid, 13.
[374] Ibid, 13 - 14.
[375] Ibid, 16 - 19.
[376] This bank is a commercial bank. In the US, the Federal Reserve System plays the role of a central bank.
[377] See George J Benston, above, n. 367, 30 - 31.
[378] Ibid, 32.
[379] Ibid, 38.
[380] Jordi Canals, "Universal Banking - International Comparisons and Theoretical Perspectives", (1997), 77.

separating commercial and investment banking in the US has been eroded. The involvement of banks in securities markets has been broadened over the time.[381] The separation between banking and securities businesses has been of little practical significance. As pointed out by Poser:

> *Today, American commercial banks, like those of the United Kingdom and other countries, conduct a wide variety of securities activities, while investment banks and securities companies are major providers of banking services.*[382]

The *Banking Act* of 1933 had thus been a major target of banking reform since its enactment, but it remained unchanged for a long time. Recently, the adoption of the *Financial Services Modernization Act of 1999* (the *Gramm-Leach-Billey Act*) has made considerable alterations to the *Banking Act of 1933, the Securities Exchange Act of 1934, the Investment Adviser Act,* and *Investment Companies Act.*

The 1999 Act makes significant alterations to the *Banking Act of 1933.*[383] It eliminates the prohibition of a member bank from being affiliated with an organization that is "principally engaged" in underwriting services, under Section 20. Accordingly, (1) Bank Holding Companies can now acquire or set up subsidiary securities firms that can engage in the flotation, underwriting, public sale, or distribution of securities; (2) securities firms can acquire banks or do banking business through a Financial Holding Company. It repeals the prohibition of interlocking directorates between securities firms and banks under Section 32.

However, the Act does not alter sections 16 and 21 of the *Banking Act* providing the framework for permissible securities underwriting activities. Consequently, Banks are still proscribed from engaging in most securities underwriting activities, and from acting as an agent or dealing in certain government securities; and banks may not purchase securities for their own account. Securities firms are still forbidden from banking business such as taking deposits and providing loans.

Securities firms and banks can carry out such activities through the holding company arrangements envisioned by the Act or through a securities subsidiary of a national bank.[384]

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381 See "United States: A Special Report Prepared by Warren F Cooke and Lynn Stofan Kaplan of Milbank, Tweed, Hadley & McCloy, Ney Work", International Financial Law Review Special Supplement 207, (Sep. 1991), 211 – 212; see also Jolina C. Cuaresma, "Business Law: The Gramm-Leach-Bliley Act" (2002) 17, *Berkeley Technology Law Journal* 497, 499.

382 See N. S. Poser, *International Securities Regulation: London's "Big Bang" and the European Securities Markets*, (1991), 185. Hereinafter, N. S. Poser.

383 The *Financial Services Modernization Act of 1999*, section 101 (a), (b) repealed respectively sections 20 and 32 of the *Banking Act of 1933*. The *Financial services Modernization Act of 1999:* available at http://www.senate.gov/~banking/conf/confrpt.htm, latest visit: Dec. 18, 2002.

384 Ibid, s 121.

The Act also alters the *Securities Exchange Act of 1934* by which banks would not be deemed as brokers or dealers for some specified "bank activities". Banks are now permitted to conduct certain limited brokerage and dealer activities without registration as a broker-dealer under the *Securities Exchange Act* of 1934.[385]

The Act makes some revisions to the *Investment Advisers and Investment Company Act*.[386] Previously, banks were excluded from the "investment adviser" definition. The new "investment adviser" definition now includes any bank or bank holding company that provides investment advice or serves as an investment adviser.

To date, the legal environment in the US allows commercial banks to enter into the business of securities companies through their subsidiaries. However, in so doing, certain conditions must be met by both the banks and their subsidiaries, as stipulated in Section 121, the *Financial Services Modernization Act*. As for banks, only national banks that are not affiliated with bank holding companies and have total consolidated assets of 1 billion USD or less, are eligible for conducting financial activities as principal through operating subsidiaries. Apart from being well capitalized, such banks must be well managed.[387] If satisfying these criteria, the national bank must then go through another step. It has to get the approval of the Office of the Comptroller of Currency before it can actually conduct financial activities through its subsidiary. The firewalls to maintain safety and soundness will be put between a national bank and its financial subsidiary only when the latter engages, as a principal, in activities, which the former can only conduct through a financial subsidiary. In such a case, the subsidiary can engage in financial activities subject to restrictions imposed on affiliate transactions. When acting as an agent, the subsidiary will not be subject to such restrictions.[388] In addition, if the activity is one in

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[385] Ibid, ss: 201 - 202.

[386] Ibid, ss: 211 - 220.

[387] The term "well managed" is construed in Section 121(a)(2). It reads:

"(6) Well managed. --The term 'well managed' means—

"(A) in the case of a depository institution that has been examined, unless otherwise determined in writing by the appropriate Federal banking agency—

(i) the achievement of a composite rating of 1 or 2 under the Uniform Financial Institutions Rating System (or an equivalent rating under an equivalent rating system) in connection with the most recent examination or subsequent review of the depository institution; and

(ii) at least a rating of 2 for management, if such rating is given; or

"(B) in the case of any depository institution that has not been examined, the existence and use of managerial resources that the appropriate Federal banking agency determines are satisfactory."

[388] Section 121(a)(2)(B) explicitly prohibits banks from engaging in four types of financial activities through bank subsidiaries: insurance or annuity underwriting, insurance company portfolio investments, real estate investment and development, and merchant banking. (Merchant banking activities are subject to section 122.) These types of financial activities may only be undertaken by subsidiaries of financial holding companies [s 103(a)].

A national bank's financial subsidiary therefore may engage in a wide range of activities previously barred to a national bank or its operating subsidiaries**,** such as underwriting, or dealing in securities (including market-making); selling insurance [ss 121, 151 & 302].

However, in order to protect the deposit insurance system from the increased risk it might incur by the expanded activities permitted to financial subsidiaries, a financial subsidiary and its parent national bank are subject to certain requirements. Those requirements include: the amount the bank has invested in its subsidiary

which the national bank could not engage directly, the subsidiary is only allowed to engage in the activity as an agent, and not as a principal.[389]

b. The European Experience

The European countries do not seem to have such a strict segregation between banking and securities businesses, compared with that in the US, even before the issuance of the *Second Banking Directive*.[390] Except for Belgium, where banks are strictly limited in engaging in securities activities, and the UK, France and Greece, where commercial banking and securities activities are separated by Chinese walls, other countries such as Germany, Italy, Switzerland and the Netherlands employ a universal banking system.[391] In the universal banking system, there is no firewall between banking and securities businesses or commercial and investment banking services. As such, commercial banks are eligible to engage in both kinds of business.

Since *the Second Banking Directive* came into force in 1989, a universal banking model has been widely adopted throughout European countries. Pursuant to this Directive, commercial and investment banking functions can be carried out by the same corporate entity, and the involvement of commercial banks in securities business is permitted.[392] The *Second Banking Directive* reflects the EU position in promoting the banking sector as well as in fostering EU financial markets. Under this position, it is intended that the participation of banks in the securities industry will diversify market participants, will provide liquidity to commercial banks, and will help banks to maintain overall earnings where profits from conventional banking business fall. And the EU sees a flexible universal banking system as powerful means that enable EU financial markets to compete with other markets around the world.[393]

Perhaps it is necessary now to see how such a system works in practice. The case of Germany might be useful to examine since it is a country that is going ahead in

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is to be deducted from its capital [s121(c)(1)(A)]; the financial subsidiary's assets and liabilities may not be consolidated with the national bank's assets and liabilities [s121(c)(1)(B)]; the assets of all of the bank's financial subsidiaries, on a combined basis, may not exceed $ 50 billion or 45% of the bank's total assets, whichever is less [s121(a)(2)(D)]; and a financial subsidiary is treated as a holding company affiliate rather than a bank subsidiary for purposes of the anti-tying provisions of the *Bank Holding Company Act*. [s 121(c)].

[389] See Section 122.

[390] See Gustavo Visentini, "Compatibility and Competition between European and American Corporate Governance: Which Model of Capitalism?" (1998) 23 *Brooklyn Journal of International Law* 833, 839. Hereinafter, Gustavo Visentini.

[391] See Guo Li, "The Collapse of the Glass-Steagall Wall and Its Potential Impacts on China's Banking Law", *Legal Forum Featured Article.* http://www.lawinfochina.com/legalForm/FeaturedAtrticle/displayContent.asp?ID=28, visited May 5, 2002. Hereinafter, Guo Li.

[392] See the Annex List of Activities subject to Mutual Recognition (this identifies the securities activities that a credit institution may carry out. Such activities include: trading for its own account or for the account of customers in long and short term securities; issuing of shares and related activities; managing of a portfolio and some investment banking activities, including those concerning mergers and acquisitions).

[393] See Guo Li, above n. 391.

employing a universal banking system in Europe and also in the world. Although Germany has permitted banks and securities companies to enter into the business of each other, it seems that both the German banking system and the German securities markets have functioned well. It is reported that the German financial market has been one of major markets in Europe for years; that the German banking system is very extensive and effective; that in terms of the size, the Frankfurt Stock Exchange ranks fourth in the world, after New York, Tokyo and London; and that the German financial center is one of the most intensely competitive European centers.[394]

c. The Japan Experience

A similar tendency to that of the US can be seen in Japan. Prior to the Second World War, Japan adopted a universal banking system in which banks could engage in any kind of business, including securities underwriting services.[395] After the Second World War, following the US model, a strict segregation between banking and securities business was introduced in Japan, i.e., a strict prohibition against securities firms engaging in banking business and banks engaging in securities business.[396]

Article 65 of the *Securities and Exchange Law* gives a legal basis for such segregation. This Article prohibits banks, trust companies or other such financial institutions from engaging in any securities business except for the purchase and sale of securities on a written order from a customer and for the account of the customer. The prohibitions are not applied to certain specified transactions in which the traded commodities are, for example, governmental, municipal, corporate and other bonds.

There have been opposite viewpoints concerning the need to eliminate such segregation.[397] However, the firewall between banking and securities business has been lifted during the 1980s and 1990s.[398] A reform of financial law initiated in 1993 has created a significant legal basis on which banks and securities firms can enter the business of each other through their subsidiaries. Securities firms could establish banking and trust bank subsidiaries while banks could set up securities subsidiaries, although the scope and size of such business was limited. Finally, the limitation on the scope and size of such business has been eliminated since the second half of 1999.[399]

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[394] See "Germany: A Special Report Prepared by Ulrich Koch of Single Loose Schmidt-Diemitz & Partners, Stuttgart and Frankfurt Am Main" (Sep. 1991) *International Financial Law Review Special Supplement* 87, 87.
[395] See Hiroshi Oda, above n. 262, 268.
[396] Ibid., 271; see also George J. Benston, above n. 367, 2.
[397] See Yusuke Kawamura, "The Present Attitude toward the System for Separating Banks and Securities Companies", *Japan's Financial Markets*, 1 -8.
[398] See Hiroshi Oda, above n. 262, 272 - 273; see also *Securities Market in Japan*, (1998), (released by Japan Securities Research Institute), 195 – 7 (hereinafter, Japan Securities Research Institute).
[399] Ibid (Hiroshi Oda).

Some Remarks

Although the debate concerning the segregation of banking and securities businesses has been continuing in the US and Japan, both countries have experienced a general statutory tendency toward lifting the fire-wall between these two businesses. This fact, together with comprehensive data found in a number of studies conducted in the US before and after the passage of the *Glass-Steagall Act,*[400] has proved that the past restriction was more or less a result of an over-reaction of the lawmakers to the market crash in 1929. In the US, the SEC has recently been aware of the negative aspect of such a separation. The SEC views the segregation of functions as undesirable since it would deprive the securities industry of an ability to raise capital.[401]

Furthermore, the European experience seems to support well the elimination of the firewall between the two industries. Lowering the barrier between banking and securities businesses thus appears desirable. However, in the transformation period, totally lifting the firewall might be a careless decision because of the distinguishing nature of the banking business. The failure of a bank can be very contagious, to the point that it can cause huge damage to public depositors. Defining the extent to which the firewall should be lowered is therefore of significance. Both the US and Japan seem to have a good approach in reforming the regulation of the financial sector. The statutory permission on which banks can directly carry out some specified securities activities and indirectly engage in others through their subsidiaries, can be deemed as one of their reasonable approaches. It allows banks to enter securities business through their securities subsidiaries while it keeps them away from risk. Of course where such an approach is employed, it should be accompanied by necessary precautions, to avoid risks that might be incurred by both banks and their subsidiaries.

2. Whether an Entire Prohibition of Direct Involvement of Banks into the Vietnamese Securities Market Will Result in Good Outcomes

One of advantages Vietnam inherits from other countries in creating a securities regulation regime is the regulation of banks' involvement in securities markets. Having learnt from the US and Japan, Vietnam generally does not adopt an absolute segregation between banking and securities businesses. Rather, a similar approach to that of both the US and Japan in dealing with banks in this area has been employed by lawmakers. *Decree 48/1998* prohibits credit institutions, insurance companies, and holding companies from directly engaging in securities business. Those who desire to carry out securities business must establish separate securities subsidiaries.[402]

The term “credit institutions” is broadly defined under Article 20.1 of the *Credit Institution Act.* The Act classifies credit institutions in terms of ownership, under which

[400] See George J. Benston, above n. 367, Chapters II, III, and IV.
[401] See N. S. Poser, above n. 382, 244.
[402] See Art. 29.1.

credit institutions fall into four categories: state-owned, shareholder-owned, cooperatively owned and foreign-owned. The last-named can be further divided into three groups: joint-venture credit institutions, non-banking institutions and foreign banks' branches.[403] The term "credit institutions" thus denotes both banks and non-banking institutions owned by different economic sectors.

Banks are those institutions which can engage in all kinds of banking activities (including taking deposits, giving loans and providing settlement services) and other related activities. They include commercial banks, development banks, investment banks, policy banks, cooperative banks, and others.[404]

Non-banking institutions are those which can engage in a number of banking activities except for taking deposits and providing settlement service. They include financial companies, financial leasing companies, and others.[405] Aside from those, credit institutions also include people credit funds and credit cooperatives.[406]

The *Credit Institution Act* does not have any article saying that banks can or cannot engage in securities business, but since 1998, by the introduction of *Decree 48/1998*, the question has been clarified. The approach adopted here is to permit banks to carry out securities business through their securities subsidiaries. In 1999, the Prime Minister made a further effort in issuing *Decision 172/1999* to lay down a legal basis for banks to set up their own securities subsidiaries. Since all credit institutions are forbidden from having direct involvement in securities business, it can be said that Vietnam, to some extent, has a stricter segregation between banking and securities businesses compared with that in the US. Previously, in the US, only commercial banks were restricted from entering securities business, and nowadays restrictions imposed on commercial banks merely confine them within certain activities such as underwriting, dealing in securities, and purchasing securities for their own account. Other securities activities such as brokerage, dealing in certain securities and investment advisory service, can now be carried out by commercial banks. In Vietnam, all kinds of securities activities are not permitted to be directly conducted by credit institutions (including banks[407] and non-banking institutions).

A question arising is whether or not it is necessary to proscribe the direct involvement of banks in all kinds of securities activities. Today, even the restriction of access to underwriting and dealing securities to commercial banks alone has been

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[403] See Art. 12.
[404] See Art. 20.2.
[405] See Art. 20.3.
[406] See Art. 20.5.
[407] The term banks here denotes both commercial and investment banks. It should be noted that in Vietnam, the term "investment bank" differs from its use elsewhere. For example, in the US, investment banks are those whose primary purpose is to acquire finance for businesses, especially through the distribution of securities. Investment banks do not take deposits and do not deal with the public at large.[407] The *Credit Institution Act* of Vietnam, as earlier discussed, treats all types of banks as depository institutions. *Decree No. 48/1998* simply proscribes all types of banks and even other non-banking credit institutions from engaging directly in securities business. Non-banking institutions, as previously mentioned, are not permitted to carry out every kind of banking business, especially acquiring deposits from the public. It seems that there is no reasonable ground to treat them in the same manner as banks.

questioned, Vietnam seems to employ a rather special measure in regulating the scope of securities business activities carried out by banks. In today's increasingly competitive business environment, banks have been struggling to expand their markets in order to survive. Whether this provision is realistic remains to be seen.

The main justification for such a provision is to avoid risks for the securities market and for the benefit of banks themselves.[408] However, the question whether or not the entry even of commercial banks into securities business is a potential source of risk has been well documented in the US, as earlier discussed. Thus, it is possibly that the prohibition of all kinds of banks from carrying out securities activities of all kinds would merely prevent unrealistic risks, while reducing market participation, which might also lessen market competition. It seems hard to justify the denial of access by banks to some less-risky business activities such as investment advising, securities portfolio management and brokerage.

As earlier discussed, nowadays in Europe, a universal banking model has widely been adopted, and so far no serious problems stemming from that system have been reported. In the US and Japan, the barriers separating traditional banking activities of a bank from its securities operations has been blurred. Perhaps, Vietnam should not ignore such statutory development in countries around the world, on the way to improving its regulation of the involvement of banks in securities markets.

Furthermore, although the Vietnamese current securities regulation adopts the indirect involvement of credit institutions in the securities market (e.g., the permission on which those institutions can do securities business through their subsidiaries), it does not have any further provision regulating such parent-subsidiary relationship. Nothing in *Decree 48/1998*, *Decision 172/1999, Decision 04/1998,* or *Decision 78/2000* lays down necessary conditions banks and their securities subsidiaries have to be subject to in order to ensure safety for both banks and their subsidiaries.

III. FUTURE REGULATION OF SECURITIES PROFESSIONALS

1. The Need for Concrete Provisions Regulating Conflicts of Interest between Securities Firms and their Customers

Regulation of conflicts of interest between securities firms and their customers is of importance in creating public confidence in securities markets. The current regulation of securities firms adopts a rather complete system of disclosure requirements with respect

[408] See Ho Cong Huong, "Quan he giua cong nghiep ngan hang va cong nghiep chung khoan" [The Relationship between Banking and Securities Industry], (2000) 6 *Tap Chi Ngan hang* [*Banking Review*] 54, 55.

to those firms, making them responsible for reporting to the SSC and the Trading Center.[409] It also lays down general rules of conduct for securities firms.[410] Some provisions covering the relationships between securities firms and their customers can be found, but they merely deal with procedures the two parties have to follow in executing customers' orders.[411] What appears to be missing here is the provision of specific duties of securities firms in relation to their customers to avoid conflicts of interest between them.

Merely imposing on securities firms duties in finding out the financial situation and investment purposes of customers is not enough. More precisely, the revised provision should require securities firms to obtain such information before recommending a type of security so that they can ensure that the recommended security is suitable to a customer's need and financial conditions.

There should also be a provision imposing duties on securities firms to investigate the nature and risk of the securities they are going to recommend to their customers.

Another provision needed is the one pursuant to which securities firms must disclose their conflicts of interest to their customers: whether they have an interest in the security they have recommended them to purchase; and whether they act as a broker or a dealer in the relevant transaction.

Finally, the regulation should expressly prohibit securities firms from engaging in excessive trading of securities in the account of customers for the purpose of getting more commissions, and also from overcharging customers when providing services.

2. No Need for Indirect Involvement of Banks in a Number of Securities Business Activities

The fact that Vietnam has adopted a relatively strict segregation between banking and securities businesses possibly results in part from the US experience of the market crash in 1929, and in part from the situation of Vietnam. With a new securities market just opened, it is logical to be more careful in regulating that market. However, it has been well documented that banks' participation in stock markets in the US prior to the market crash of 1929 had not been the cause of the market crash; and that the previous separation of banking and securities business in the US is, more or less, out of context. A question arising is why Vietnam should follow such an old trend that has been dropped over time almost everywhere in the world: firewalls have been, little by little, lifted in the US and Japan and have been totally eliminated in Europe.

Securities markets in Vietnam therefore, should be more open to banks. Less risky securities services such as brokerage, investment advice and securities portfolio management could quite well be carried out directly by banks. The presence of banks in the securities market, even merely within these business areas, would diversify market participation and also strengthen the competitive forces in the market, which in turn

[409] See *Decision 79/2000,* Art. 5.
[410] See *Decision 04/1998,* Art. 20.
[411] See *Decision 79/2000,* Arts: 10 - 14.

would promote market development. On the other hand, this would also expand the business environment of banks and enable them to increase their chances to earn profits.

Other highly risky business activities such as underwriting and dealing in securities should probably be left for banks' securities subsidiaries, to assure the soundness of the banking system.

3. The Need for More Concrete Provisions Regulating Banks and Securities Subsidiaries

Where banks are permitted to set up their own securities subsidiaries, some necessary requirements should be imposed both on banks and on their subsidiaries, so as to avoid risks.

There should be requirements concerning capital, assets and the state of management that banks have to meet in order to set up subsidiaries. After being established, banks should be required to deduct the amount invested in the subsidiaries from their capital for purposes of minimum capital requirements provided in the banking law.

Some restrictions are also required on transactions conducted by subsidiaries of banks to ensure that the securities business they conduct will not affect their parent banks' soundness.

CHAPTER V
WHETHER THE EXCHANGE MARKETS ARE WELL ORGANIZED

One of the factors that have a crucial impact on market development is the structure of the exchange market. Whether the impacts are positive or negative depends on whether an adequate legal form for the exchange market has been adopted. What is required, then, is to work out which legal structure for the exchange market can assure the attainment of a well functioning securities market.

This chapter examines the current legal form of the exchange market adopted in Vietnam in relation to those adopted in other jurisdictions and their recent movements. It maintains that such a legal structure cannot foster good outcomes for Vietnam.

I. STOCK EXCHANGES AND THE SECURITIES INDUSTRY: PAST AND PRESENT

1. Mutual Form of Stock Exchange

Since their inception under coffee shop meetings of stockbrokers in London and Amsterdam, public stock exchanges in many jurisdictions have developed as cooperatives or mutual enterprises,[412] which were spontaneously chosen by the exchange founders.[413] In the US, the New York Stock Exchange, the American Stock Exchange, the futures exchanges, and the regional stock exchanges are all structured as cooperatives.[414] In the UK, such a structure was also employed by the London stock exchange, and by the four futures exchanges in London.[415] In Australia, the Australian Stock Exchange and the Sydney Future Exchange were developed as mutual enterprises.[416]

Under the cooperative or mutual form, a stock exchange operates on a not-for-profit basis. Members of the exchange are those who own seats on the exchange and get benefits from their membership such as lower trading costs or access fees. However, this does not imply that all stock exchanges always operated in such a way. The London Stock Exchange operated on a for-profit basis throughout the early 19th century and during the

[412] See Frank Donnan, "Self-regulation and the Demutualization of the Australian Stock Exchange" (1999) 10, *Australian Journal of Corporate Law* 1, 4; see also John Coffee (2002), above n. 187, 1800.
[413] See Caroline Bradley, "Demutualization of Financial Exchanges: Business as Usual?" (2001) 21 *Journal of International Law and Business* 657, 660. Hereinafter, Caroline Bradley.
[414] See Oliver Hart and John Moore, "The Governance of Exchange: Members' Cooperative Versus Outside Ownership", (1996) (12) (4), *Oxford Review of Economic Policy* 53, 54. Hereinafter, O. Hart and J. Moore.
[415] Ibid.
[416] See Frank Donnan, above n. 412, 5 and 15. The Australian Stock Exchange was a company limited by guarantee, having neither share capital nor shareholders. It was owned collectively by its members, whose liability was limited to the amount of the guarantee they had nominated. Members were also the users of its facilities.

first half of the 20th century, and distributed generous amounts of dividends to its members.[417] The amendment of the Exchange's deed of settlement in 1948 stopped the Exchange's payment of dividends.[418] In 1986, the London Stock Exchange converted into a private limited company[419] (non-profit making company) under the *Company Act* of 1985.[420]

The not-for-profit structure of mutual stock exchanges around the world has been, however, dominant until recently.[421] A mutually owned stock exchange differs from an externally owned one in its governance structure, and members' financial rights.

Mutual structure of governance permits the exchange members at the same time to own, control, and govern the exchange. Members are also owners and managers of the exchange. They are all equal in decision-making and subject to the one-member, one-vote rule.

Members' financial rights or ownership rights do not allow the members to access the exchange's surplus. Rather they give the members an entitlement to the direct use of the exchange's trading services at a lower cost. Ownership rights are thus also trading rights and usually not easily transferable, while revenues from the business are accumulated rather than distributed.

The mutual form was attractive not only within the securities industry but also in other areas such as banking and insurance. Such a tendency continued even after the introduction of the joint stock company form.[422] Recently, however, this tendency has been reacted against and replaced by another movement. In the security industry, such a movement brings a new legal form for stock exchanges.

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[417] Ibid (Frank Donnan), 13-14; see also Roberta S. Karmel, "Stock Exchange Demutualization in Sweden and Australia", (Thur. Aug. 19, 1999) *New York Law Journal* 3, para. 3. Hereinafter, Roberta Karmel (1999). (This Article is published in *New York Law Journal*, in Securities Regulation Section, Page 3, as a column. Page number for all the citations from the article thus cannot be indicated. The pinpoints indicating paragraph number, counted by the author of this paper, will be provided instead of page numbers. The same will be applied with other Articles found in *New York Law Journal.*)

[418] Ibid (Frank Donnan), 14.

[419] *Company Act 1985* (Eng) c 6, s 81 says:

"(1) A private limited company (other than a company limited by guarantee and not having a share capital) commits an offence if it--

(a) offers to the public (whether for cash or otherwise) any shares in or debentures of the company; or (b) allots or agrees to allot (whether for cash or otherwise) any shares in or debentures of the company with a view to all or any of those shares or debentures being offered for sale to the public (within the meaning given to that expression by section 58 to 60)."

[420] See "London Stock Exchange: History", http://www.londonstockexchange.com/about/about_05.asp, visited Aug. 8, 2002. Hereinafter, "London Stock Exchange: History".

[421] See Craig Pirrong, "A Theory of Financial Exchange Organization", (2000) 43 *The Journal of Law & Economic* 437, 442. Hereinafter, Craig Pirrong.

[422] See Caroline Bradley, above n. 413, 662.

2. Corporate Form of Stock Exchange

Today, the whole world is experiencing a new global movement, where stock exchanges are converting themselves from mutual enterprises into shareholder-owned companies.[423] Such a movement was initiated by the Stockholm Stock Exchange in 1993, and quickly followed by the Helsinki Stock Exchange in 1995, the Copenhagen Stock Exchange in 1996, the Amsterdam Stock Exchange in 1997, the Australian Stock Exchange in 1998,[424] and then Toronto Stock Exchange, Frankfurt Stock Exchange, Singapore Stock Exchange, Hong Kong Stock Exchange and so on.[425] The most recently demutualized ones include the London Stock Exchange,[426] the Paris Bourse, the Chicago Mercantile Exchange and the Deutsche Bourse.[427] In Japan, the Tokyo Stock Exchange was demutualized in November, 2001.[428] In the United States, the New York Stock Exchange (NYSE), the National Association of Securities Dealers (NASD)[429] and the American Stock Exchange[430] have been considering a privatization proposal since 1999. In January, 2001, NASD completed a private placement while NYSE was in the process of disclosing its privatizing intention.[431]

After going through the privatization process, a stock exchange will turn into a "for-profit" entity from a "not-for-profit" entity, or a new corporation will be formed. The exchange's proprietors will be shareholders instead of members. Where the exchange goes public, its shares will be listed and freely traded. In the literature, such a process has often been referred to as "demutualization".

3. Reasons for Demutualization

Deficiencies of the mutual form of stock exchanges have recently been brought into discussion. Generally, commentators contended that it is not as efficient as the corporate form.[432] The following discussion will examine whether deficiencies are the causes that force stock exchanges to demutualize.

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[423] John C. Coffee Jr., "Privatization and Self-Regulation of Stock Exchanges", (May 20, 1999) *New York Law Journal* 5, para. 2. Hereinafter, John Coffee.
[424] See John Coffee (2002), above n. 187, 1800; see also Roberta Karmel (1999), above n. 417, para. 11 & 20.
[425] See Laura Cha, (Deputy Chairman and Executive Director Securities & Future Commission, at the Commonwealth Club California, USA, Jun. 6, 2000), "Securities Market Reform: the Hong Kong Experience", http://www.hksfc.org.hk/chi/press_releases/html/sp.../lc000606.htm, visited May 26, 2001. Hereinafter, Laura Cha.
[426] The London Stock Exchange was privatized in 2000. Since July 2001, it has become a listed company. For further information, see "*London Stock Exchange: History*", above n. 420.
[427] See Roberta S. Karmel, "Turning Seats Into Shares: Causes and Implications of Demutualization of Stock and Future Exchanges", (2002) 53 *Hastings Law Journal* 367, 368 – 369. Hereinafter, Roberta Karmel (2002).
[428] See Tokyo Stock Exchange: History, http://www.tse.or.jp/english/about/history.html, visited Aug. 9, 2002.
[429] See Roberta Karmel (1999), above n. 417, para. 1.
[430] See John C. Coffee Jr., above n. 423, para. 2.
[431] See Caroline Bradley, above n. 413, 668.
[432] See O. Hart & J. Moore, above n. 414, 56; Frank Donnan, above n. 412, 8-9; and Roberta Karmel (1999), above n. 417, para. 5 & 19; Laura Cha, above n. 425.

Critics of the mutual form attribute deficiencies of this form to the two following elements: the variation in the exchange's membership in terms of the size or nature of the members' business, and the extent to which the exchange has to compete. They argue that these elements have direct impacts on the relative performance of different stock exchanges. Mutual enterprises seem to face constraints in their membership and a lower degree of competition by comparison with stock enterprises. As a result, the latter is seen as more efficient than the former.[433] Some other opponents of the mutual form of stock exchange go further in contending that it is the voting tendency, the structure and the governance of mutual exchanges that make the exchanges hard to respond in a timely manner to the challenges of new technology. It is very unlikely that members will vote for any change concerning the subscription of additional capital.[434] The same can be said about voting for changes relating to the customary way in which the stock exchange does business and concerning the potential value of membership.[435] Making decisions on contentious business seems much harder to do in a mutual than in a corporate structure.[436] The structure and governance of a mutual exchange tend to favor members' interest rather than those of the market and the investors. In the absence of control by competition or regulation over market power, mutual exchange members have the potential to influence the price, quality and range of services offered by the exchange.[437] All reveal the weaknesses of the mutual form of exchanges.

A proponent of the mutual form, however, has argued that the corporate form does not affect efficient monitoring of management. Rather it is competition among firms that promotes the efficiency of such a management; that the diversified ownership in stock enterprises even weakens shareholders' power to monitor management effectively; and that the non-ownership structure of the mutual form does not necessarily cause inefficient monitoring.[438]

Perhaps there are questions here arising that are more important than whether the mutual form is actually less efficient than the corporate form. Such questions are: why mutual stock exchanges were in operation for centuries, yet their deficiencies were not a controversial issue; why such deficiencies have become a matter of concern only recently; and what newly emerging phenomena have made the mutual form of stock exchanges to reveal weaknesses which have made it no longer appropriate for today's need. So, what are those phenomena?

One can easily recognize that technological advance has brought new life for the securities industry in the last decade: that is the change from floor trading to screen trading. Perhaps this is one of the factors, if other factors actual exist, that make a traditional exchange with a physical trading floor and membership cards to be outdated,

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[433] Ibid (O. Hart & J. Moore).
[434] See Laura Cha, above n. 425; John Coffee, above n. 423, para. 5.
[435] Ibid (Laura Cha).
[436] See Roberta Karmel (1999), above n. 417, para. 19.
[437] See Laura Cha, above n, 425; see also Roberta Karmel (1999), above n. 417, para. 19.
[438] See Fama, "Agency Problems and the Theory of the Firm", (1980) (88) (21) *Journal of Political Economy* 288, 289 - 295.

or no longer to have much value. This factor has thus put traditional exchanges into tense competition with other electronic communication networks (ECNs) or alternative trading systems (ATSs). In this competition, mutual exchanges are in need of financial support for computerizing their trading services. Clearly, in doing so, exchanges need first to raise more funds, which seems hard to do with a mutual structure, as earlier mentioned. Switching to another form that will enable them to adapt with new challenges of technological development has thus become urgent.

There has been evidence supporting the above-mentioned hypothesis. Chicago Mercantile Exchange Inc. said that demutualization enables it to generate a new financial decision-making mechanism in accordance with the value of equity held by each member; to facilitate the exchange in making use of new business strategies as well as to allow the exchange to cooperate with strategic partners; to permit its governance and managerial structure to adapt quickly to a competitive environment; and to provide exchange members with equity values. The Australian Stock Exchange found it hard, at the same time, to represent interests of both groups, large and small brokers, and compete with other exchanges. Thus it sees demutualization as a solution to the problem. The Toronto Stock Exchange deems demutualization as a factor that can foster the competitiveness and commercialization of the exchange as well as channel the exchange into paying more attention to customers.[439]

These items of evidence, once again, reveal actually existing weaknesses of the mutual form of stock exchanges that arose when the securities industry entered a new era of technological advance. And the move of a considerable number of mutual-form exchanges toward for-profit corporations further tends to prove that all of those demutualized stock exchanges had encountered the same problems and tried to overcome such situations by demutualizing. Demutualization seems to be the single means employed by exchanges around the world to enable them to escape from constraints of the mutual form and so to cope with new challenges of technological change. It is a matter of adapting to a new environment. It can be said that technological development itself has triggered competitive force exchanges have to face, and has pushed them in such a demutualizing movement.

This view seems to be supported by Richard Grasso and Henry M. Paulson. They also see competition as a consequence of technology in maintaining that technology has given rise to the development of new forms of competition. One such form is ECNs that might adversely affect the efficiencies of stock exchanges.[440]Grasso believes that after being demutualized, the owners of stock exchanges will be diversified; competitive challenges will be faster responded to in a more innovative way; and all of the financial

[439] See Caroline Bradley, above n. 413, 668– 670.

[440] See Richard A. Grasso (Chairman and CEO of NYSE), "Investor Ownership of Stock Exchanges", (Sep. 28, 1999) *FDCH Congressional Testimony,* <Academic Search Elite>. Hereinafter, Richard Grasso; see also Henry M. Paulson (Chairman and CEO of Goldman Sachs and Co.), "Hearing on the 'Financial Marketplace of the Future'", (Feb. 29, 2000) *Senate Banking Committee,* http://www.senate.gov/~banking/00_02hrg/022900/paulson.htm, visited May 26, 2001.

requirements for competing with private trading systems will be more easily met. In other words, demutualized stock exchanges can cope with competitive challenges.[441]

John Coffee looks at the factor that resulted in the need for demutualization by closely focusing on the case of NASDAQ. In working out why NASDAQ should privatize, he thinks that the intense competition from ECNs which NASDAQ has been facing is the reason; and that as a not-for-profit organization, NASDAQ runs into financial difficulties with such competition with ECNs. He further maintains that, by privatization, NASDAQ will be able to raise funds directly from capital markets so that it can improve technology based on such mobilized funds.[442] Here, although he does not directly say that technology leads to competition, Coffee points out clearly that it was the competition in modernizing technology with ECNs that triggered NASDAQ's intention to demutualize.

In the literature, commentators, however, do not seem to have a unanimous view concerning the reasons for the demutualization of stock exchanges. They do not seem to agree that technological development is the single reason that leads to demutulization. Apart from rapid changes in technology, some other factors pointed out include: competition facing mutual stock exchanges and the globalization of securities markets.

Roberta Karmel agrees that technology is one of the factors that lead to demutualization, but she does not see competition as a consequence of technology. She clearly distinguishes the two factors, technology and competition, that lead to demutualization.[443] She points out that screen trading which has replaced trading on exchange floors on most exchanges is one of the rationales leading to stock exchange demutualization.[444] But she also maintains that competition, regardless of whether it is among exchanges themselves or between exchanges and ATSs or between domestic and foreign exchanges, is another cause that has pushed exchanges into demutualization.[445] However, one can argue that, whether it is competition between exchanges or between exchanges and ATSs, or between domestic and international exchanges, all were originated or triggered by technological development. It is technology that introduces electronic trading system so that for-profit business entities having strong financial resources can computerize their trading services, which in turn, causes transactions on traditional trading floors to become costly; it is also technology that has turned the role of traditional brokers down by providing investors with complicated market analysis at a click on their own personal computers. Thus it seems that the original cause of demutualization remains technological advances.

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[441] Ibid (Richard A. Grasso).
[442] See John Coffee, above n. 423, para. 3.
[443] See Roberta Karmel (1999), above n. 417, para. 2.
[444] Ibid, para. 4.
[445] Ibid, para. 5, 11, and 16. She points out that the Stockholm Stock Exchange and the Australian Stock Exchange decided to demutualize to enable them to compete in the international environment.

Lisa I. Fried[446] and Doris Dumlao[447]posit another factor leading to demutualization, namely the internationalization of stock exchanges or the globalizing challenges. The demutualization of exchanges in New York, London, Hong Kong, Singapore, and Australia is said to have been for the purpose of raising money for the exchanges to enable them to adapt to globalizing challenges.[448] However, arguably, this actually results from the fact that, in the globalization process, exchanges around the world have to compete with each other, both in terms of technology and finance (to afford them to be equipped with such technology), in order to survive. And here, once again, technological challenges are clearly the cause of demutualization.

Demutualization, therefore, has a number of advantages. It eliminates constraints resulting from the governance structure and voting tendency of traditional exchanges. It diversifies ownership of the exchange and permits external owners. In that way it creates a new form of governance for exchanges and separates members' ownership rights from their trading rights and generates value to these rights. It converts members' ownership rights into shares, but still maintains the trading rights of the owners who are also securities firms. In addition, demutualization transforms mutual exchanges into commercial entities that tend to give more weight to the business aspects of operating a marketplace: they will operate on a more customer-oriented and profit-driven basis. Demutualization will also enable the exchange to widely raise capital from the public, which in turn will facilitate the exchange in coping with well-financed competitors.

4. Matters of Concern about the Consequences of Demutualization

Having such advantages, still demutualization is a matter of concern. That is, demutualization might render the stock exchange unable to carry out well its self-regulatory functions, because of the conflict of interests it has to face, and the threat of takeovers and mergers over corporate stock exchanges.

Frank Donnan is suspicious of the Australian Stock Exchange's ability in enforcing its listing rules against itself.[449] John Coffee finds almost unacceptable the existence of a private body having regulatory authority over its competitors; he also wonders whether NASD Regulation Inc. could enforce its own levies in the absence of significant revisions of NASD and SEC rules.[450] Roberta Karmel worries about "*whether the profit motive will undermine the fairness and effectiveness of self-regulation*".[451] Aside from the concerns of problems arising when a demutualized exchange lists and trades its own shares[452] and

[446] See Lisa I. Fried, "Plans Debated for Stock Markets' For-Profit Conversion" (Sep, 30, 1999) *New York Law Journal* 5, para. 3.
[447] See Doris C. Dumlao, "State Funds' Participation Key to PSE Demutualization", *Philippines Daily*, (Nov. 6, 2000) http://www.inquirer.net/issues/nov2000/nov06/business/bus_5.html, visited May 26, 2001.
[448] Ibid.
[449] See Frank Donnan, above n. 412, 88.
[450] See John Coffee, above n. 423, para. 8 – 9.
[451] See Roberta Karmel (1999), above n. 417, para. 6.
[452] See Caroline Bradley, above n. 413, 682– 686.

of problems occurring when a proprietary business acts as a regulator,[453] Caroline Bradley even fears the risk that a proprietary exchange will become a takeover target or be merged into another.[454] However, Richard Grasso's observation seems to address, in part, these concerns:

> *I believe these concerns are well-intentioned but ill-founded. Because of the long-standing importance of market integrity to the NYSE's competitive position, converting to for-profit status will, if possible, strengthen our resolve to maintain the highest standards of self-regulation.*[455]

Richard Grasso even goes further in contending that *"demutualization will strengthen the NYSE's commitment to regulation"*; that *"the NYSE has successfully regulated its competitors for over half a century"* and that *"spinning off regulation would weaken investor protection"*.[456] On balance, Grasso's arguments are in favour of the demutualization of the NYSE. In practice, there has come into existence a fear of conflicts of interest occurring when a private body is responsible for enforcing listing standards against itself. However, there seem to be some good ways to cope with the problems. After the demutualization of the Stockholm Stock Exchange and the Australian Stock Exchange, both the Swedish and Australian government dealt with such problems, by vesting in their public securities watchdog a supervisory power over public disclosure and the compliance with listing standards of the demutualized stock exchange.[457] And, to date, such a measure seems to have worked well. The *Corporation Law Amendment Act* 1997 of Australia, however, does not narrow down the regulatory framework of the Australian Stock Exchange. Justification of this is that the Exchange has been a for-profit entity since its inception in 1987, and *"its conversion to a public limited company simply confirms the fact."*[458]

The concern that demutualized stock exchanges might be threatened by takeovers and mergers, although stemming from practical experience of what happened with the Stockholm Stock Exchange[459] and the London Stock Exchange,[460] does not seem to be a

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[453] Ibid, 686 – 695.
[454] Ibid, 696 – 701.
[455] See Richard A. Grasso, above n. 440.
[456] Ibid.
[457] In Sweden, new legislation was passed to give the Financial Supervisory Authority a direct supervision of public disclosure by OM (a clearing house and option exchange in Swedish stocks) and the Stockholm Stock Exchange. Independent disciplinary committees having rights to initiate disciplinary proceedings with respect to companies with a qualified holding in an exchange, were set up. For further information, see Roberta Karmel (1999), above n. 417, para. 12-13.

In Australia, the *Corporation Law Amendment Act 1997* (*Australian Stock Exchange Act*) preserves the essential features of self-regulation and the autonomy of the Australian Stock Exchange while giving the Australian Securities and Investment Commission powers to oversee the conduct of SROs. For further information, see Frank Donnan, above n. 412, 68 - 69.
[458] Ibid. (Frank Donnan), 68.
[459] The merger of the Stockholm Stock Exchange by OM Gruppen will be mentioned later.

real threat if necessary measures are employed. To cope with this potential problem, the Australian *Corporation Law Amendment Act* imposes limits on the holding (no more than 5%) of shares in the Australian Stock Exchange, so that no single person or entity can gain control of the exchange and the Exchange's ownership will be diversified.[461]

Even in the absence of such statutory limitations, it can be argued that takeovers and mergers amongst stock exchanges are not always harmful to the public. Stock exchanges have long been seen as market places for capital-laden investors to meet capital-needy businesses, places where business entities can broadly raise funds from the public to meet their financial demands to expand their businesses. In that sense, even takeovers and mergers do occur, but after the transformation of the relevant stock exchange, if the exchange remains a fair, transparent and efficient marketplace, then what harm would actually result for the public? The Swedish experience seems to support this argument. Since the Swedish government does not impose limits on the holding of shares as the Australian government does, the Stockholm Stock Exchange, after being demutualized, was controlled by OM, a 20% shareholder, and then in early 1998 was merged into OM. However, the Swedish government thinks that even this would be beneficial to the country's capital market. To strike a balance, on the one hand, the new law enhances the overseeing power of the Financial Supervisory Authority over the Exchange; and on the other hand, the Swedish government has tended to become a 10% shareholder of the combined entities.[462]

Regardless of what happened in Sweden and Australia, and of the on-going controversy over demutualization in the literature, stock exchanges around the world have recently witnessed rapid changes. This is because technology that has substantially lowered transaction costs and allows investors direct access to on-line trading has put much pressure on exchanges. As a result, traditional transactions on tangible trading floors have become out-dated and costly. In addition, the globalization of securities markets has blurred geographical borders of traditional exchanges. Exchanges must reform themselves to attract cross-border customers or to compete with their counterparts. The initial stage of such a reform effected by traditional exchanges is demutualization. Perhaps the reform will not stop here but will need further innovation in terms of exchange governance structure and changes in the extent to which the exchange can act as a self-regulator, to enable demutualized stock exchanges to overcome new challenges introduced by the new corporate form of stock exchange, the stock corporation.

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[460] The London Stock Exchange (LSE) had also been threatened by a hostile tender offer by OM Gruppen in August 2000. However, the LSE was ultimately successful in fending off the offer. For more information, see Caroline Bradley, above n. 413, 657, 697-698.

[461] See *Australian Corporation Act 2001* (Cth) s 766E (Unacceptable Ownership Situation) under Division 2 (Limitation on holding shares in the Exchange). This Section reads: *"For the purposes of this Division, an unacceptable ownership situation exists if any one person's voting power in the Exchange exceeds 5%."* http://www.austlii.edu.au, visited Jul. 5, 2002.

This provision was first introduced in the 1997 Amendment of the *Australian Corporation Act*. For further information, see Frank Donnan, above n. 412, 67.

[462] See Roberta Karmel (1999), above n. 417, para. 12.

II THE LEGAL STRUCTURE OF THE VIETNAMESE EXCHANGE MARKETS IN RELATION TO AN EFFECTIVE MARKET

1. Securities Trading Centers as Non-profit Organizations that Belong to the SSC

The Vietnamese Government intends initially to set up securities trading centers in Hanoi and Ho Chi Minh City (HCMC) and to upgrade them into stock exchanges later.[463] The grounds for such an intention was claimed to be: (1) lack of commodities for securities markets; (2) poor awareness of public investors about securities and securities markets; (3) lack of expertise in securities firms; (4) lack of practical experience in the management apparatus of securities markets; and (5) low level legal documents regulating securities markets.[464] It was further argued that as a stock trading center, the center will be fully supported from the SSC in terms of granting licenses for public offering, and licenses for running securities business.[465] A question that might arise here is what obstacles the SSC would have to encounter in providing such supports for stock exchanges if the exchanges were initially set up as such instead of securities trading centers.

Because HCMC is the biggest industrial and commercial center in Vietnam, the first securities trading center had been planned to be erected there in late 1998. While this intention was being put into practice, a number of objective and subjective difficulties arose, which delayed its birth until July, 2000. The reasons for the delay are numerous, but some principal ones include: (1) the Asian Financial Crisis in late 1997;[466] and (2) the lack of commodities for trading in stock trading centers.[467]

Although having learnt from the experience of countries around the world, neither the *mutual form* nor the *corporate form* of stock exchanges has been brought into the context of Vietnam. Under *Decree 48/1998*, a securities trading center is a non-profit-making legal person having its own seal and bank accounts. It belongs to the SSC and its operational expenses are covered by the state budget. Its main functions include: managing, conducting and supervising securities transactions occurring in the securities trading center.[468]

Securities trading centers, thus, act as components of the SSC rather than as independent organizations having the full functions of a securities trading center. An arising question is whether or not a governmental administrative body should be put so closely with securities trading entities.

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[463] See *Decree No. 48/1998*, Art. 20; See also *Decision No. 127-1998*, Art. 1.
[464] See Tran Dac Sinh (et al), "Nhung van de co ban trong quan ly, to chuc, van hanh va phat trien Trung tam giao dich chung khoan o Viet nam" [Fundamentals in Management, Organization, Operation and Development of Securities Trading Centers in Vietnam], (*Working Paper, Ho Chi Minh City Securities Trading Center, State Securities Commission*, 2000), 77. Hereinafter, Tran Dac Sinh.
[465] Ibid.
[466] See above n. 6.
[467] See above n. 5.
[468] See Art. 21.

The rationale for adopting a government-owned rather than a mutual or corporate securities trading center, mainly involves the three following issues. First, the mutual form of stock exchange is only suited to countries having a highly developed economy and financial market, and a complete legal framework for the operation of securities market.[469] The argument might be further developed regarding the way that the corporate form of exchange is only appropriate for the even more highly developed economies.

Secondly, for the time being, both of the mutual and corporate forms are not feasible since the notion of securities markets is quite new in Vietnam. Securities firms are short of the knowledge, experience, and necessary financial resources required to set up and to run a stock exchange by themselves. Only the government can gather all necessary resources for the erection and development of securities markets. For this reason, Vietnamese securities trading centers should be set up by the Government as governmental organizations. In other words, the government-owned form of securities trading centers is the most suitable choice for Vietnam.[470]

Thirdly, in the early stage, governmental ownership and government management of securities trading centers are required to ensure the fairness and discipline of the market. Securities trading centers that are directly run by the state on a not-for-profit basis will maximally assure the interests of public investors. This is of importance when Vietnam does not yet have a complete and transparent legal framework governing securities markets. [471]

In response to the above-mentioned justifications, it can be argued, first, that as a matter of fact, in most countries around the world, it was the securities markets that triggered the passage of securities laws, while in Vietnam it was the laws that triggered the birth of the securities market. Accordingly, the Vietnamese securities market was probably born with a more complete legal framework than were many other securities markets around the world. Furthermore, the answer to the question whether the economy and financial market of Vietnam in this 21st century are less developed than those of England and America in the 18th century[472] remains unclear. Thus, it can hardly be said that Vietnam could not adopt the mutual form of stock exchange for the reason that the Vietnamese securities market does not have a complete legal framework for its operation, or because Vietnam does not have a highly developed economy and financial market as other countries have when their first stock exchange commenced business.

Practical evidence shows that even when economies in general and financial markets in particular are highly developed, it is the time when the mutual structure of stock exchanges can become outdated. The whole world has experienced a recent

[469] Tran Dac Sinh, above n. 464, 76.
[470] Ibid.
[471] Ibid, 76-77.
[472] In practice, some financial exchanges developed as mutual businesses before the introduction of general incorporation statutes. For example, the London Stock Exchange commenced its business in coffee house in Change Alley, and then moved to a building marked as "The Stock Exchange" in 1773; the early stage in the development of the New York Stock Exchange was marked by the Buttonwood Agreement of 1792, entered into by brokers in New York. For further information, see Caroline Bradley, above n. 413, 662 – 664.

movement in which stock exchanges in various jurisdictions have been converted from mutual into corporate form in response to technological advances achieved by highly developed economies, as previously discussed. The corporate form of stock exchanges, however, does not seem only appropriate with today's highly developed economies and financial markets. Japan employed a corporate form for its stock exchanges even in the late 1870s, when its stock exchanges first saw the light of day. Tokyo and Osaka Stock Exchanges, the first two exchanges established in Japan, took the legal form of stock corporations and worked quite well.[473] This fact provides strong evidence that it would be quite feasible to adopt the stock corporation form for an exchange market at the time such a market first commences business.

Secondly, most stock exchanges around the world had initially been set up under the form of mutual organizations by member firms of stock exchanges, or even under the corporate form as occurred in Japan. However, they did not seem to encounter any financial problem in raising funds for the establishment of the exchanges and for their operation. The early corporate-form stock exchanges in Japan even proved their advantageous position in raising funds from the public. It was reported that their shares were listed and traded on the particular exchanges and were even the most popular shares in trading volume.[474] The corporate-form stock exchanges in Japan were finally dissolved in 1947. The reason, however, was not because of their inappropriate legal structure, nor was it their failure in mobilizing necessary funds to run the exchanges. Rather the reason stemmed from the political situation of Japan at that time, which made it impossible for corporate-form stock exchanges to get the authorization of the occupation authorities.[475]

On this point, it would seem to be undervaluing the financial potentiality of the public if one were to say that the government is the only entity that can afford the pecuniary demands of establishing an exchange market. Even if the establishment of the first trading center actually required big financial resources to the point that the Vietnamese securities firms could not afford it by themselves, another alternative is that the Government could financially support them to promote the birth of the first securities trading center. Since the mutual form is no longer appropriate for today's securities industry, as noted above, the government could promote the birth of the exchange market by establishing a trading center under the form of a stock corporation, with the government as a controlling shareholder. This approach is very likely to materialize, since, three months before the date the trading center was to come into existence, it was

[473] In Japan prior to 1878, there were no stock exchanges. The *Stock Exchange Ordinance of 1878* adopted the stock corporation form for stock exchanges. Tokyo and Osaka stock exchanges were established under that form.

The *Exchange Law of 1893*, which had been in force for 50 years, continued to recognize the stock corporation form, in parallel with membership organization form for stock exchanges. And in fact every stock exchange at that time was set up under the form of a stock corporation, not that of a membership organization.

For further information, see Louis Loss *et al* (eds.), above n. 261, 27.

[474] Ibid.

[475] Ibid, 28.

reported that there had been four securities firms established[476] to be ready to participate in the center's operation. Those firms together with the government would be quite able to become the founding shareholders of the trading center.

Thirdly, the idea that state-ownership of non-profit securities trading centers will maximally assure the interest of public investors sounds suspicious, since in most countries the stock exchanges have been owned either by members under a mutual form, or by shareholders under a corporate form; and such ownership forms have done no harm to public interests. If government ownership and government management could really ensure the fairness and discipline of the market, there would be no need for privatizing state enterprises around the world.[477] The arguments for privatizing state-owned stock exchanges will be further discussed when considering the legal structure of the planned stock exchange in Vietnam.

The organization of securities trading centers in Vietnam seems to be distinct but not unique. At least in China, the current *Securities Law of the People's Republic of China*, which was adopted in December 1998, still defines a stock exchange as a non-profit making legal person,[478] regardless of the fact that China is about a decade ahead in building up stock markets compared with Vietnam.[479] The legal form of Chinese stock exchanges is however not clearly provided for in the Law. If one merely looks at the provisions concerning members' financial rights, one might think that stock exchanges take the form of a mutual organization. That is because Article 98 of the *Securities Law of the People's Republic of China* says:

> *The income from various charges that is at the discretion of a stock exchange shall first be used to ensure the normal operation and gradual gains improvement of the premises and facilities of the stock exchange.*
> *The gains accumulated by a stock exchange shall belong to its members, and its rights and interests shall be shared by the members. The accumulated gains may not be distributed to the members while the stock exchange is in existence.*

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[476] Those firms are Bao Viet Securities Company, Securities Investment Company, Ltd., De Nhat Securities Joint Stock Company, and Sai Gon Securities Joint Stock Company. See "Vietnam is set to Launch Stock Exchanges in July", (Apr. 24, 2000) *ASIA PULSE*, <LexisNexis: All Sources: Country & Region: Vietnam: Country Reports: Vietnam Country Files>.

[477] It is reported that in contrast to decades ago when privatization of state-owned enterprises was only discussed in a few industrial countries, today, privatization is moving forward very fast in many countries throughout the world. For more information, see "Expediting the Privatization of State-Owned Enterprises in Taiwan" (Feb.2001, Sectoral Planning Department, CEPD), http://www.cepd.gov.tw/english/special/9002212.htm, visited May 4, 2002.

[478] See *Securities Law of the People's Republic of China 1998*, Art. 95. The English version of this law was found at http://www.csrc.gov.cn/CSRCsite/eng/elaws/elaw05.htm, visited Apr. 25, 2002.

[479] The first stock exchange in China, the Shanghai Stock Exchange, was established in 1990. For further information, see Roman Tomasic, "The Securities Law of the People's Republic of China: An Overview", (1999) 10, *Australian Journal of Corporate Law* 1, 3.

If one further looks at the governance structure of stock exchanges in China, one might gain the impression that they are governmental organizations. Article 99 says: *"A stock exchange shall have a board of governors."* And Article 100 states: *"A stock exchange shall have a general manager, who shall be appointed and removed by the securities regulatory authority under the State Council."*

Another example of a state-owned stock exchange is the case of the Cayman Islands Stock Exchange established in 1997. Although it is state-owned entity, it takes the legal form of a private limited company and operates as an independent entity.[480]

Vietnam is probably one of a very limited number of countries where securities trading centers are owned by the state, as a component of the public securities regulator, the SSC. Experience from other developed securities markets around the world shows that securities trading activities should be separated from governmental management activities, and stock trading centers should be independent legal entities.[481] Vietnam should have a worldwide comparable model for its current securities trading centers as well as for its planned stock exchanges.

2. The Uncertain Legal Structure of the Planned Stock Exchanges

The intention of the government to convert securities trading centers into stock exchanges in the future is explicitly revealed in *Decree 48/1998*:

> *The Central Transaction Market will be organized step by step from Securities Trading Centers to Stock Exchanges.*[482]

According to the language of this Article, it seems that the stock exchanges will be put into use when the trading centers become mature, or the stock exchanges will be founded on the maturity of the securities trading centers. Thus, by the time the stock exchanges come into operation, all necessary conditions required for running formal stock exchanges will presumably be available.

Although such an intention is clearly stated in *Decree 48/1998*, the legal structure of the planned stock exchanges remains ambiguous. Article 23, *Decree 48/1998* merely says that the planned stock exchanges are legal entities having financial autonomy, operating under the supervision and administration of the SSC. The governance of the planned stock exchanges is to be vested in a management board. The board is to be composed of nine members: one president, two vice presidents (one being the general managing director), and six ordinary members (two members representing securities firms; two for the public, and two for the government). The components of the management board represent different interests, but they are all to be appointed and dismissed by the government. The

[480] See "The Cayman Islands Stock Exchange": http://www.cxs.com.ky, visited May 3, 2002.
[481] In countries having long historical development of securities markets such as the UK, US, and Japan, stock exchanges have never been operated as a dependent government organization. Rather they have been established and operated as independent legal entities.
[482] See Art. 20.

president, vice presidents, and general managing director are to be appointed and dismissed by the prime minister based on recommendation from the SSC president. Other members are to be selected by the president of the SSC for appointment and dismissed.

Though the capital raising mechanism of the planned stock exchanges is unclear, their governance structure gives an impression that they are designed as government-owned organizations.

That impression is perhaps true since policymakers still argue for a state-owned form of stock exchanges. Their arguments are based on similar grounds to those used in defending the state-owned form of securities trading centers.[483] By adopting a state-owned structure for planned stock exchanges, Vietnam then will have stock exchanges whose legal form is different from those of almost all other stock exchanges around the world (which have been independent entities in the form of mutual enterprises). In addition, there has been a global tendency towards demutualizing stock exchanges, the question whether the statutory structure of the planned stock exchanges in Vietnam is appropriate or not should be taken into account, in order to avoid failures in attaining a well operational securities market.

Furthermore, by the time the stock exchanges are established in place of the current securities trading centers, the experimental period of running a securities market in Vietnam will no longer exist. It seems hard to imagine that we will find any new reasonable ground for state-owned stock exchanges at that stage. Even for the time being, the state-owned form of the current securities trading center has been questioned. If such form of ownership will continue to be taken by the planned stock exchanges, probably it will further trigger greater controversy. Of course the principal question is not that of a great or small controversy which might result from the state-owned stock exchanges. Rather the question is whether such legal form will generate expected outcomes or will promote an effective securities market. In defining an appropriate form for the exchange market, experience from other countries around the world should not be ignored.

One might argue that it is too early to judge the efficiency of the state-owned stock exchanges in Vietnam, especially when they have not yet come into existence; that each country has different socio-economic circumstances, so that what is best for other countries' stock exchanges, especially those in developed countries, is very unlikely to be best for those in Vietnam, a developing country; and that it is not always wise and right to directly import successful experience from overseas into the country, and so on.

In response to these arguments, first, it can be said that state-owned entities, regardless of where they may be, often reveal a number of weaknesses and deficiencies in their operation. For this reason, state enterprises have been privatized everywhere around

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[483] See Tran Cao Nguyen (et al), "So giao dich chung khoan Viet nam: Mo hinh to chuc, quan ly va giam sat" [Vietnam Stock Exchanges: Organization, Management, and Supervision], (*Working Paper No. CK-99.03*, *SSC*, 1999) 11, 48-49. Arguments for state-owned structure of future stock exchanges include: to maintain public investors' confidence, to ensure that the future stock exchanges are well financed so that they can be equipped with modern facilities, to minimize errors when transactions are effected, and to assure that the stock market is healthy and effective.

The preceding section provides arguments against these arguments.

the world, as earlier mentioned. Vietnam has also experienced inefficient or loss-making state enterprises for decades.[484] This fact has prompted the Vietnamese Government to initiate the state enterprises equitization process since the early 1990s.[485] And why should state-owned exchanges be an exception?

Secondly, to date, the world-wide demutualization or the global conversion of mutual stock exchanges to private ones seems to be another factor that confirms the rightness of such a new movement, which is, in a way, similar to what has happened with state enterprises. In the words of Caroline Bradley '*[t]he move to private ownership of these exchanges*[486] *is comparable to the movement to privatize state owned enterprises generally.*'[487]

Thirdly, as pointed out in the first chapter of this work, one of the goals of the Vietnamese government in establishing the securities market is to create a potential channel for capital flow into the country from overseas. This goal can only be materialized if the market is attractive to foreign investors in terms of its prestige. Principal factors that contribute to good reputation or the attractiveness of a stock exchange include fairness, transparency, market compatibility, and good capability in providing services or financing technological advances (the latter is of importance in allowing an exchange to compete with others in terms of trading volume, liquidity, and selling services and data).

A fair and transparent market: to achieve such a market, the completion of the information disclosure regime, anti-fraud provisions, and the regulation of market professionals is vital. These issues have been discussed earlier in this paper. The following discussion will focus on the two factors: market compatibility and financing technological advances.

Market compatibility: the previous discussion shows that nowadays the state-owned form of stock markets is rarely employed by countries around the world. Obviously, foreign investors, who have been used to dealing with non-government owned stock exchanges for centuries, will not easily get familiar with a state-owned stock exchange. Once they have to make a choice between a marketplace that is familiar to them (or of which they at least have a relatively full image) and another which is not, then for the sake of their investments, they tend to choose the former, except for some more venturesome investors.

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[484] It is reported that:

"[U]p to 60% of SOEs constantly record losses and ask for subsidies from the State. Vietnam now has 5,655 SOEs. Sixty percent have an average capital of VND5 billion ($333,333) or less, and 30% have an average capital of VND30 billion ($2 million) or more.

Forty three percent of machinery in SOEs has operated for ten years or more, and 44.7% has run for five years or less. SOE debts in the 1991 - 2000 period amounted to VND277.8 trillion ($18.5 billion)."

For more information, see "State Owned Enterprises: Govt Determined to Push up SOEs Reform" http://www.vietnampanorama.com/business/soes.html, visited May 4, 2002.

[485] For concrete legal bases of equitization program, see Section II, Sub-section 2, Chapter I of this paper.

[486] Here, Caroline Bradley uses the term "these exchanges" to denote exchanges in different jurisdictions (author added).

[487] See Caroline Bradley, above n. 413, 661.

Technological advances employed by the market: to date many stock exchanges around the world have privatized or reformed themselves into for-profit organizations with diverse ownership. With such a global tendency, the coming years will witness a continuously increasing number of demutualized stock exchanges from country to country. As earlier mentioned, technological development itself has driven the transformation of stock exchanges into a shareholder-owned form to enable them to finance technological advances so that they can computerize all trading services. It is even predicted that technology and telecommunication companies may own or be owned by some stock exchanges in years to come; and that exchanges will compete not only in trading volume and liquidity but also in selling services and data.[488] Such developments in the securities industry permits an investor in Japan, for example, to access all necessary information on a company in the US, and vices versa, without difficulty and to route an order to buy its shares, at a click on a computer key board. If Vietnam cannot offer cross border transactions in such a simple and time-saving manner, then the country will lose a great population of foreign investors. Even if the government can afford to computerize the trading services offered by the future Vietnamese stock exchange, it will still be a real burden for the state budget to cover such a financial demand, while instead it could rely on the public to provide such finance.

These analyses reveal that the state-owned form of stock exchanges would put Vietnam in a disadvantageous position since it might cause foreign investors to refrain/abstain from investing in the market, while it would add to the state budget deficit, or make the deficit more severe. Apparently, to avoid such disadvantages that might face Vietnam, stock exchanges as departmental units of the SSC cannot accomplish the tasks.

III. A DESIRABLE MODEL FOR FUTURE EXCHANGE MARKETS

The previous discussion shows that the state-owned form of the current securities trading centers and of the planned stock exchanges in Vietnam cannot promote the achievement of an effective market.

The discussion also reveals that the mutual form of exchange market has a long history, but recently its weaknesses have been exposed. These deficiencies have become increasingly obvious when the securities industry enters a new era of high technology and intense competition. This fact makes mutual stock exchanges no longer suitable for today's securities industry. For that reason, the whole world has experienced an increasing tendency in privatizing stock exchanges in the last decade. It is submitted that Vietnam should learn from such experience so that it can save both time and money in achieving an ideal form for the current securities trading centers and the planned stock exchanges: that is, to adopt a corporate structure of stock exchanges, or in other words, to legalize a shareholding company form of stock exchanges. The current securities trading center should now be privatized. As long as the government finds it necessary to interfere

[488] See Laura Cha, above n. 425.

in the governance of the trading center, the government should remain a controlling shareholder of the center after the privatization. In that way, the ownership of the center will be diversified, which, in turn, will generate a new and more effective form of governance for the center, while the state, when necessary, can still have influence on the center's decisions as a large shareholder. The corporate form of exchange market should continue to be taken by the planned stock exchanges when they come into existence.

Taking this approach does not imply that the privately owned structure of securities trading center/stock exchange (hereinafter, stock exchange) is perfect. Because the business carried out by stock exchanges differs from that carried out by other bodies corporate, further steps following privatization should be taken to prevent potential problems that might occur. The next and immediate step to be taken may be a statutory reform in the division of regulatory functions between stock exchanges and the public regulator, and in the exchange governance. The reform will avoid conflicts of interest between stock exchanges and their competitors, and will avert potential hostile takeovers and mergers amongst privatized exchanges.

Division of regulatory powers between stock exchanges and SSC: after being privatized, stock exchanges would have a new legal structure: a shareholder-owned one; each stock exchange would be governed by a board of directors; the board's members would be persons who have good reputation; the general shareholders' meeting would be the highest decision-making body of the exchange, and so on. It would be appropriate that the exchanges, after being formed by the SSC in conformity with the securities law, would also be subject to the *Enterprise Act*, as are other shareholding companies.

Furthermore, under the new legal form, stock exchanges would themselves be shareholding companies having their shares listed on their own trading floors and having outstanding shares held by the public. To avoid conflicts of interest that might occur when stock exchanges are in charge of enforcing listing standards and trading rules against themselves, the SSC should probably retain supervising power over the compliance of stock exchanges with such standards and rules.

Remedies to avoid takeover and merger: to avoid takeovers and mergers, there are at least two alternatives. The first is to adopt shareholding stock exchanges whose controlling block of shares is held by the government. In this way, the government could interfere in the governance of the exchanges as a major shareholder, when necessary. Secondly, to recognize shareholding stock exchanges whose shares are not held by the government at all. This approach can be dealt with in one of the two following directions: (1) to create some statutory limits on the holdings of a stock exchange's shareholder. This can avert the possibility of a person or a body corporate gaining control over the exchange and influencing its decision-making processes; and (2) to adopt some statutory requirements pursuant to which, if there would be any takeover or merger occurring among exchanges, such a takeover or merger would not be effected without approval from the government.

CHAPTER VI
WHETHER THE MARKET REGULATORY SYSTEM CAN ENSURE THAT THE SECURITIES REGULATION WILL BE WELL ENFORCED

The role of the management apparatus over the securities market cannot be denied, even when all other components of the securities regulation such as regulation of information disclosure, of anti-fraud, of securities professionals, and exchange market structure, are all completed. This is because, even when laws and regulation are perfect, in the absence of an effective regulatory system, nothing can ensure that such laws and regulation will be actually implemented in practice.

This chapter scrutinizes the current market regulatory system of Vietnam in relation to those in other jurisdictions. It argues that such a management apparatus has not been appropriately adopted, so that the system will not be able to ensure that the securities regulation will be well enforced.

I. SECURITIES REGULATORY SYSTEMS: A THEORETICAL ANALYSIS

1. Securities Regulatory Systems in General

Regulatory systems over securities markets are significant in enforcing securities laws, to protect the investing public and to control market risks. Each securities market is subject to one kind of regulatory system or another. As M.I. Steinberg put it, regardless of the sophistication of any particular securities market, there must be some form of regulation appropriate to the relevant market. The alternatives can range from (1) a central government regulator having extensive authority, or (2) government regulation by means of regional bodies, to (3) self-regulation conducted by stock exchanges or by other organizations, or (4) a combination of the above mentioned forms.[489]

The first and second form of regulation is actually governmental regulation or public regulation, so that the options can now be seen as three: public regulation, self-regulation, and a combination of both. All these forms have been adopted somewhere or other around the world. In the past self-regulation was primarily employed in many European countries[490] and none of the member states of the EU had a securities regulatory agency.[491] The UK, the Netherlands, Ireland[492] and Germany[493] are examples of countries

[489] See Marc I. Steinberg, above n. 7, 259.
[490] See Maria A. Volarich, "Easing the Regulation of a Pan-European Securities Market: Applying the Recommendations of the Rudman Report to EASDAQ", (1996) 19, *Fordham International Law Journal* 2230, 2250. Hereinafter, Maria A. Volarich.
[491] Ibid., at footnote n.160.
[492] See Roberta S. Karmel, "The Case for a European Securities Commission", (1999) 38 *Columbia Journal of Transnational Law* 9, 31. Hereinafter, Roberta Karmel (1999) 38.

that mainly employed self-regulation, and where government merely supported such regulatory apparatus. For example, in the UK, apart from the London Stock Exchange acting as a self-regulator, regulatory responsibilities were divided among some ministerial agencies such as the Bank of England, the Treasury, and the Department of Trade and Industry;[494] in Germany, no federal securities agency existed, but stock exchanges acted as self-regulators under the supervision of a state agency in their own jurisdiction.[495] In some other European countries such as France and Italy public regulation has been adopted.[496] A combination of public regulation and self-regulation has been in existence in countries such as Japan,[497] the US,[498] Canada[499] and Australia.[500]

Later, both the UK and Germany moved toward a regulatory system in which a combination of public regulation and self-regulation is employed. In the UK, after the passage of the *Financial Services Act* in 1986, a new regulatory structure has been adopted. In such a structure, the Securities and Investment Board (the SIB), a quasi-governmental body, is the highest body sharing regulatory functions with self-regulatory organizations. The SIB Director-General is responsible for rule-making, and for awarding and revoking licenses for securities firms, while SROs are entitled to draw up and oversee rules concerning business practices in their respective fields.[501]

The regulatory system of Germany has changed since 1994 after the enactment of the *Financial Markets Promotion Act*. The Act establishes the Federal Supervisory Office for Securities Dealing, which is in charge of overseeing German securities markets. The Office, the eight individual stock exchanges and the state governments compose the regulatory system of German securities market.[502]

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[493] See Maria A. Volarich, above n. 490, 2253.

[494] See Henry Laurence, "The Rule of Law in the Era of Globalisation: Spawning the SEC", (1999) 6 *Indiana Journal of Global Legal Studies* 647, 661. Hereinafter, Henry Laurence.

[495] See Maria A. Volarich, above n. 490, 2253.

[496] See Roberta Karmel (1999) 38, above n. 492, 31.

[497] See *Securities and Exchange Law of 1948* (2001 Japan): The Law seems to vest in the Prime Minister the power of a market watchdog (Arts. 4, 28, 68, 80, 186, and 194-6). But the Prime Minister can delegate such power to the Director General of the Financial Services Agency, which in turn has to delegate part of his/her power to the Securities and Exchange Surveillance Commission.

On the other hand, Article 87 treats securities exchanges as self-regulatory organizations. Under this Article, members of a securities exchange must comply with laws, regulations and the rules of the exchange; the exchange has the right to impose a fine on a member, to order a member to suspend or restrict the sale or purchase of a security in the exchange, and to revoke the trade qualification of a member who has violated laws, regulations or the rules.

[498] See Marianne K. Smythe, "Government Supervised Self-Regulation in The Securities Industry and the Anti-trust Laws: Suggestion for an Accommodation", (1984) 62, *North Carolina Law Review* 475, 483. Hereinafter Marianne K. Smythe.

[499] See Mark Gillen and Pittman Potter, "The Convergence of Securities Laws and Implications for Developing Securities Markets", (1998) 24 *North Carolina Journal of International Law & Commercial Regulation* 83, at footnote 14. The Canadian securities industry used to rely on the self-regulation by the stock exchanges before adopting public regulation.

[500] See Frank Donnan, above n. 412, 68.

[501] See Henry Laurence, above n. 494, 662 - 663.

[502] Ibid, 681.

2. Public regulation

The term "public regulation" can be construed as that regulation which is carried out by government through either a single central governmental agency or a system of central and local governmental authorities. In the latter case, coordination between central and local government in policing markets is adopted. Italy is an example, where public regulation has been loaded on to both a central governmental commission and local authorities.[503]

In countries where public regulation has been adopted in the form of a single public regulator, either with or without parallel self-regulators, a governmental authority in charge of enforcing securities law is often set up. Such a body can either be a dependent or an independent governmental agency. In the literature, the US market watchdog is often referred to as an independent agency,[504] while that of Japan is referred to as a dependent one.[505]

A dependent regulatory agency can be either a component of the government or part of a governmental ministry. It often oversees securities markets within powers delegated to it by the government or the ministry it belongs to.

An independent agency, in contrast, is a separate branch of government. According to A. L. Peter, it is the fourth branch of government, which although it is subject to the supervision or review of the other three branches, operates separately from them. Such a governmental body is vested with executive, judicial and legislative power to oversee a certain area of government interest.[506] The reasons why an independent agency is required to oversee securities markets will be clarified while discussing the experience of the US and Japan in running securities markets.

3. Self-regulatory system

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[503] See D. E. Ayling, *The Internationalization of Stockmarkets* (1986), 122. Hereinafter, D. E. Ayling.

[504] See A. L. Peters, "The Independence of Independent Agencies: Independent Agencies: A Government's Scourge or Salvation?", (1998) *Duke Law Journal* 286, 287. Hereinafter A. L. Peters.

See also Nicole J. Ramsay, "Japanese Securities Regulation: Problems of Enforcement", (1992) 60 *Fordham Law Review* 255, 281. Hereinafter, Nicole J. Ramsay.

See also Hal S. Scott, Philip A. Wellons, *International Finance: Transaction, Policy and Regulation* (6th Ed. 1999), 251.

[505] See Curtis J. Milhaupt, above n. 311, 472.

See also Nicole J. Ramsay, above n. 504, 269.

See also Gregory D. Ruback, "Master of Puppets: How Japan's Ministry of Finance Orchestrates its Own Reformation", (1998) 22, *Fordham International Law Journal* 185, 213 - 214. Hereinafter, Gregory D. Ruback.

[506] See A. L. Peters, above n. 504, 286.

"The term self-regulation", As A. J. Campbell puts it, "means different things to different people".[507] In the literature, a range of definitions can be found. The term can be understood as the regulation carried out by industry or professional groups rather than by the government.[508] It can mean regulation by a group of individuals or institutions realizing that regulation of its activities is required for the common interest of the whole group.[509] It can also refer to circumstances where the government has formally delegated the power to an industry to oversee the operation of the industry itself.[510]

To provide a closer image of self-regulation in relation to the securities industry, David Ratner's observation might be useful. While discussing the "self-regulation" of the US securities industry, David Ratner refers to the regulatory authority lodged in a number of private associations of broker-dealers, known as "self-regulatory organizations". Such associations have been delegated both powers and responsibilities by Congress, (a) to create and enforce rules for the conduct of their members and (b) to assure compliance with the federal securities laws by their members.[511]

In countries where a self-regulation system has been employed, whether in parallel with governmental (public) regulation or as a single system, different organizations under the form of stock exchanges or associations of securities dealers or of investment companies or investment trusts, lay down their own rules binding their members. Thus the term "self-regulatory organization" has been used.

a. Advantages of Self-regulation

In the history of the securities industry, the self-regulatory system is much older than the governmental regulatory system.[512] The former plays an important role in the securities industry and is said to have a number of advantages over the latter. Commentators generally agree on the following advantages: more efficiency, more flexibility, a higher level of compliance, and lower cost.[513]

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[507] See Angela J. Campbell, "Self-Regulation and the Media", (1999) 51 *Federal Communications Law Journal* 711, 714. Hereinafter, Angela J. Campbell.

[508] Ibid, 715.

[509] See Betty M. Ho, "Rethinking the System of Sanctions in the Corporate and Securities Law of Hong Kong", (1997) 42, *McGill Law Journal* 603, 627.

[510] See Angela J. Campbell, above n. 507, 714.

[511] See David Ratner (3rd Ed. 1986), above n. 256, 838.

[512] As earlier mentioned, in European countries, securities industries were initially overseen by self-regulatory systems. The same can be said about the regulatory system of the US securities markets. As David Ratner points out, *"[w]hen Congress created the SEC in 1934, stock exchanges as private associations, had been regulating their members for up to 140 years."* See David Ratner (3rd Ed. 1986), above n. 256, 838.

[513] See Angela J Campbell, above n. 507, 715 - 717; see also Margot Priest, "The Privatisation of Regulation: Five Models of Self-Regulation", (1997-98) 29, *Ottawa Law Review* 233, 269 – 270, hereinafter, Margot Priest; see also Frank Donnan, above n. 412, 61 – 64.

Aside from those, some other advantages of self-regulation are also mentioned in the literature e.g. political advantages and practical advantages. For more information, see Margot Priest, above n. 513, 268-269 and 271.

More efficiency: it is argued that technical knowledge is an essential requirement in developing tailored rules to regulate an industry, and that industry members often have better technical knowledge of the relevant subject compared to a government agency. Therefore directly using the industry's collective expertise to regulate the industry would be more efficient than reproducing such expertise at the governmental agency level.

More flexible: self-regulation is more flexible than governmental regulation. SROs can easily and quickly alter rules to adapt them to changing circumstances. Having superior knowledge of its own area, the industry will know better than a governmental agency when a rule should be changed to assure better compliance, and how the rule should be altered so that it will be more tailored to the particular industry. Of course a governmental agency can also modify rules but can only do so after obtaining necessary political support and consensus. Furthermore, the revision of rules by governmental agencies often has to follow specified administrative procedures. All such things are often very time consuming and can slow down the revision process.

Greater incentives for compliance: for psychological reasons, self-regulation provides greater incentives for compliance. It is often easier for industry participants to perceive rules that are developed by the industry itself than those adopted by the government. Furthermore, industry participants often better understand, and are more conscious of, the rationale and goals of regulation as well as the rules themselves, where these are developed by the industry.

Lower cost borne by the government: in employing a self-regulatory system, the government can reduce the cost of developing and enforcing rules since this burden will be transferred to the industry. Even where the government retains oversight functions over a self-regulatory system, such tasks still cost the government less than if it carried out the whole task itself.

b. Disadvantages of Self-regulation

Self-regulation, although it has numerous advantages, also has a number of disadvantages. These are: self-interest,[514] lack of an adequate enforcement, potential source of monopoly conduct,[515] and favoritism.[516]

A disadvantage frequently referred to by commentators is self-interest. It is sometimes doubted whether, with self-regulation, an industry can protect the public interest and avoid public harm. Although it might have greater expertise than the government, what assurance is there that this will be used for the public interest, that the industry will not put its own interest over the public interest? Critics are even concerned about the likelihood that the industry will turn regulatory goals into its own goals.

[514] See Angela J. Campbell, above n. 507, 717; see also Margot Priest, above n. 513, 271 - 272; see also Frank Donnan, above n. 412, 65.
[515] See Angela J. Campbell, above n. 507, 718 - 719.
[516] See Margot Priest, above n. 513, 272.

The adequacy of enforcement in self-regulation is also questioned since it is claimed, it is very unlikely that the industry has enough power to enforce adequate sanctions. Even when it has enough power, its willingness to impose vigorous self-enforcement is questionable.

Self-regulation even causes a concern that it might provide favorable condition for the existence of anti-competitive conduct. In self-regulatory industries, industry members and members of each SRO in the industry will have to reach agreement on the way to conduct their business. However, within the industry, members are also competitors. Having to agree on the way to conduct their business, they would no longer be competitors.

Another problem resulting from self-regulation is said to be favoritism. Self-regulation is carried out by SROs who are very likely to be dominated by larger or long-established firms. The regulatory policy thus might reflect the interests of such firms rather than those of either other industry members or of the public.

In the literature, a number of other disadvantages can be found.[517] And this fact seems to make it hard to decide whether self-regulation should be employed in regulating securities markets. As noted by Margot Priest, while discussing advantages and disadvantages of self-regulation, *'it is difficult to fully articulate the advantages and disadvantages of a self-regulatory system in the abstract.'*[518]

c. What Might Actually be the Strength and Weakness of Self-regulation?

One thing that can be seen from most of the above-mentioned criticisms of self-regulation, except for that on inadequate enforcement power, is that they actually stem from a common concern of whether the industry will act for its own benefit to the detriment of the public. For example, one might well argue that, if the securities industry cannot protect public investors, if it puts its own interests over public interests, then the public will surely refrain from investing in securities markets. Rather they will channel their investment into a safer sector, for example: banking. In such a circumstance, the securities industry itself cannot survive. The securities industry thus has to develop and well implement its self-regulatory rules to protect the public, and of course, also to help it survive; or at least to harmonize its own interests and those of the public. Even when such disadvantages do exist, there must be some appropriate statutory measures to nullify them. It should be the task of the lawmakers and legal researchers to find out such measures.

Perhaps the criticism that the self-regulatory system does not have adequate power in enforcing rules and regulations has reasonable grounds. No private organization seems

[517] Such disadvantages include under-regulation, over-regulation, narrow regulatory concerns, reduction of accountability and higher cost to the public. For further information, see Margot Priest, above n. 513, 273 - 274.
[518] Ibid, 275.

to hold such power adequately, even when it is provided by legislation. It appears that only the government is able to accomplish the enforcement task properly, since apart from having various ministerial agencies administering different areas, it has in its hands necessary forces such as courts, police and army. However, it is worth noting that whether or not the enforcement can be done properly by the government also depends on certain subjective and objective factors, such as the willingness and the independence of the relevant government agency. The questions whether a governmental agency wants to enforce, and whether it is able to enforce, thus arise. As long as these two questions have not been properly solved, the reality of law enforcement, even at governmental level, is also in doubt.

II. EMPLOYING AN ADEQUATE REGULATORY SYSTEM: THE EXPERIENCE OF THE US AND JAPAN

1. The US Securities Regulatory System

Initially, the regulation of the US securities markets was self-regulatory. Stock exchanges had been regulating their members' activities for more than 140 years until the passage of the 1934 *Securities Exchange Act*.[519] That Act, for the first time, has adopted a regulatory system where self-regulation by the securities industry and professional groups plays an important role under the oversight of the Securities and Exchange Commission (SEC).

The SEC, a body acting as a public regulator, is an independent agency[520] formed by Congress.[521] It might be useful to examine the legal structure of the SEC to clarify the notion of an independent regulatory agency.

The *Securities Exchange Act* of 1934 creates the SEC as a body composed of five commissioners appointed by the President, with a five-year term of service. Among the five commissioners, not more than three are to be members of the same political party. The commissioners cannot be dismissed by the Congress, they can only be fired by the President for good cause.[522] Such a structure, as A. L. Peters contends, creates a shield that can protect the commissioners from the vagaries of shifting political opinion.[523]

The *Securities Act* of 1933 empowers the SEC with all three powers: rule-making, executive and judicial, that are necessary for an agency to be independent. Rule-making powers of the SEC are prescribed in Section 19(a), the *Securities Act*. It reads:

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[519] See David L. Ratner (3rd Ed 1986), above n. 256, 838.
[520] In the literature, the US SEC is often referred to as an independent agency. For further information, see A. L. Peters, above n. 504, 286, 287; see also Nicole J. Ramsay, above n. 504, 281; see also Hal S. Scott, Philip A. Wellons, above n. 504, 251.
[521] See *Securities Exchange Act of 1934* s 4, 15 USC 78d (2002).
[522] Ibid.
[523] See A. L. Peters, above n. 504, 287.

> *The Commission shall have authority from time to time to make, amend, and rescind such rules and regulations as may be necessary to carry out the provisions of this title, including rules and regulations governing registration statements and prospectuses for various classes of securities and issuers, and defining accounting, technical and trade terms used in this title.*

The SEC further can issue rules and regulations pursuant to which a class of securities can be added to securities that are exempted from registration.[524]

Executive powers of the SEC can be found in Section 19 (b), the *Securities Act of 1933*. It reads:

> *For the purpose of all investigations which, in the opinion of the Commission, are necessary and proper for the enforcement of this title, any member of the Commission or any officer or officers designated by it are empowered to administer oaths and affirmation, subpoena witnesses and the production of such documentary evidence may be required from any place in the United States or any Territory at any designated place of hearing.*

The SEC can even institute disciplinary proceedings to censure, suspend or revoke the registration of any broker or dealer where such measures are necessary in the public interest.[525] The SEC is also vested with hearing power where necessary:

> *All hearings shall be public and may be held before the Commission or an officer or officers of the Commission designated by it, and appropriate records thereof shall be kept.*[526]

Although the independence of the SEC is laid down in the *Securities Act* of 1933, such independence is not always absolute and can be affected by the administrative and legislative branches of the government under the *Securities Exchange Act* of 1934. That is because both the Congress and the President might have significant influence on the SEC. Congress, although it cannot remove the SEC's commissioners in the ordinary course, the Senate or the House of Representatives can do so through a trial or through the drastic method of impeachment, respectively. The influence of the President derives from his/her power in appointing the SEC's chairman and other commissioners.[527]

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[524] See *Securities Act of 1933* s 3 (b) & (c), 15 USC s 77c (2002).
[525] See *Securities Exchange Act of 1934* s 15 (b) (4), 15 USC s 78*o* (2002).
[526] Section 21, *Securities Act of 1933* s 21, 15 USC s 77u (2002).
[527] See A.L. Peters, above n. 504, 286 – 288.

The independence of the SEC nevertheless, is said to be extremely important in effectively implementing the statutory scheme.[528] According to A.L. Peters, the necessity of such independence stems from the SEC's tasks to protect public investors and to ensure a fair and integrated market. A.L. Peters argues that statutes governing primary and secondary securities markets as well as the business activities of financial intermediaries are so complex that they require a regulator with special technical knowledge and expertise to ensure the effectiveness of the market regulation. And only independent agencies can provide such a high degree of technical expertise that enables them to administer those complex statutes. Therefore the SEC's independence is of significance.

In addition, the need to segregate securities regulation from the vagaries of the political process is stressed by Congress. As such, the regulation of the American securities markets carried out by a system consisting of self-regulatory organizations and an independent SEC seems to be ideal. In such a system, self-regulatory organizations operate under the oversight of the SEC, and cooperate with the SEC to accomplish the SEC's tasks.

A.L. Peters goes on to say that another justification for the SEC's independence is that such independence is required to enable it, as a law enforcement agency, to investigate and prosecute high-ranking persons that commit fraud in securities markets. In so-doing, the Commission need not get permission from both the executive and legislative branches of the government, nor is it governed by these two organs.[529] One might argue that as for a trial of powerful and high ranking persons, judicial independence is enough. Perhaps this is true, but in some specific areas such as commerce and finance that are vital to the strength of an economy, only the regulatory agencies have enough technical expertise to detect fraud. To save time and speed up enforcement proceedings, which in turn, can quickly prevent further damage to the public, the independence of these agencies is required. Such independence should ensure that investigating and prosecuting procedures are consummated in the shortest time without interference by other governmental branches. This is especially important where high ranking persons are involved. Such independence should also enable the regulatory agencies to marshal necessary evidence quickly so that legal action can promptly be taken in the courts.

Finally A.L. Peters contends that the best justification for the SEC's independence from either political or economic interference stems from the nature of the securities markets. In the US markets, the collective judgments of a vast number of investors from institutional to individual are reflected, and the use of regulatory means that rely on a particular political ideology and aim at achieving certain economic effects cannot succeed. A sound regulatory means must thus ensure that the markets are free and fair. To achieve such means, the market regulator must strike a balance between employing regulatory constraints needed to ensure the markets' fairness and integrity and assuring

[528] Ibid, 291 - 293.
[529] Ibid, 291.

reasonable freedom in such markets. According to A.L. Peters, an independent SEC can maximally attain such a balance.[530]

An independent regulatory agency, although it can benefit the regulated industry, might also be a source of potential problems, especially in connection with the resolution of inter-agency disputes. According to A. L. Peters, that is because the government cannot simply choose one course of action over another in mediating disagreements between independent agencies. Sometimes legislation or judicial action may be required to effect the compromise agreements between independent agencies even though such agreements result from their own negotiations.[531] Nevertheless, it can be said that benefits generated by the independence of a regulatory agency are still overweight compared with the problems that might result from such independence. That can be well proven by the long term existence of an independent SEC in the US. The American SEC has now almost reached its 70th year of age despite criticism of its governmental over-regulation[532] and even of its existence.[533]

2. Japan's Securities Regulatory System: Past and Present

Japan, in contrast to the US, is a country where the public regulator over securities markets is not independent from the government. Japan has gone through consecutive reforms of the public regulation system overseeing securities markets. Initially an independent agency modeled after the SEC of the US, the Japan Securities and Exchange Commission was established in May 1948. In 1952, the Commission was consolidated into the Financial Management Bureau, which belonged to the Ministry of Finance. Since the role of the securities market in Japan had been increasingly important in the national economy, a separate bureau had become much in demand. As a result, in June 1964, the Securities Bureau was set up.[534]

The Securities Bureau is one of the seven internal units of the Ministry of Finance - the actual regulator of Japan’s securities markets. Since its birth, the Bureau assists the Ministry of Finance by carrying out supervisory and administrative activities over the securities industry. Its functions are similar to those of the US Securities and Exchange Commission, although it is not an independent regulatory agency. Such functions include (1) licensing for stock exchanges, for securities firms and for securities investment trusts; (2) supervising these exchanges and entities, as well as their business associations; (3)

[530] Ibid, 292 - 293.
[531] Ibid, 288 - 289.
[532] See Thomas Lee Hazen, above n. 301, 10.
[533] See Jonathan R. Macey, “Administrative Agency Obsolescence and Interest Group Formation: A Case Study of the SEC at Sixty”, (1994) 15 *Cardozo Law Review* 909, 921 - 925, 933 - 936. In this article, the author does not specifically criticize the independence of the SEC. Rather he criticizes the SEC's obsolescence when the US securities industry has undergone various changes. He maintains that the existence of the SEC is no longer required in such circumstances.
[534] See Japan Securities Research Institute, above n. 398, 278 - 279.

examining the securities registration; (4) establishing corporate accounting standards; (5) supervising public accountants and auditing corporations.[535]

The Securities and Exchange Council is another important assistant of the Ministry of Finance. The Council, established in August 1952, acts as an advisory body. It studies problems concerning the issuance, trading and other securities transactions that arise in the securities markets and then recommends necessary measures to the Ministry of Finance.[536]

Such a public regulatory system overseeing Japanese securities markets did not generate expected outcomes. A number of problems concerning market manipulation, fraud and unfair trading frequently occurred. It was claimed that most of the problems stemmed from the failures of the Ministry of Finance in enforcing securities law.[537] For this reason, a number of proposals were made to reform the public regulatory system in Japan.[538] The reform, at last, resulted in the birth of the Securities and Exchange Surveillance Commission (SESC) in July 20, 1992, a watchdog agency independent from the securities market regulators.[539] It is necessary to emphasize that the Ministry of Finance is allowed to carry out the same tasks as those of the SESC. Consequently, the SESC has to observe what the Ministry has done in order to avoid overlaps.[540] Because of this fact, it is hard to say that the SESC is entirely independent from the Ministry of Finance.

The SESC is an external bureau of the Ministry of Finance, headed by a chairman who is, in turn, assisted by two commissioners. All are appointed by the Finance Minister with the approval of both Houses of the Diet.[541] Their term of service is three years and they can only be removed from office for extraordinary reasons. The operational goals of the Commission are to ensure the fairness and integrity of the securities market and to protect investors. With such aims, the SESC is delegated powers by the Ministry of Finance such as (1) criminal investigations of irregularities; (2) inspection and monitoring of securities trading including securities transactions engaged in by Japanese banks.[542] The SESC, however, does not have power to take enforcement action on its own initiative. Where evidence of violation of either the securities law or regulations is found, the SESC cannot prosecute criminal offences, nor can it impose administrative sanctions. The SESC, in such a case, will have to make a formal accusation to the Public Prosecutors Office or recommend administrative sanctions to the Minister of Finance. The

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[535] See Nicole J. Ramsay, above n. 504, 268.
[536] See Japan Securities Research Institute, above n. 398, 281 - 282.
[537] See Nicole J. Ramsay, above n. 504, 271.
[538] Ibid, 281.
[539] See Japan Securities Research Institute, above n. 398, 284; see also Curtis J. Milhaupt, above n. 311, 468 - 471.
[540] See Gregory D. Ruback, above n. 505, 212.
[541] See *Ministry of Finance Establishment Law* (Japan) Art. 10.1 & 11.1.
[542] See Japan Securities Research Institute, above n. 398, 285 - 287; see also Curtis Milhaupt, above n. 311, 470.

Japanese banks have increasingly been involved in securities business recently. For further information, see Section II, Sub-section 2, Chapter IV of this paper.

Minister of Finance, pursuant to the law, must respect the recommendations of the SESC, although the Minister does not have to act on them.[543]

Curtis Milhaupt, in examining the roles of the SESC, points out some weaknesses of the SESC that result from its legal structure. First, the SESC does not only lack enforcement capability where violations are found, but also lacks administrative powers. Secondly, the SESC does not have authority to act as a rule-maker and administrative adjudicator. Milhaupt then concludes that the SESC does not have enough independence in acting as a market oversight agency. He further contends that the success of securities regulatory reform in Japan greatly depends on whether or not the SESC's independence is sufficient. Such independence is of importance since it can enable the agency to accomplish its tasks as a watchdog over securities markets.[544]

The recently revised version of the *Securities and Exchange Law* of Japan seems to lay down an even more complex system of public regulators over securities markets. Public issuing can only be made after the issuer has filed a registration with the Prime Minister.[545] Persons who seek to engage in securities business also file registration with the Prime Minister.[546] The Prime Minister is also responsible for granting the authorization on which a securities dealers association can be founded;[547] and for granting a license on which a securities exchange can be set up.[548] This provision gives the impression that the Japanese Prime Minister is functioning as a single market watchdog over Japanese securities markets. However, if one scrutinizes relevant articles embodied in the Law, one will note that the Prime Minister is not acting on his/her own but in many cases can delegate powers to another person such as the Director General of the Financial Services Agency who, in turn, can delegate the delegated powers to the SESC.[549] The SESC has become a component of the Financial Service Agency since June 1998.[550] The involvement of the Ministry of Finance beside the Prime Minister can also be seen in the interrogation process conducted pursuant to the *Securities and Exchange Law*.[551]

III. THE CURRENT VIETNAMESE REGULATORY SYSTEM: A DEPENDENT PUBLIC REGULATOR ACTING IN THE ABSENCE OF AN IMPORTANT SELF-REGULATORY SYSTEM

[543] Ibid (Curtis Milhaupt), 471.
[544] Ibid, 474 - 475.
[545] See Art. 4.
[546] See Arts. 28-2, 28-3 & 28-4.
[547] See Arts. 68 & 70.
[548] See Arts. 80, 82 & 83.
[549] See Art. 194 - 6.
[550] See "*Securities and Exchange Surveillance Commission: History and Functions*", http://www.fsa.go.jp/sesc/english/aboutsesc/aboutsesc01.htm, visited Sep. 13, 2001.
[551] See *Securities and Exchange Law of 1948* (2001 Japan), Art. 186.

1. The Absence of an Important Self-Regulatory System

For the time being, Vietnam has only one securities trading center. It is located in Ho Chi Minh City. The duties and rights of the center (and eventually of the stock exchanges) include:

1. *Organizing, managing and handling the purchase and sale of securities;*
2. *Managing and handing the system of securities transactions;*
3. *Providing services that support the purchase, sale and custody of securities;*
4. *Registering securities;*
5. *Providing clearing settlement for securities transactions;*
6. *Disclosing information concerning securities transactions;*
7. *Inspecting and policing securities transactions;*
8. *Collecting listing fees, membership fees, transaction fees, information disclosure fees and other service fees as provided by laws;*
9. *Implementing the reporting, statistical, accounting and auditing regimes in conformity with State regulations.*[552]

Although having a number of rights and duties of a management nature, the center can hardly be deemed a self-regulatory organization. This is due to its legal structure, as discussed in Chapter IV of this work.

Other self-regulatory organizations such as a securities dealers association or a securities investment funds association are not yet available. The former seems to be not feasibly, since to date, a legal basis for the operation of an OTC market has not yet been introduced in Vietnam. The latter perhaps shares the same fate with the former since securities investment funds have not yet come into existence in Vietnam.

As a self-regulatory system has been absent in the Vietnam securities industry, all securities regulatory powers are thus vested in the SSC.

2. The SSC: Lack of Independence and being Inadequately Empowered

a. The SSC Structure and Personnel

[552] See *Decree 48/1998*, Art. 24.

Decree 75/CP established the SSC in 1996,[553] but the Commission formally came into existence on April 1, 1997.[554] *Decree 75/CP* was rather simply designed, with only 6 articles, which lay down the whole legal structure as well as the functions, rights and duties of the SSC.

The SSC is a governmental agency whose functions include organizing and administering securities and securities markets.[555] The SSC has legal personality. Its operating expenses are funded by the state budget. Its functions include organizing and managing securities and securities markets.

In contrast to the US securities laws stating that the SEC is an independent agency, not part of the president's cabinet and specifying the number of commissioners and their terms,[556] *Decree 75/CP*, while expressly saying that the SSC belongs to the government, does not specify a fixed number of SSC members nor does it have any article providing the members' terms of service. It merely says that the SSC consists of a president, vice presidents and other commissioners being deputy ministers of different ministries such as the Ministry of Finance, Ministry of Justice, Ministry of Planning and Investment and the State Bank of Vietnam. The president and vice presidents are appointed and dismissed by the Prime Minister. Other commissioners are recommended by the relevant ministries and the State Bank of Vietnam, also to be decided by the Prime Minister.[557]

A notable point here is that all the commissioners of the SSC are working on a part-time basis since at the same time they hold other positions in the said ministries. Regulating securities markets is complicated and burdensome work. With such a dual-function, it is hard for them to accomplish their tasks adequately. In the US, the commissioners of the SEC, under the law, cannot hold another position in any other office. Pursuant to the *Exchange Act*:

> *・・・No commissioner shall engage in any other business, vocation, or employment than that of serving as commissioner, nor shall any commissioner participate, directly or indirectly, in any stock-market operations or transactions of a character subject to regulation by the Commission pursuant to this title・・・*[558]

This provision was clearly designed to ensure that the commissioners devote their whole time and expertise to their job.

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[553] On November 28, 1996, the Vietnamese Government signed *Decree 75-CP* to establish the State Securities Commission.

[554] See State Securities Commission, *"Noi dung bai giang khoa dao tao ve Chung khoan va Thi truong chung khoan" [The Contents of Lectures Delivered at a Training Session on Securities and Securities Markets]* conducted from July 27 to August 15, 1998 (This training course was held by the Chinese Hong Kong Institute and the State Securities Commission), 196.

[555] See *Decree 75/CP*, Art. 1.

[556] See *Securities Exchange Act of 1934* s 4, 15 USC 78d.

[557] See *Decree 75/CP*, Art. 1 and 3.

[558] See *Securities Exchange Act of 1934* s 4 (a), 15 USC 78d (2002).

b. The SSC Powers

Article 2, *Decree 75/CP* contains 12 sub-articles spelling out the powers and duties of the SSC. Such powers and duties can be classified into two groups: rule-making and administrative powers.

b.1. Rule-making powers

Rule-making powers can be found in Sub-articles 1 and 7 of Article 2, under which the SSC is in charge of:

> *Drafting legal rules on securities and securities markets to submit to the competent authority for consideration and approval; organizing and guiding the implementation of such approved legal documents.*
>
> *Issuing rules concerning listing, issuing announcements and other information about securities transactions, purchase and sale; cooperating with the Ministry of Finance in establishing fees and costs concerning the issuance and trading of securities.*

To date the SSC has showed its effort in the rule-making area by issuing voluminous documents within its powers, under the form of decisions and circulars. These rules range from those governing securities trading centers and securities firms to others regulating public issuance and securities transactions on secondary markets. A number of such rules have been revised, even several times.

b.2. Administrative Powers

Administrative powers allow the SSC to act as a public regulatory agency over securities markets. The SSC is responsible for granting securities business licenses, suspending and revoking such licenses where necessary, and granting securities issuing licenses to those who desire to go public for fund raising. Such powers are laid down in Sub-article 3, which reads:

> *Granting, suspending and revoking securities business licenses with respect to securities firms, securities advising companies, securities investment funds, fund management companies and other organizations that are eligible to issue securities on the securities market.*

b.2.1. Securities Business Licensing

The SSC's power to confer a business license on those who seek to carry out securities business seems unnecessary and goes against the freedom of doing business entrenched in the 1992 *Constitution*.[559] Usually, in other countries, those who seek to do securities business merely file registration documents with the relevant government authority.

In Japan, a switch between registering and licensing systems has been made several times. After the Second World War, Japan adopted a registration system for securities companies.[560] The 1965 Amendment of the *Securities and Exchange Law* replaced that system with a licensing one.[561] At that time, the Ministry of Finance was in charge of granting business licenses for securities companies.[562] By this licensing system, the lawmakers hoped that unqualified broker-dealers would be excluded and the Finance Ministry would be more powerful in administering securities firms.[563]

The revision of the Japan *Securities and Exchange Law* in 1998, however, went back to a simple procedure of registration applied to those who desire to do securities business.[564] Under the recent revision of the Law (in 2001), this registering system has remained intact.[565] Corporations that desire to engage in securities business have to file with the Prime Minister an application containing specified statements for registration. Such an application must be accompanied by certain documents as provided for by the law.[566] Where the application does not fall into the specified items that can be deemed as "Rejection of Registration",[567] the Prime Minister makes the securities company register available for public inspection.[568]

A similar simple procedure to that of Japan can be seen in the US, where those who are seeking to act as a broker or dealer are merely required to file with the SEC an application for registration.[569] This should be taken into account while revising the securities regulation of Vietnam.

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[559] Article 57 of the *Constitution* vests the freedom of doing business in Vietnamese citizens.
[560] See Louis Loss *et al* (eds), above n. 261, 90.
[561] Ibid, 91; see also Japan Securities Research Institute, above n. 398, 18.
[562] See Louis Loss *et al* (eds), above n. 261, 91.
[563] Ibid.
[564] See *Securities and Exchange Law of 1948* (1998 Japan), Art. 28. This article reads: "*No person other than a joint stock company registered with the Prime Minister shall engage in the securities business.*"
[565] See *Securities and Exchange Law of 1948* (2001 Japan), Art. 28. The new Article 28, although it keeps the registering system intact, is slightly altered in that it is no longer confined those who seek to do securities business within join stock companies. This Article reads: *"No person shall engage in securities business except for a corporation that has registration therefore made by the Prime Minister."*
[566] Ibid, Art. 28-2.
[567] Ibid, Art. 28-4.
[568] Ibid., Art. 28-3.
[569] See *Securities Exchange Act of 1934* s 15 (b), 15 USC s 78*o* (2002). Section 15(b) (1) reads: *"A broker or dealer may be registered by filing with the Commission an application for registration in such form and containing such information and documents concerning such broker or dealer and any persons associated with such broker or dealer as the Commission, by rule, may prescribe as necessary or appropriate in the public interest or for the protection of investors・・・"*

b.2.2. Public Offering Licensing

The Vietnam SSC even has a discretionary power in granting securities issuing licenses under *Decree 48/1998*. Depending on which kind of securities will be issued, the issuer has to file different documentation with the SSC. Article 9, *Decree 48/1998* gives two separate lists of documents to be included in the application for the issuance of shares and bonds.[570] Within 45 days from the date of receipt of the application, the SSC must grant or refuse to grant the issuing license to the applicant. When refusing to grant the license, the SSC has to issue a letter of explanation to the applicant.[571]

China used to adopt a similar approach to that of Vietnam before the passage of the *Securities Law of the People's Republic of China*. By such an approach, there were requirements of issuing approval procedures and qualifications imposed on those who sought to make a public offering of either stocks or bonds. The future issuers had to go through certain specified processes such as filing application documents, being examined by the state authority, and obtaining an approval from such an authority. These provisions were said to reflect one of the "aspects of excessive government control" under the *Interim Regulations* in China.[572]

The new *Securities Law of the People's Republic of China*, passed in December 1998, however, has in part eliminated the above-mentioned difficulties. Nowadays, those who seek to initiate public issuance of shares are no longer required to obtain the approval of the market watchdog. Rather they are required to have their application verified by the state authority overseeing the securities market. The current regulation reads:

> *Public offers of shares shall, in compliance with the conditions provided for in the Company Law, be reported to the securities regulatory authority under the State Council for verification. The issuer shall submit to the said authority the application documents prescribed in the Company Law and the relevant documents specified by the authority.*[573]

It is interesting that the public issuance of bonds still seems to overcome strict control of the government. The Law further says:

> *The issuing of corporate bonds shall, in compliance with the conditions provided for in the Company Law, be reported to the department authorized by the State Council for examination and approval. The issuer shall submit to the department authorized by the State Council the application documents prescribed in the*

[570] These lists were mentioned in Section I, Sub-section 1, Chapter II of this paper.
[571] See *Decree 48/1998*, Art. 11.
[572] See Jay Zhe Zhang, above n. 257, 625.
[573] See *Securities Law of the People's Republic of China 1998*, Art. 11, first paragraph.

> *Company Law and the relevant document specified by the said department.*[574]

The new *Securities Law of the People's Republic of China* more or less shows an improvement, while Vietnam seems to have stepped in the same direction China did in the past. The statutory discretionary power of the Vietnamese SSC might cause some fears to the public as to whether the SSC decision would be very likely to have been affected by its own interests. This can be contrasted with the simple procedure of filing a registration statement to the government authority adopted in many countries around the world, including the US and Japan. The US is an example where the issuers do not have to get an issuing license from the SEC. They merely file a registration statement with the SEC[575] and disclose specified information[576] to the public in a detailed prospectus.[577] The registration statement will automatically become effective within 20 days after the filing date.[578]

b.2.3. Powers over Securities Trading Centers/Stock Exchanges

Administrative powers also put the SSC in charge of establishing and dissolving stock exchanges; and inspecting and supervising the operation of stock exchanges and other entities issuing securities or having engaged in securities business. Article 2 Sub-articles 5 and 6, *Decree 75/CP* gives legal bases for such authority. It reads:

> *Reporting to the government for decision-making concerning the establishment, suspension or dissolution of stock exchanges.*
> *Inspecting and overseeing the activities of stock exchanges and other relevant organizations which engage in securities issuance and trading and other securities services.*

While expressly saying that the SSC can inspect activities engaged in by stock exchanges and other organizations, Article 2 keeps silent on the SSC's ability to impose administrative disciplinary sanctions on those who are subject to the licensing authority. It does not say whether or not the SSC has subpoena and enforcement power either, or whether or not it can directly perform prosecutorial functions. Article 2.10 merely says that the Commission can:

> *Act on its own initiative and cooperate with relevant governmental branches in applying necessary measures to ensure that the*

[574] Ibid, second paragraph.
[575] See *Securities Act of 1933* s 6, 15 USC s77f (2002).
[576] Ibid, s 7, 15 USC s 77g.
[577] Ibid, s 10, 15 USC s 77j.
[578] Ibid, s 8 (a). 15 USC s 77h.

> *operation of securities markets is effective and in accordance with the laws.*

Clearly, this provision does not tell which activities the SSC can do on its own initiative and which should be done in coordination with other governmental agencies. The term "necessary measures" should be explicitly explained here.

b.2.4. Sanctioning Powers

The SSC powers in imposing administrative sanctions, however, are provided for in Article 15, *Decree 22/2000*. According to this article, there are two governmental agencies in charge of imposing administrative sanctions: the Inspection Department of the SSC and the Provincial People's Committees. The chief inspector and other inspectors of the said Department can act on behalf of the SSC. Administrative sanctions include warning sanctions; fines; and revocation of licenses (including issuing licenses held by issuers, securities business licenses held by securities firms, and practicing licenses held by securities trading staff working in securities firms). Administrative sanctions also extend to some other measures such as confiscating all amounts earned by the violators; and making the violators restore the safety ratio (to meet the initial stage or the statutory requirement), revoking or correcting misinformation, and compensating damages.

Article 18, *Decree 22/2000* further says that the violators must implement such sanctions imposed by the persons in charge. Should the sanctions not be implemented, enforcement will be carried out in conformity with Article 55, *Ordinance on Administrative Violations Settlement*. Sub-article 2 of this Article say that persons who have power to impose administrative sanctions also have power to enforce the implementation of such sanctions. This means that the SSC does have enforcement powers. Although the SSC powers are not as broad as those of the US SEC, they are broader than those of the Japan SESC, since it can impose administrative sanctions and it has enforcement capability where violations are detected and sanctions are defined.

b.2.5. Mediating Powers

An interesting provision, that cannot be found in either the US or Japan securities laws, concerns the dispute reconciliation powers of the SSC. *Decree 75/CP* does not say that the SSC has such powers but, they are provided for in Article 79, *Decree 48/1998*. This article allows the SSC to act as a mediator to settle disputes concerning the issuance and trade of securities and other securities transactions. This article reads:

> *Disputes arising in securities issuance and trading and securities transactions must first be handled by negotiation and reconciliation. Securities Trading Centers, Stock Exchanges, or the State Securities Commission can act as a mediator in such disputes.*

However, in solving disputes, the SSC powers are merely confined to reconciling. The SSC cannot hold an administrative hearing to determine the violation of the securities regulations.[579] Such a procedure can only be done at a court of law. Article 79 says:

> *If the reconciliation is not successful, parties to the dispute can bring the dispute to an economic arbitration or to a court to be settled in accordance with the laws.*

b.2.6. Other Administrative Powers

The SSC administrative powers also allow the SSC to develop and promote securities markets as well as to ensure that the markets operate effectively and lawfully. To achieve such goals, the SSC is empowered to act as follows:

> *Acting on its own initiative and cooperating with other relevant ministries and governmental branches in establishing and developing securities markets in Vietnam.*[580]
> *Establishing and administering organizations which provide services and assistance in securities markets.*[581]
> *Training market managers, securities dealers and strengthening their special expertise.*[582]
>
> *Cooperating with international organizations and countries in developing securities markets.*[583]

In addition, the SSC is responsible for managing its premises and personnel in conformity with the government's provisions. It also carries out other tasks as assigned by the government.[584]

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[579] In the US, the SEC has an entitlement to bring an action in a court of law to enjoin violation of securities laws. The *Securities Exchange Act of 1934* says: "・・・*it may in its discretion bring an action in the proper district court of the United States, the United States District Court for the District of Columbia, or the United States courts of any territory or other place subject to the jurisdiction of the United States, to enjoin such acts or practices, and upon a proper showing a permanent or temporary injunction or restraining order shall be granted without bond*・・・". [See *Securities Exchange Act of 1934* s 21 (d) (1), 15 USC s 78u (2002)].

The SEC can also order an administrative hearing against persons and firms registered with it, to define liabilities of the violator and to impose sanctions [see *Securities Exchange Act of 1934* ss 21B & 21C, 15 USC ss 78u-2, 78u-3 (2002)].

[580] See *Decree 75-CP*, Art. 2: Sub-Art. 2.

[581] Ibid, Sub-Art. 4.

[582] Ibid, Sub-Art. 8.

[583] Ibid, Sub-Art: 9.

[584] Ibid, Sub-Arts: 11 - 12.

Some Remarks

By adopting these provisions, it is very likely that Vietnam will undergo the same experience as Japan did before reforming its Ministry of Finance in response to the scandals. That is, having a governmental agency with a dual role: acting as a promoter and regulator of the securities industry at the same time.[585] This situation in Japan has been criticized since it gives rise to potential conflict of interest where an agency acts as both protector and overseer of securities regulation.[586]

Another similarity between the Vietnam SSC and the Japan SESC is that both lack authority to prosecute criminal offenses. All these shortcomings might result in some constraints to the effectiveness of the SSC work.

As earlier discussed, the effectiveness of the operation of a public regulator depends greatly on the extent to which the regulator can act independently. This has been proven by what happened in the US and Japan. Experience undergone by these two countries seems to support the need for an independent public regulator. Although Japan has not yet had a formal independent agency as the US does, the need for an independent SESC has been discussed for years.[587] However, the situation has not been improved much, since the Ministry of Finance does not support the Japanese-style SEC proposal.[588] The Ministry does not want to narrow down its exclusive control over securities industry.[589] It desires to retain its authority over the SESC and argues that an independent agency is not necessary since the securities companies can be better monitored by a licensing system and an independent agency would be too isolated from the information to work properly;[590] that an independent agency modeled after the US SEC would not work because of the distinguishing features of the securities industry in each country.[591]

It can be said that if Japan does not have an independent SESC, that is not because an independent agency is not necessary in Japan. Of course Japanese people are also aware of that need; however, as earlier-mentioned, the Ministry of Finance does not want to lose its power over securities markets. The reason that led to the failure of Japan in achieving an independent regulator seems to be quite distinct. This should be an invaluable lesson for Vietnam in seeking a suitable model for the future SSC.

IV. THE FUTURE REGULATORY SYSTEM OVER THE VIETNAMESE SECURITIES MARKET

[585] See Curtis J. Milhaupt, above n. 311, 444.
[586] Ibid.
[587] Ibid, 474 - 475; see also Nicole J. Ramsay, above n. 504, 256, 268, 280.
[588] Ibid, (Nicole J. Ramsay), 280.
[589] Ibid.
[590] See Gregory D. Ruback, above n. 505, 211 - 212.
[591] See Nicole J. Ramsay, above n. 504, 280.

1. A Single Public Regulator or a Self-regulatory System or a Combination of the Two: Which Model should be chosen for the Future Regulatory System?

In the earlier discussion of advantages and disadvantages of self-regulation in the securities industry, the literature seems to favor this form of regulation over the governmental one. It is generally recognized that self-regulation is a more effective way to regulate, more flexible and adaptable to the changing demand of the market, and so on. Yes, it seems hard to deny the advantageous aspects contributed by self-regulatory organizations to the regulation of securities markets. The presence of self-regulatory organizations in the regulatory system is thus necessary. Such a presence becomes especially demanding where the government runs short of financial and human resources, if the government embraces all regulatory tasks. The US had undergone such an experience. That was during the New Deal, when the US government was unable to effectively deal with abuse and fraud in the securities markets because of certain constraints in financial resources and expertise. It had to rely on the strength of the securities industry to deal with such problems.[592]

Many even think that government regulation gives rise to more problems than it solves, and in many cases it did not succeed in alleviating market failure.[593] Regardless of these criticisms, however, empirical evidence shows that securities markets do need a measure of governmental surveillance. One might recall that the US securities markets had been under the regulation of the private sector - the securities industry itself - for more than a hundred years before the SEC came into existence. The adoption of a public regulator over securities business in the US is said to have stemmed from the stock market crash of 1929 when the US government perceived the need of a market watchdog.[594]

Furthermore, the whole world has observed a number of countries that have vibrant securities markets which used to employ a single self-regulatory system, but which have been moving toward adopting a similar system to that of the US, where a public regulator is set up side-by-side with self-regulatory organizations. The UK, Germany and Canada are examples of countries that have also adopted a public regulator after a relatively long period of time almost employing a self-regulatory system to govern their securities markets. The move toward a model similar to that adopted in the US can be seen in Japan, as in Henry Laurence's words, *'the creation of the SESC is clear evidence that the Japanese have moved decisively, if incompletely, toward a more American style of financial regulation.'*[595] This observation has recently been further confirmed by Japan.[596]

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[592] See Margot Priest, above n. 513, 268.

[593] Judith O'Hare, "Regulation of the Securities Industry in Hong Kong: The Securities and Futures Commission", (1996) 6 *Australian Journal of Corporate Law* 1, 27.

[594] See Henry Laurence, above n. 494, 658 - 659.

[595] Ibid, 679.

[596] The Chyunichi Shimbun released on September 20, 2000 reported that Japan is going to adopt an independent market watchdog following the US SEC style.

The choice of a regulatory system with the two components, a public regulator and self-regulatory organizations, has become dominant in vibrant securities markets in the last few decades. All these facts have proven that when securities markets developed to a certain extent, governmental intervention is needed because the industry itself can no longer manage the entire regulatory work. Although self-regulation has a number of widely perceived advantages, it sometimes cannot properly cope with frauds in markets because of certain constraints in its enforcing capability.

On this point, one might find a contradiction since it seems that neither self-regulation nor public regulation can cope with market fraud. This is because dealing with market fraud is not a simple task. Mere self-regulatory organizations or public regulation alone cannot accomplish the anti-fraud task, since the former does not properly have enforcing capability while the latter might fall short of resources and expertise. All of these weaknesses of the two regulatory institutions are no longer mere assumptions, rather they have actually been revealed in practice. However, when the two cooperate, they can support each other, as the deficiencies of self-regulation seem to be able to be fulfilled by public regulation and vice versa. A combination of these two institutions into a regulatory system can thus ensure better regulatory outcomes. Securities markets therefore require both government oversight and that of the industry itself. The former is needed to enforce law and regulations against and impose sanctions on market participants as well as to oversee the self-regulatory organizations. The latter is necessary to readily produce and develop tailored rules that are desperately required for regulating the industry whose members often have better technical knowledge of and expertise in the regulated area than the government agency.

From these arguments, it is advisable that Vietnam should adopt a regulatory system with the two components: a self-regulatory system and a public regulator. In that system, the public regulator would delegate a number of rule making and enforcing activities to SROs. The public regulator could concentrate on rule-making activities at a macro level, while SROs could focus on developing concrete rules regulating securities industry members and listed companies, and supervising their compliance with such rules. The public regulator would play a principal role in enforcing laws and regulations; but SROs, while carrying out their supervising tasks, also need enforcing power to enhance market discipline. For example, they should have the rights to revoke membership of their members and to de-list listed companies when the members or the listed companies have violated trading or listing rules. The public regulator should retain the power to oversee SROs to ensure that their activities are taken in conformity with the public good.

By this way of power division, both law enforcement and the development of regulatory rules could be strengthened. Clearly, too many tasks being accomplished by an organization will lessen the organization’s possibility to discharge the tasks well. However, when such assignments are reasonably divided and vested in appropriate bodies, then the outcome should be better.

2. What Should Constitute a Self-Regulatory System over the Vietnamese Securities Market?

a. Stock Exchanges as Self-Regulatory Organizations (SROs)

In Vietnam, when the stock exchanges are put in operation in place of the current stock trading centers, they should also act as SROs. The law should have concrete provisions regulating the operation of stock exchanges as SROs. Their legal structure should resemble that of shareholder-owned corporations as discussed in Chapter V. The SROs' rules of conduct for their members would be approved by the SSC after being open to the public for comment. Securities firms should have their own right in deciding whether to become members of an SRO. However, once a securities firm becomes a member, the member would be bound by rules and regulation of the self-regulatory exchange. Therefore memberships should be revoked by SROs where violations of such rules and regulation are detected. This would more or less create enforcement power for SROs, which in turn, would strengthen market discipline.

b. Other Self-Regulatory Organizations Necessary for a Healthy Market

Other SROs such as the securities dealers' association, the securities investment fund's association, and the association of securities investment advisers are necessary when the number of securities firms increases. The operational purposes of such associations are to cooperate with and support each other in order to promote professional special expertise, and to represent as well as to protect the lawful interests of their members.

The legal structures of these associations should also be specified in the law. In contrast to the stock exchanges, these associations would not take the legal form of shareholding companies. As an association, their operating expenses would be covered by membership fees subscribed by their own members.

Their proposed governance structure might include: (1) a members' meeting to be the highest decision-making body of the association; (2) an executive committee having a specified term of service, and having duties of enforcing rules and regulations of the association; (3) other committees responsible for different tasks of the association such as functioning, advisory and so on.

The rules of these associations should also require the approval of the SSC before taking effect. After that, they would bind the conduct of their members.

When such a system of SROs is put in operation, the SSC could delegate a number of market oversight duties (rule-making and enforcing) to them. And in that way the SSC workload could be reduced, which in turn would give more opportunities for the SSC to accomplish its tasks well.

In the early days, after the national association of securities dealers comes into existence, perhaps its legal form should resemble that of an association. In the later

stages, when the association has central facilities comparable to an exchange floor, and performs broader functions which in combination are those of an exchange, then a corporate form might be a better choice.

3. An Ideal SSC

a. What Form of SSC is best for Vietnam?

In an earlier section of this chapter, the advantages of an independent agency acting as a securities market watchdog have been analyzed in detail. It was well documented that a governmental agency, independent from political and economic ideology as in the case of the US, is necessary to protect public investors and to ensure a free but fair and integrated market. To achieve such goals, the regulatory agency should be able: (1) to segregate securities regulation from the vagaries of the political process; (2) to strike a balance between employing regulatory constraints required to ensure that the market is fair and integrated, and to assure reasonable freedom in markets; (3) to acquire high technical knowledge and expertise necessary for administering complex statutes; and, last but not least (4) to investigate and prosecute high ranking persons who commit fraud in markets. The agency would not accomplish such tasks in the absence of necessary independence. Such an agency therefore seems to be ideal for the times since there has been a tendency to move towards the American approach in choosing an appropriate public regulator. Japan, the UK and Germany are countries involved in such a process.[597] One commentator even recommends that the American SEC model should be adopted in forming the watchdog for the EU securities markets.[598]

It seems hard to deny the necessity of a free, fair and integrated securities market, and of adequate investor protection in Vietnam. It is even harder to say that such goals could be achieved in Vietnam without an independent SSC. This is because most of the factors that require an independent market watchdog in the US seem to exist in any economy. The possibility of political or ideological interference, the likelihood of facing violators who are high ranking persons, the complicated nature of statutes governing securities markets, all are available everywhere including Vietnam. An independent market watchdog is thus also required in Vietnam in achieving a healthy market.

Probably, the future SSC will be set up by the National Assembly acting independently from the government. The composition of the SSC and the term of services served by the commissioners should be clearly provided. The commissioners should not work on a part-time basis as they are doing under the current law, since their posts are so important and their jobs within the SSC office are so complicated. If at the same time they are responsible for their jobs in their own ministries and for that in the SSC, there will be no possibility for them to discharge their duties adequately.

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[597] Ibid, 656.
[598] See Roberta S. Karmel (1999) 38, above n. 492, 34.

b. The SSC Roles in Enforcing Securities Law

Meanwhile, the SSC has rather complete rule-making and administrative powers but lacks a properly adjudicating power to enable it to act as an independent agency.

The SSC rule-making powers are comparable to those of the SEC in the US. The SSC of Vietnam is even more powerful than the US SEC with its administering powers. That is to say, the SSC has too much power in granting issuing licenses for issuers and in conferring business licenses on securities firms.

Power to grant an issuing license to issuers: this licensing power of the SSC distinguishes Vietnam as the country where public issuance of securities is put under the strictest control and where the regulatory body has the deepest power of interference as a watchdog. An arising question is whether with such a deep power of intervention, the SSC would be responsible to public investors if the approved issuing companies were to go bankrupt.

In practice, it is very likely that public investors find securities offering and trading on organized trading centers very reliable, since all listed companies have gone through a very thorough screening process done and approved by the SSC. The SSC thus plays an important role in creating public confidence in securities listed on the trading floor. However, nowhere in the current securities regulation is it said that the SSC will be responsible for losses incurred by public investors in the event of failure of listed companies. Rather, there is a provision saying that

> *The permission of the SSC on which an issuer can publicly issue its securities merely means the issuance has already met statutory requirements but does not imply that the SSC acts as a guarantor for the security's value.*[599]

All these things suggest that perhaps Vietnam should adopt a similar provision to that in other countries in regulating public issuance of securities, which is to allow a simple registration process effected by issuing companies in order to get their securities publicly offered. By this approach, the question of the SSC responsibilities with respect to public investors in the event of the issuing companies becoming insolvent or their security values dropping, will be avoided. Also this can diminish the discretionary power of the SSC in granting issuing licenses to companies that are seeking to go public.

Power to grant business license to securities firms: This power goes against the freedom of doing business. Usually, in other countries, in order to carry out securities business, a company that meets necessary conditions as provided for by the law will merely have to file a registration statement with the agency in charge of overseeing securities markets. This registration requirement should be adopted in Vietnam to simplify the procedure companies have to go through before engaging in securities business. Eliminating the procedure of getting permission from the SSC by securities

[599] See *Circular 02/2001*, Part IV.4.f.

firms is entirely constitutional, since freedom to do business has been enshrined in the Constitution since 1992.

While having ample power in administering the securities market, the SSC does not have enough power in handling cases brought into its office except for the mediating power. Neither does the SSC have power to prosecute criminal offenses. These shortages in its powers will weaken the SSC's capacity, and thus should be taken into account when revising the statutory provisions regulating the operation of the SSC.

CHAPTER VII
SUGGESTIONS FOR A BETTER OPERATIONAL SECURITIES MARKET IN VIETNAM

I. FEASIBLE SCHEDULE FOR LAW REFORM

Earlier discussions draw out a number of law reform tasks for lawmakers. Perhaps it is too demanding to expect all those tasks to be consummated at one time. A feasible schedule for accomplishing all the tasks, or how to make progress in law reform should thus be deliberated.

Since, at the present time, both the Vietnamese people and the corporate community are not very familiar with securities markets and their operation, the initial task of the lawmakers is to make the market become really attractive to the public, which is to build up public confidence over the securities market. To achieve that, strong investor protection plays a significant role. Therefore, in the early stage of law reform, a pressing issue, the assurance that public investors be well protected, should get first priority. An immediate task should thus be concerned with the information disclosure regime, antifraud provisions, and then the regulation of securities professionals. Success in implementing the antifraud provisions greatly depends on the completion of the information disclosure regime, and on an adequate sanctioning system. That is because typical fraudulent activities in the securities market, such as insider trading and misinformation, can occur when the information disclosure requirements are weak, and any type of fraudulent activities can be conducted in the absence of adequate statutory sanctions. Therefore, these areas of securities regulation should be improved in parallel. The strengthening of the regulation of market participants and conflicts of interest amongst them should be the following step.

At a later stage, when the number of listed companies and that of securities firms are enriched, perhaps institutional reform is required. It might be the right time then to redefine the legal structure for the current securities trading center and the planned stock exchanges in order to foster an effective market. That is, to diversify the ownership of stock exchanges, which, in turn, would give them a new form of governance and create more opportunity for them to raise funds from the public. New decision making mechanisms and potential financial capability generated by the new legal form of exchange market, corporate form, would allow the exchange market to cope with an increasingly competitive securities business environment.

Last but not least is to design an appropriate regulatory system to oversee market operation, and to adequately enforce law and regulation. This final step is very important, since in the absence of a strong regulatory apparatus over the market, even if laws and regulations are complete, there seems to be no means to ensure that such laws and regulations are actually implemented.

All these law reform activities would contribute to the attainment of a fair, effective and disciplinary market. Following are concrete law reform activities that should be taken to achieve a well operational securities market in Vietnam.

II. ENHANCING THE EFFECTIVENESS OF A FUTURE INFORMATION DISCLOSURE REGIME

1. Future Disclosure Requirements applying to those who make a Public Offering and to Listed Companies

Concerning the information disclosure regime applying to those who make a public offering (public issuers), and to listed companies, the following issues need to be taken into consideration.

First, concrete guidance and a unique form designed for information disclosure by public issuers and listed companies should be created. It is the lack of such guidelines that has partly led to failures in compliance with the current regulation. Furthermore, educational measures are also important to the success of the implementation of the information disclosure regulation. This is to ensure that information disclosure staff in individual companies are well trained, so that they are able to discharge their disclosure duties skillfully.

Secondly, there should be more helpful ways in which public investors can access company information. Some possible ways include: (1) securities firms shall directly furnish relevant information with an individual investor who shows interest in a relevant security; (2) the issuers shall make information available at their offices for public access; (3) the SSC or securities trading centers shall create a web site (containing all required information of listed companies and of those seeking to go public) providing free access for public; and (4) a computer network among securities trading center, listed companies and securities firms shall be connected.

Thirdly, the *Enterprise Act* should explicitly require companies to furnish company information including a resume of the financial statement, to shareholders before a general shareholders' meeting. This will help shareholders of the companies make informed and prudent decisions at the meeting.

Finally, information disclosure requirements in tender offers should be strengthened: (1) the revised version should clearly prescribe what information is required to be reported, and to whom such information should be reported; and (2) it should also impose disclosure duties on any group of people who purchase, in collusion, more than 5% of voting shares of an issuer.

2. New Information Disclosure Regime governing those Whose Securities Offerings Do not Fall into the Purview of the "Public Offering" and Non-listed Companies

Since the number of non-public-offering companies and that of companies whose securities are traded outside a formal trading center are large, the absence of information disclosure requirements imposed on these companies has become a real threat to the investment safety of the public.

A legal framework for the operation of the OTC market with a comprehensive information disclosure regulation is thus urgently required. Such a regulation should embrace a disclosure regime, which is composed of offering disclosure and continuous disclosure requirements. Only when such a regime comes into existence can the above-mentioned threat be eliminated in part and the market gain more investor confidence.

3. The Need for Comparable Accounting Standards and Adequate Auditing Regulation

Accounting rules and accounting practice are decisive to the quality of information disclosed by companies. Only when a good system of accounting rules are adopted and accounting practice is performed in conformity with such rules, can information disclosed by companies be said to be reliable and useful to the public. Then the securities market can really attract public investors. A deliberate revision of the current accounting regulation of Vietnam is thus required to ensure that accounting rules adequately support the implementation of the future regulation of information disclosure.

The quality of disclosed information, however, is not only dependent on accounting rules but also on accounting practice. Merely having good accounting rules does not ensure that such rules will be followed by companies. It is hard for companies to follow rules and regulations strictly in the absence of a review system. Auditing work is thus of importance in attaining such a goal. In other words, to ensure that disclosed information is of good quality, corporate accounting books should be audited by independent auditors, and all accounting and auditing practices should be overseen by a supervisory body.

The *Enterprise Act* merely requires independent auditing with respect to a number of shareholding companies.[600] Such a provision might give opportunities for officers of the remaining companies to commit fraud. Auditing by independent auditors should thus be required of all shareholding companies. The frequency of such auditing can be defined depending on the company size. Large companies should face auditing work more often then small ones.

A body in charge of overseeing accounting and auditing practices should be set up and work under the supervision of and report to the SSC.

[600] For the discussion of auditing regulation and which companies have been required to submit to independent auditing under the current law, see Chapter II, Section II, Sub-section 2 of this paper.

4. Answers to the Practical Problems of Non-Compliance with the Current Disclosure Regime

a. A Call for a New Enforcement Mechanism

An adequate legal basis for the enforcement of an information disclosure regime should be created. The current securities regulation lacks adequate provisions to enforce the regulation of information disclosure. With a low level of sanctions - merely administrative sanctions- against violations, non-compliance with the current information disclosure regime in particular, and the securities regulations in general, is obvious. Criminal sanctions are thus urgently demanded to ensure that the disclosure regime will be strictly followed.

b. Remedies for Hesitancy of Trading-Center-Ready Companies

To eliminate or at least to mitigate the negative attitude of bourse-ready companies towards going public to raise funds:

First, the *Revised Enterprise Act* should impose information disclosure duties on all the big shareholding companies (whose number of shareholders and amount of equity capital are large) regardless of whether they are listed or not. Companies whose shares' price quotations are frequently published should also be subject to disclosure duties.

Secondly, the government should use its voting rights as a controlling shareholder to drive equitized enterprises on to the trading floor.

Finally, educational measures could be employed to equip the public, including the corporate community and investors, with knowledge of (1) the benefits companies can attain by becoming listed companies; and (2) the benefits generated to the public investors by transparent disclosure by listed companies.

III. STRENGTHENING THE ANTI-FRAUD REGULATION

1. Future Antifraud Regulation and Enforcement Mechanism

a. New Regulation of Short-swing Trading

The future regulation of insider trading needs concrete provisions to:

(1) Impose reporting duties on any persons who, by the acquisition of shares, become large shareholders, and on company insiders having purchases and sales of shares.
(2) Define the point of time such duties should be discharged: that is, at the time the acquisition occurs and at the end of the month the purchasing or selling transactions are effected.

(3) Specify a concrete period of time within which a purchase and its matching sale, generating profits to the company insider, can be deemed as constituting short-swing trading.
(4) Create a legal basis on which a company can confiscate short-swing profits when the purchase and sale are made within a short period of time, as specified by the law.
(5) Last but not least, lay down a legal basis for derivative suits to enable shareholders to institute proceedings against directors or large shareholders when wrong-doing is detected.

b. New Legal Basis for Stabilizing Activities

A legal basis for stabilization of market price should be taken into consideration to enable participants in a securities distribution to employ necessary measures to prevent and to retard falling trend of securities' prices during a public offering, or to avoid risk to them (the underwriters). New statutory provisions are thus required to distinguish bidding and purchasing activities done by securities distributors to induce others to purchase the distributing securities with activities that are actually done to stabilize the securities price to ensure safety to underwriters of the offering securities.

As for the repurchase of outstanding shares by companies, for the time being, the law merely requires share buyback to be approved by the general shareholders' meeting and then by the SSC or the relevant securities trading center. No statutory provisions prescribe the criteria a company has to meet to realize the proposal of share buyback. There should be provisions laying down the limits concerning the time at which share buybacks can be effected, and the maximum price at which companies can repurchase their shares. This is of importance to avoid situations where a company can manipulate its share price.

c. Prohibition of Omissions of Material Information

A mere prohibition of false statements is not enough to avoid public investors being misled. The proscription of the omission of information is thus required since a true statement does not always mean a full statement.

Furthermore, the forbiddance of misinformation that merely applies to limited groups of persons will not ensure good outcomes for the securities regulations. Such a prohibition should be applied to other potential persons (e.g. securities trading centers, appraisal agencies, law firms and accounting firms) to eliminate possibilities where they can commit fraud.

d. New Legal Bases for Rights of Action and for Sanctions against Violations

d.1. Rights of action

At present, in order to seek legal action against wrongdoers that do not fall within the purview of administrative violations, investors have to rely on the general provision of the *Ordinance on Procedure for Settlement of Civil Disputes.* Nothing in the securities regulation explicitly vests the right in investors to sue the securities law offenders to protect themselves. Only the rights of individuals to make accusations regarding administrative violations to the competent state authorities are stipulated. Accordingly, other violations not of an administrative nature cannot be accused by individuals since the securities regulation does not give a legal basis for doing so. Concrete provisions concerning private right of action should thus be created so as to build up the faith of investors in that where necessary, they are entitled to sue in court to protect their lawful interests.

The *Enterprise Act* also needs concrete articles providing for class and derivative actions to ensure that company shareholders have adequate legal remedies to protect their own interests as well as those of the company.

In the absence of concrete provisions stipulating such rights of action, it will take time and also energy for courts to define fairness while hearing a case.

In contrast to a suit instituted by a private action or class action, in a derivative suit, the plaintiff will not receive any compensation even if he/she eventually defeats the defendant. High court fees will thus minimize the number of derivative suits brought to court. To cope with this problem, reasonable court fees should be adopted.

d.2. Statutory Sanctions for Violations

The securities regulation merely sets out the levels of sanction to be borne by violators. Depending on the nature of the violation and the extent to which the securities regulation are breached, then disciplinary, administrative, criminal, and civil sanctions can be imposed on the violator. However, apart from administrative sanctions, the concrete levels of disciplinary, civil, and criminal sanctions are not yet provided. Provisions concerning adequate criminal sanctions, a fine system, as well as proper compensations for damages caused by fraud, should be created to enable the securities regulation to be well enforced.

As long as public confidence in a securities market is maintained, the market can attract customers. Failure in doing so will result in an ineffective market that go against the goal of Vietnam in creating a market place where capital demands can be increasingly and widely met to support the economic development of the country.

2. New Supporting Instruments for a Future Market

a. Margin Trading should be allowed Within a Certain Threshold

It seems to be an over-regulated provision when totally prohibiting the purchase of securities on margin instead of setting a margin on which investors can purchase securities for speculation. Possibly a certain percentage of credit extending for the purchase of securities should be stipulated to enable margin transactions that have been deemed helpful for the creation of healthy markets.

b. Short Sale should not be totally prohibited

This activity is also over-regulated since it is definitely prohibited under the current regulation. The future regulation should make a distinction between short selling done by company insiders and that done by other persons. It should also embody a distinction between a short sale consummated when the price is falling and that effected when the price is increasing. And possibly short sales should only be prohibited (1) when such transactions are effected by company insiders, or (2) where there is a falling trend in the price of the relevant securities.

3. Eliminating Technical Deficiencies

A general lack of definitions of a number of significant terms employed in the anti-fraud regulation will make it hard to avoid the committing of fraud. Thus, each prohibited activity should be well defined when revising the regulation.

Inconsistencies in the use of legal terms in different legal texts that constitute the anti-fraud regulation are other obstacles to ensuring that the securities regulation will be well enforced. This should also be avoided so as to enhance the effect of the regulation.

IV. COMPLETING FUTURE REGULATION OF SECURITIES PROFESSIONALS

1. Conflicts of Interest Issues

Since the regulation of conflicts of interest between securities firms and their customers is of importance in creating public confidence in securities markets, concrete provisions spelling out duties of securities firms in relation to their customers to avoid conflicts of interest between them are thus required.

Merely defining the duty of securities firms to find out the financial situation and investment purposes of their customers is not enough. The provision should be more detailed so as to require securities firms to obtain such information before recommending

a type of security, so that they can ensure that the recommended security is suitable to a customer's needs and financial conditions.

Other provisions essential to insert in the regulation include: a provision, which imposes duties on securities firms to investigate the nature and risk of the securities they are going to recommend to their customers; a provision on which securities firms must disclose their conflicts of interest to their customers (that they have interests in the security they recommend the customer to purchase; or whether they act as a broker or a dealer in the relevant transaction); and a provision to prohibit securities firms from engaging in excessive trading of securities for the sake of getting more commission from customers; and from overcharging customers when providing services.

2. Banks and the Securities Market

As earlier discussed, regulation of the involvement of banks in the securities market in Vietnam is rather strict. In the future, such a market should be more open to banks. Less risky securities activities such as brokerage, investment consultancy and securities portfolio management are quite suitable for banks to carry out directly. The presence of banks in the securities market, even within these business areas, would widen the market participants and also strengthen competitive force in the market, which in turn would promote the development of the market. And it also expands the business environment for banks.

For the sake of the banking system, other highly risky business activities such as underwriting and dealing in securities should probably be left for banks' securities subsidiaries.

3. Banks and their Securities Subsidiaries.

Since banks should be permitted to set up their own securities subsidiaries to carry out underwriting and dealing activities. Both banks and their subsidiaries should be subject to a number of criteria specified by the law to avoid risks in doing business. Such criteria should cover bank's capital, assets and state of management. After setting up a subsidiary, a further requirement needed is that the capital of a bank and that of its subsidiary should be clearly distinguished. In addition, permissible activities for banks' subsidiaries should be clearly specified in order to avoid risks for their parent banks.

V. INSTITUTIONAL REFORM

1. A Desirable Model for Future Exchange Markets

State-owned entities in general, and state-owned stock exchanges in particular, have shown to be inefficient in practice. The mutual form of stock exchanges has recently

exposed weaknesses. Defining an accurate form for the current securities trading centers and the planned stock exchanges is thus of importance. The shortest and most economic way to achieve such a goal may be to learn from overseas experience. And that would mean adopting a shareholders-ownership structure for stock exchanges.

In such a legal form, stock exchanges themselves are shareholding companies having their shares listed on their own trading floors and having outstanding shares held by the public. The exchange would be governed by a management board and a director. The highest decision-making body of the exchange would be the general shareholders' meeting. The exchanges, after being formed by the SSC in conformity with the securities law, should also be subject to the *Enterprise Act* as are other shareholding companies. The SSC should retain supervising power over the compliance of stock exchanges, with listing standards and trading rules, so that conflicts of interest that might occur when stock exchanges are in charge of enforcing listing rules against themselves will no longer be a matter of concern for the public.

To cope with the threat of mergers to stock exchanges, the following two alternatives can be chosen: (1) the state should hold a controlling block of shares in such exchanges and act as a shareholder having rights and duties corresponding to its equity ownership; or (2) where the state is not a controlling shareholder of stock exchanges: (a) the law should put some limit on the maximum equity that can be held by each shareholder of a stock exchange; or (b) all takeovers and mergers among stock exchanges should be required to get approval from the government before they can actually be effected.

2. An ideal SSC

a. The Form of a Future SSC

The future SSC should be set up by the National Assembly as an agency independent from the government. The composition of the SSC and the term of services served by the commissioners should be clearly prescribed in the law. Part-time commissioners should be avoided since the tasks of the commissioners working in the SSC office are very onerous and complicated. If at the same time they are responsible for their tasks in their own ministries and for these in the SSC, there will be no possibility for them adequately to discharge their duties.

b. The SSC's Powers in the Future

Meanwhile, the SSC as it now exists has rather complete rule-making powers, which are comparable to those of the US SEC. Its administrative powers are even broader than those possessed by that body. However, it lacks a properly adjudicating power to enable it to act as an independent agency.

It can be said that the SSC has too many powers in granting an issuing license for issuing companies and in conferring a business license on securities firms. Since Vietnam adopts a licensing system rather than a registration system for public offerings of securities, the SSC might be expected to be responsible for the securities being issued on the approval of the SSC. That is because such an approval seems to give a guarantee for value of the approved securities. This could put the SSC in a deadlock situation as in practice it cannot bear all such liabilities.

All these things suggest that Vietnam should adopt a similar provision with that in almost all other countries in regulating public offering of securities. That is, to allow a simple registration process by issuing companies in order to get their securities publicly offered. This approach would eliminate the SSC responsibilities with respect to public investors in the event of the issuing companies become insolvent or the values of their securities dropping. It would also diminish public concern about the discretionary power of the SSC in granting issuing license.

The elimination of the SSC's power to grant business licenses to securities firms is also required since this power goes against the freedom of doing business entrenched in the *Constitution*. A simple registration procedure for those who seek to carry out securities business should thus be adopted in Vietnam.

In contrast to administrative power, dispute resolution power of the SSC is at present merely confined to reconciliation. The SSC is not able to adjudicate disputes brought into its office, which is of importance in ensuring its independence, which is vital in order to administer the market effectively.

The SSC does not have powers to prosecute criminal offenses. This shortcoming in its powers will weaken the SSC’s capacity, and thus should be taken into account when revising the relevant statutory provisions.

3. The Need for a Self-Regulatory System

A self-regulatory system in Vietnam should consist of stock exchanges and some other associations of securities professionals. The latter might include a securities dealers association, a fund management companies association, and an investment consultancy companies association.

The law should thus include concrete provisions regulating the formation and operation of these SROs. Their legal structures should resemble that of a stock corporation in the case of stock exchanges, or of an association in the case of others. The SROs’ rules should be approved by the SSC after being open to the public for comments. The membership of these SROs should be subject to the initiative of securities firms. However, after becoming a member, the member would be bound by rules and regulation of the relevant SRO. The SROs should be able to revoke membership once a member is found breaching SRO rules. This is of importance in enhancing market discipline.

With such a regulatory system, the SROs can utilize their strength in developing tailored rules governing industry members and listed companies, while the SSC's

workload can be reduced by switching a number of rule making and enforcing duties to the SROs. This would enable the SSC to concentrate rather on macro issues, and give more opportunities for the SSC adequately to accomplish its tasks. The SSC, however, should retain powers to oversee these SROs, to ensure that they act in conformity with rules and regulations, especially when they themselves are also legal entities competing with one another.

APPENDIX

CREATING A FAVORABLE LEGAL ENVIRONMENT SURROUNDING SECURITIES REGULATIONS FOR THE FUTURE SECURITIES MARKET

Professor Louis Loss, in "Fundamentals of Securities Regulation", points out: securities regulation is like *"an amalgam of everything from contracts and torts to corporations and international law, it is difficult to draw precise boundary lines around the subject matter."*[601] Therefore, it seems proper and necessary for our present study to analyze the operation of securities markets in a broad legal environment in which many aspects - from the constitution, enterprise law, tax law and foreign investment law to civil law and criminal law - will be discussed. The discussion will seek out statutory deficiencies that need to be eliminated in order to create a really supportive legal environment that will make possible a vibrant securities market in Vietnam.

I. RELEVANT LAWS CONCERNING THE OPERATION OF THE SECURITIES MARKET IN VIETNAM

1. The Constitution

Although the economic reform was introduced in 1986, the supreme legal basis that strongly supports such a reform only came into existence in 1992, when the new *Constitution* was passed. Its passage by the National Assembly has given strongest legal foundation for the long term existence of a multi-component commodity economy. Article 15 reads:

> *The State promotes a multi-component commodity economy modeled on a socialist-oriented market mechanism functioning under state management. The multi-component economic structure with diversified forms of production and trading organizations is based on a regime recognizing the whole people ownership, collective ownership, and private ownership. Among them, the whole people ownership and collective ownership constitute the foundation.*

Recently the *Constitution* was revised[602] and this Article was altered. Recognition of the multi-sectoral economy has remained and has been strengthened. The Article has further

[601] See Louis Loss, *Fundamentals of Securities Regulation*, (1988), 72.

[602] On December 25, 2001 the Vietnamese National Assembly passed "The Resolution on the Amendments of and the Additions to a Number of Articles of the 1992 Constitution of the Socialist Republic of Vietnam".

been developed compared with its old version to ascertain a strong will of the Government in developing the economy as well as in industrializing and modernizing the country. The revised Article 15 reads:

> *The State shall build up an independent and autonomic economy, based on the promotion of internal forces and of international economic integration; the State shall accomplish the industrialization and modernization of the country.*
> *The State shall consistently implement a policy on the development of a socialist-oriented market economy. That is a multi-sectoral economy having diversified forms of production and trade. Such forms should be based on whole people ownership, on collective and private ownerships. Among them, the whole people ownership and collective ownership constitute the foundation.*

The *Constitution* has also created fundamental principles for the operation of the newly emerging market economy, such as freedom to do business,[603] and equality before the law of all business entities regardless of what economic sector they may belong to.[604] The state also recognizes the diversification of economic sectors and protects lawful ownership of individuals and entities doing business.[605] The legalized economic sectors are to include the state, cooperatives, private business and that of private capitalists (*kinh te tu ban tu nhan*). The recent revision of the *Constitution* further legalizes one more type of economic sector, namely that of small shopkeepers (*kinh te tieu chu*).[606]

These supreme principles once again reflect the government policy of promoting a multi-sectoral economy, an important criterion for the establishment of securities markets. Such policy has also been embedded in various laws governing the Vietnam economic system such as enterprise law, banking law, foreign investment law, and tax laws.

2. The Enterprise Law

Enterprise law is closely connected with securities regulation, for example: the way in which a company can raise capital; duties of a company in raising funds from the

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[603] See Art. 57. This Article reads: *"Citizens have a freedom to do business"*.

[604] See Art. 22. This Article reads:

"Production and trade entities that belong to any economic sector shall fully discharge their duties with the State. They shall be equal before the law. Their capital and lawful properties will receive protection from the State.

Enterprises that belong to any economic sector are eligible to establish joint-ventures, and to associate with other individuals, and domestic and foreign economic organizations in conformity with laws and regulations."

[605] See Arts. 19 - 23, 25 and 58.

[606] See the Revised Article 21.

public; rights of a company in reducing capital (share buyback), and so on. Enterprise law thus has a crucial impact on the effectiveness of a securities market.

In practice, securities markets have a longer history than that of securities law. This means that law was a consequential product following the securities markets, created by lawmakers where they found it necessary to put some statutory constraints over market transactions. However, in Vietnam, one might say that the securities market is a "product" of law. Is this true? If we look for a securities market by seeking an organized stock exchange, then the answer will be "yes". That is because we have witnessed the government's efforts in preparing a legal framework for the birth of the first Stock Trading Center in Ho Chi Minh City. However, if we take the view that the presence of any securities transaction being conducted can be deemed as a proof of the existence of a securities market, then the answer may be "no".

As mentioned in Chapter I of this paper, the legal recognition of shareholding companies has been in existence since 1990 when the *Company Act*[607] was passed. Consequently, securities markets, in theory, must also have existed since then to enable the establishment of such a new form of company. From 1990 to 1997, however, a separate securities regulation had not been available. In the absence of such a regulation, the *Company Act* was clearly expected to more or less cover securities transactions. However, the *Company Act* merely provided for some fundamental principles such as: company members' equity ownership;[608] members' right in transferring subscribed capital or shares;[609] limited liability of company members;[610] and a simple company management structure.[611] Many areas concerning securities regulation were left open, such as: an adequate information disclosure when a company goes public for capital raising; necessary limits on the right of members of management boards and directors in engaging in securities transactions; disclosure of equity ownership of such members, directors and controlling shareholders; the minimum length of time for which company incorporators are required to hold shares; the transfer of equity ownership where such equity was subscribed in the form of immovable assets; the distinction between private and public offerings, and so on.[612]

In addition, some prohibitions under the Act even caused difficulties to companies in raising funds for business development. For example, limited liability companies were forbidden from issuing any kind of securities.[613]

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[607] In Vietnam, each type of enterprise is regulated by a different law. In terms of their ownership, enterprises fall into four categories: (1) state-owned enterprises, (2) foreign invested enterprises, (3) cooperative enterprises, and (4) privately owned enterprises. They are subject to the *State Enterprise Act*, *Foreign Investment Act*, *Cooperative Act*, and *Enterprise Act*, respectively.
[608] See Arts. 5 & 8.
[609] See Arts. 25.2 & 30.4.
[610] See Art. 2.
[611] See Arts. 27, 28, & 37 - 41.
[612] For further information, see Section III, Sub-section 1, Chapter I of this paper.
[613] See Art. 25.1.

Only in 1998 was a separate securities regulation adopted - under the form of a governmental legal document, *Decree 48/1998*. Two years later, in January 2000, the 1990 *Company Act* was also replaced by the *Enterprise Act*.[614]

The *Enterprise Act* was said to represent a big step forward that Vietnam was making toward general standards of corporate laws comparable to those in most of the developed economies.[615] This Act introduced a number of new concepts, such as corporate governance,[616] company disclosure,[617] and minority shareholder protection.[618] Furthermore, by permitting companies to issue securities,[619] by recognizing shareholders' rights and obligations in offering, selling and purchasing shares[620] and so on, the Act, to some extent, shows its cooperation with *Decree 48/1998* in regulating securities markets. However, the *Enterprise Act*, once again, does not clarify private and public offerings, while clearly saying that the offering and issuing of securities by shareholding companies will be subject to securities regulation[621] (the term "securities regulation" covers *Decree 48/1998* and other relevant legal documents guiding the implementation of this Decree). It should be emphasized that the current securities regulation only covers public offerings. Private offerings, consequently, are not subject either to the *Enterprise Act* or to the current securities regulation. This is surely a matter of great concern for investors in private offerings.

Furthermore, although the regulation of information disclosure was inserted in the *Enterprise Act*, such regulation is too rudimentary and merely gives some general principles concerning shareholding companies' duties in disclosing information on an annual basis. This issue has already been discussed in depth in Chapter II of this paper.

3. State Enterprise Law

State enterprise law may appear to have no connection with the securities regulation, since it regulates a kind of enterprises having capital subsidized from the state budget. However, some issues concerning the rights of state enterprises in raising funds and using their capital under the *State Enterprise Act* (*Luat doanh nghiep Nha nuoc*) are considered appropriate for discussion here.

Pursuant to the law, state enterprises can raise funds by issuing bonds and shares, and by borrowing from banks and elsewhere, provided that the ownership of such enterprises is not converted into another kind of ownership by way of capital

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[614] As earlier mentioned, the *Enterprise Act* was passed in 1999. On January 1, 2000, it came into force and replaced the 1990 *Company Act* and *Private Enterprise Act*.
[615] See: "Vietnam", *APECA Press Release*, http://apecsec.org.sg/whatsnew/press/rel52_99.html; see also "Obstacles Ahead for Lauded Vietnam Business Law", http://vinsight.superb.net/1999news/1217.html, visited Dec. 23, 2001.
[616] See Arts. 34, 49, 69, 97 & 101.
[617] See Arts. 20, 21, 53 & 93.
[618] See Arts. 31, 20, 21, 23 & 93.
[619] See Art. 51.2.
[620] See Arts. 53 & 64.
[621] See Art. 61.4.

mobilization.[622] This provision is, by itself confusing, since once a state enterprise has issued shares, part of its ownership would be transferred to shareholders under Article 2.1 *Decree 48/1998*.[623] Consequently, the enterprise ownership would no longer be a pure state-ownership, but rather be converted into another form, private ownership, and the enterprise itself would become a shareholding company.

The *State Enterprise Act* does not have a single article saying that state enterprises can transfer their capital. Article 7.h merely allows state enterprises to use capital *"to invest in, to join up or cooperate with, and to subscribe equity to other enterprises in conformity with the law."*

However, owing to socio-economic circumstances which have changed since the passage of the *State Enterprise Act*, the Government's intention to equitize a number of state enterprises has been implemented on a large scale since May 1996 by the issuance of *Decree 28/CP*.[624] This Decree was replaced by *Decree 44/1998*, which in turn has recently been again repealed by *Decree 64/2002*.

The legal recognition of the equitization of state enterprises means that the transfer of capital in such enterprises is permitted. It has been roughly estimated that by 31 December 2000, the number of state enterprises throughout Vietnam that had been equitized was 532. In the year 2000 alone, 188 out of 692 state enterprises were equitized or had their ownership converted into other forms, which accounts for 27.2% of the target.[625] Pursuant to Article 1.2, the *Enterprise Act*, the newly formed shareholding companies after being equalized, are to be subject to the *Enterprise Act*. This Article was inserted in the Act since the lawmakers hoped that it would promote the equitization process of state enterprises, improving their management and facilitating the formation of securities markets in Vietnam.[626]

Title to the shares can be sold to any economic organization or individual. Where such transactions involve foreign investors (including individuals and entities) they must be subject to some statutory restrictions. Under Article 2, *Decision 145/1999*,[627] foreign investors can only purchase shares from state enterprises operating in 12 business areas as

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[622] See The *State Enterprise Act*, Art. 8.1.b; see also Art. 1.3, *Decree 27/1999/ND-CP* dated 20 April 1999, revising *Decree 59/CP* dated 3 October 1996 promulgating the "Regulation of Financial Management and Business Accounting in State-Owned Enterprises".

[623] This Article reads *"Securities are certificates or book-entry records, certifying eligible ownership of security holders with respect to the asset or capital of the issuer・・・"*

[624] Art. 1, *Decree 28/CP* set out two goals of the equitization program. The first is to mobilize savings from enterprises' employees, from individuals and economic organizations inside and outside Vietnam to modernize technology and promote enterprises' development. The second is to create opportunities for enterprise employees and others to become enterprise owners, which, in turn, is expected to foster more effective business performance by the equitized enterprises.

[625] See: Minh Huong, "Tinh hinh CPH DNNN nam 2000 & cac bien phap trong thoi gian toi" [The Equitization of State-Owned Enterprises in the Year 2000 and Necessary Measures in the Coming Time], *Thong tin Tai chinh [Financial Bulletin]* 28, (1/2001) (Iss. 1+2), 28.

[626] See "Enterprise Law Passed, May 1999", *Trade Information Center*, http://infoserv2.ita.doc.gov/apweb.n, visited March 20, 2001.

[627] The full name of this legal document is *Decision 145/1999/QD-TTg*, issued on June 28, 1999 by the Prime Minister, promulgating "The Regulation of the Sale of Shares to Foreign Investors".

provided in the Appendix of *Decision 145/1999*. Furthermore, according to Article 6, *Decision 145/1999*, the total value of shares sold to foreign investors must not exceed 30% of charter capital of the issuing company.

However, according to Article 1, *Decision 139/1999*,[628] foreign entities and foreigners can maximally hold 20% of the total outstanding shares of one issuer. Any one foreign entity and any one foreigner can own, at most, 7% and 3% of the said shares, respectively.[629] It is very likely that the total shares of a company held by foreign investors could satisfy the requirement under Article 6 of *Decision 145/1999* (not to exceed 30% of company charter capital) but not meet the requirement under Article 1, *Decision 139/1999* (not to exceed 20% of total outstanding shares of the company). In such a case, if the company meets all statutory requirements for listing its shares on a securities trading center, then it is unclear whether or not the company has to buy back the excessive amount held by foreign investors. Article 6, *Circular 01/1999*[630] says only that, in such a case, the foreign investors "*are only allowed to sell shares*". This might be construed as meaning that what the investors can do is to sell their securities, not to buy more securities. Nevertheless, this does not necessarily mean that they must sell their shares to meet the ratio provided for in Article 1, *Decision 139/1999*.

The recently released *Decree 64/2002* says that foreign investors can purchase shares of an equitized enterprise, provided that the total value of the purchased shares does not exceed 30% of the charter capital of the equitized enterprise operating in specified areas as defined by the government.[631] Thus *Decree 64/2002* does not make any change to the ceiling limit on the amount of shares purchased by foreign investors as provided in *Decision 145/1999*. The above-mentioned problem therefore remains intact.

It can generally be said that the legal permission under which state enterprises can be converted into other form of ownership, and can go public to raise capital, will actively promote the development of the securities market, since it provides the market with more commodities. However, whether such a permission results in positive impact on the market depends on a number of factors. The above-mentioned statutory uncertainties, for example, can be hurdles on the way to converting state enterprises into other ownership forms.

4. Banking law

The *Credit Institutions Act* permits the establishment of shareholding credit institutions including shareholding banks, shareholding financial companies and shareholding financial leasing companies.[632] When such shareholding companies are

[628] The full name of this legal document is *Decision 139/1999/QD-TTg*, issued on June 10, 1999 by the Prime Minister, promulgating "The Regulation of the Proportion of Foreign Ownership in Vietnamese Securities Markets".
[629] Those figures apply to any circumstance regardless of which economic sector the issuer belongs to.
[630] The full name of this document is *Circular 01/1999/TT-UBCK1*, dated December 30, 1999, guiding the implementation of *Decision 139/1999*.
[631] See Art. 5, paragraph 2.
[632] See Art. 12.

formed or raise more funds during their lifetime, then they actively participate in securities markets as issuers.

The *Act*, while recognizing shareholding credit institutions, is silent on a number of issues concerning the issuance and transfer of shares by credit institutions and concerning the rights and duties of shareholders of credit institutions. It does not even say that the issuance of shares by credit institutions has to be subject to securities regulations. Only in the year 2000, three years after the passage of the *Credit Institutions Act*, was a governmental level legal document, *Decree 49/2000*,[633] passed where by these legal loopholes were eliminated. This Decree explicitly gives legal basis for the issuance of shares by commercial banks. Sub-articles 2 and 3 of Article 43 read:

> 2. *The issuance of shares shall be done in conformity with the State Bank's rules.*
> 3. *The issuance of shares to the public and through the securities market shall be done in accordance with the regulations of securities and the securities market.*

Credit institutions can act as investors, since the *Act* allows them to use their charter capital and/or reserved funds to subscribe capital into or to buy shares from other companies or other credit institutions.[634]

Since the *Credit Institutions Act* was passed in 1997, and before the issuance of *Decree 48/1998,* there were some discrepancies between these documents.

First, the Act does not have any article specifying whether or not credit organizations can directly participate in securities markets. In other words, it seems that the Act does not prohibit direct participation of credit institutions in the securities market, nor does it say that credit institutions are not to carry out securities business. Accordingly, credit institutions can enter securities business. However, *Decree 48/1998* explicitly prohibits credit institutions from carrying out securities business directly.[635] If they desire to engage in this kind of business, they have to set up their own securities subsidiaries. In 1999, *Decision 172/1999* issued by the Prime Minister once again confirms the prohibition entrenched in *Decree 48/1998*, by laying down legal foundation for banks to establish their own securities subsidiaries.

The *Credit Institution Act,* although silent on the issue concerning the participation of banks in securities business, allows banks to provide a wide range of financial services: (1) Banks can manage assets for their customers.[636] The term "asset" is construed in the *Civil Code* as various things including securities.[637] Thus, pursuant to the *Civil Code* and

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[633] This Decree is dated September 12, 2000, promulgating "The Regulation of the Organizations and Operation of Commercial Banks".
[634] See Art. 69.
[635] See *Decree 48/1998*, Art. 29.1.
[636] Art. 72.
[637] Art. 172.

the *Credit Institution Act*, banks can manage securities without obtaining a license from the SSC.

However, according to *Decree 48/1998*, organizations that engage in securities custody service must (a) meet a number of criteria concerning capital, material and technical bases and specialty in conformity with the SSC rules; and (b) must obtain a license from the SSC to provide such a service.[638]

(2) Banks can provide financial advisory services.[639] Since the *Credit Institution Act* does not define the term "financial advisory service", securities investment advisory services might arguably be included in financial advisory services. Consequently, banks can directly act as securities investment advisers without obtaining a license from the SSC as required under Article 29, *Decree 48/1998*.[640]

(3) Banks can serve as custodians of papers that can be valued in cash (negotiable instruments).[641] Once again, through the lack of definition of “papers that can be valued in cash” in the *Credit Institution Act*, it can be argued that securities can also fall into the meaning of that term. As a result, banks would be entitled to the custody of securities pursuant only to their banking business license issued by the State Bank, without needing the SSC permission.

Secondly, while *Decree 48/1998* expressly states that all public issuance must be approved and licensed by the SSC,[642] the *Credit Institutions Act* says that with an approval from the Governor of the State Bank of Vietnam, credit institutions can issue depository certificates, bonds and other certificates that can be valued in cash (negotiable instruments) to raise funds.[643] Accordingly, there seem to be two governmental authorities from whom issuers can obtain permission to make a public issuance: the State Bank of Vietnam (giving permission to the issuers that are credit institutions) and the SSC (giving permission to issuers other than banks). This might cause difficulties in managing and supervising issuing activities on the market.

5. Foreign investment law

In 1987, immediately after the initiation of the economic reform in Vietnam, the first statute on foreign investment in Vietnam, the *Foreign Investment Act*, was passed. The Act set out the basic structure for foreign investors' businesses conducted in the country. The main purposes of the Act included: developing economic cooperation with

[638] Art. 62.
[639] Art. 75.
[640] This Article allows banks to enter securities markets by setting up their own subsidiaries under the form of securities firms. Such firms must get a business license from the SSC to act as brokers, dealers, underwriters, providers of portfolio management service, and securities investment advisers.
[641] See Art. 76.
[642] See Art. 3.1.
[643] See Art. 46.

foreign countries, achieving domestic economic development, and expanding export based on effective exploitation of natural and human resources.[644] This Act was revised twice, in 1990[645] and then in 1992,[646] to adapt to changing circumstances previously unknown to the lawmakers and to make the business environment in Vietnam more attractive for foreign investors.

As the economic circumstances had further changed since the passage of the first *Foreign Investment Act* (in 1987), this Act was replaced in 1996. The purposes of the 1996 Act seems to have been broader than those in the 1987 Act. The 1996 Act aimed to expand economic cooperation with foreign countries to foster industrialization, modernization and national economic development on the basis of the efficient exploitation and use of various resources of the country.[647]

However, after the Act had been in force for several years, a number of issues arose that came under the scrutiny of the lawmakers. First, the 1996 Act did not allow foreign invested enterprises to be converted into other business forms. Pursuant to the 1996 Act, foreign investors, under provisions similar to those of the 1987 Act, could do business in three forms: 100% foreign owned enterprises, joint venture enterprises and business cooperation contracts. During their life time, they could not change their form when they desired to do so. For example, a 100% foreign owned enterprise could not be converted into a joint venture enterprise or vice versa even though such a conversion might benefit the enterprise. Secondly, during the course of business, foreign invested enterprises might need to raise more funds but they could only do so through banking finance, not through the issuance of securities. This caused difficulties to such business entities in seeking to expand their businesses. These are among a number of controversial issues that have been discussed over several years.

The 1996 Act was again revised in June 9, 2000. The *2000 Revised Act* tends to give more legal protection to foreign investors,[648] and more tax incentives[649] and to eliminate troubles for foreign investors in transferring legal capital.[650] Under the *2000*

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[644] See *"The Foreign Investment Act"*, first paragraph.

[645] On June 30, 1990, the National Assembly promulgated the *Act on Amendment of and Addition to a Number of Articles of the Foreign Investment Act* (hereinafter, the *1990 Revised Act*).

[646] On 23 December 1992, the National Assembly, once again, issued the *Act on Amendment of and Addition to a number of Articles of the Foreign Investment Act* (hereinafter, the *1992 Revised Act*).

[647] See the *Act on Amendment of and Addition to a number of Articles of the Foreign Investment Act* dated 9 June 2000 (hereinafter, the *2000 Revised Act*), first paragraph.

[648] See the *2000 Revised Act*, Articles 1.4 and 1.5. For example, under Article 1.5, if a change in laws adversely affects the interests of foreign invested enterprises and parties to business cooperation contracts, they will be permitted to continue to apply the incentives or favorable conditions stipulated in their investment license under the *Foreign Investment Act* or may be entitled to (1) change the objectives of the project; (2) exemption and reduction of taxes according to laws; (3) deduction of damages from taxable income; (4) proper compensation in cases of necessity.

[649] Ibid, Arts. 1.11, 1.12, and 1.14, For example, Article 1.11 offers more favorable profit remittance tax rates (at 3%, 5%, and 7%) depending on the amount of contributed capital. In the old law those figures were 5%, 7%, and 10% respectively.

[650] Ibid., Art. 1.7. Under this Article, the transfer of capital no longer needs the approval for validity from the state authority. It will only be subject to registration with the licensing authority. This will save much time and

Revised Act, the transformation of forms of investment is permitted. Foreign invested enterprises are now able to switch to another investment form by division, separation, merger or consolidation.[651]

It can be said that a number of favorable conditions have been provided to promote foreigners doing business in Vietnam. In fact, Vietnam has recorded important achievements in the foreign direct investment area. It is estimated that by the 13th year from the date the first *Foreign Investment Act* was promulgated (in 1987), more than 3,000 foreign direct investment projects have been licensed.[652]

However, the second controversial issue was not dealt with in the *2000 Revised Act*. That is the right of foreign invested enterprises to go public to further mobilize capital. In other word, the equitization of foreign invested enterprises was not adopted in the *Revised Act*. In practice, foreign investors in Vietnam view equitization as an efficient way to mobilize capital and expand business. They have expected a firm legal basis to enable such a process. Nevertheless, the equitization has merely been conducted on an experimental basis because of the lack of statutory provisions.[653] It is reported that *"previously, FIE equitization was included in the ministry's draft amendments to the Law on Foreign Investment in Vietnam* (the Act), *but not in the final version."*[654]

It may be useful at this point to define the gains and losses that might result from the equitization of foreign invested enterprises. First, the equitization can benefit foreign invested enterprises. It diversifies forms of capital mobilization, facilitates business expansion and thus makes the investment environment in Vietnam more attractive. Secondly, the equitization can also be a good way to enrich commodities for the newly established Securities Trading Center in Vietnam. However, the current *Foreign Investment Act* only recognizes one corporate form of foreign invested enterprises, namely the limited liability company.[655] If foreign invested enterprises are permitted to be equitized, then they will turn into shareholding companies, which do not fall within the scope of the Act. Another subsequent step that should be taken is to modify the *Foreign Investment Act* once more to enable it to govern all the forms of foreign invested enterprises. Even if the modification process at legislative level is not costly, another question concerning the current foreign investment policy adopted by the Vietnamese

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effort for the relevant parties to the transaction. This Article no longer requires the transferor to give priority to Vietnamese entities in the case of joint venture enterprises; no longer require the transferor to offer preemptive rights to Vietnamese entities in the case of 100% foreign owned enterprises - in such transactions.

[651] Ibid, Art. 1.3.

[652] See "Foreign Invested Enterprises Eager to Fill out Ranks of VN's New Stock Market" *Vietnam Economic Times* (Nov. 9, 2000) http://www.vneconomy.com.vn/en/ext_economic/fdi/e10057.htm, visited Mar. 20, 2001.

[653] Ibid.

[654] See "11 FIEs Apply to Go Public", *Vietnam Economic Times* (Nov. 1, 2000) http://www.vneconomy.com.vn/en/ext_economic/fdi/e10050.htm, visited Mar. 20, 2001.

[655] See Arts. 6 and 15. The former, *inter alia*, says: "*A joint venture enterprise can be established under the form of a limited liability company having legal personality pursuant to the Vietnamese law*"; the latter also states, *inter alia*: "*A 100% foreign owned enterprise can be set up under the form of a limited liability company having legal personality pursuant to the Vietnamese law* ".

government arises. That is, since 1987 the Vietnamese government has initiated a policy with generous incentives to attract foreign capital directly invested in the country. If the equitization of foreign invested enterprises is legalized, whether or not this will go against such a policy remains to be seen.

Because of these reasons, possibly an acceptable approach that would benefit both foreign invested enterprises and the newly established securities trading center, while still well supporting the above-mentioned policy, would be to permit foreign invested enterprises to issue bonds. This would help the enterprises to raise more funds for business expansion where necessary, would provide the trading center with more commodities, and would not result in any new corporate form under which foreign investors could do business in Vietnam. More importantly, raising capital through the issuance of debt instruments would not go against the government policy of attracting more capital invested directly into the country from foreign investors.

6. Tax law

Tax policy has great impact in promoting the development of securities markets. In many countries, in the early stage of development of securities markets, listed companies can enjoy tax holidays and tax reductions.[656]

In Vietnam, to prepare for the birth of the securities market, a number of preferred policies have been adopted, including tax policy. Even before the time the first securities trading center was set up, various tax incentives had been offered to securities businesses under *Decision 39/2000*.[657] Pursuant to this Decision, securities firms have temporarily been given maximally preferred tax treatments aside from tax incentives provided for in other tax laws and ordinances. This shows the government's intention of promoting the development of securities business. Such favorable treatments include: (1) Value added tax:[658] this kind of tax is temporarily not being applied to legalized business activities[659] of securities firms within the 3 year period: 2000 - 2002; (2) Corporate income tax:[660] apart from enjoying tax incentives under the *Corporate Income Tax Act*, securities firms and fund management companies are entitled to one year of tax exemption and 50% tax reduction in the two following years.

Decision 39/2000 also offers favorable treatment to listed companies by giving them corporate income tax reduction. If a company has securities listed on the trading

[656] See Pham Quang Huyen, "Chinh sach thue doi voi su phat trien thi truong chung khoan" [Tax Policy and the Development of Securities Markets], (Oct. 2000) 20, *Thong tin tai chinh [Financial Bulletin]* 10, 10.
[657] The full name of this document is *Decision 39/2000/QD-TTg* dated 27 March 2000, issued by the Prime Minister (promulgating "The Temporary Regulation of Tax Incentives Enjoyed by Securities Businesses").
[658] See Art. 2.
[659] Pursuant to *Decree 48/1998*, Article 29.2, such activities are brokerage, dealings, management of investment portfolios, underwriting, and advising services on securities investment.
[660] See Art. 3.1.

floor for the first time, it can enjoy up to 50% tax reduction in the two years following the listed date.[661]

To channel investors into investment in the securities market, *Decision 39/2000* even offers tax incentives to securities investors. Securities investors are exempted from "tax on high income earners"[662] with respect to their dividends, and to interest derived from their shares and bonds, and with respect to the difference between the selling prices and purchase price of securities.[663]

It can be said that Vietnam has rather generous tax incentives applying to securities businesses and securities investors compared with those in other countries where tax exemption and reduction are merely offered in relation to direct tax. In Vietnam such favorable treatments can also be found in relation to indirect tax policy (i.e. the value added tax policy).

7. Civil law

Civil law usually covers various areas of socio-economic life including a number of aspects of securities and securities markets. It plays an important role in creating a favorable environment for the operation of securities markets in each country. In Vietnam, the current *Civil Code* that was enacted in 1995 contains a number of concepts that can be seen as a legal foundation for the securities regulation. However, at the time the *Civil Code* was drafted, neither a formal securities market nor a separate securities regulation had been available. Accordingly, discrepancies between the Code and *Decree 48/1998* are inevitable. Such discrepancies concern the concepts of asset, ownership of property, and contract for the custody of assets.

Article 172, the *Civil Code* says that: *"Asset includes tangible assets, money, papers that can be valued in cash and other rights over assets."* Apart from these, others cannot be deemed as assets under the *Civil Code*. However, the first paragraph, Article 2.1, *Decree 48/1998* states:

> *Securities are certificates or book-entry records evidencing rights and eligible interests of securities owners with respect to the assets or capital of the issuers. Securities shall include:*
> *a. Shares;*
> *b. Bonds;*
> *c. Securities investment fund certificates;*
> *d. Other types of securities.*

[661] See Art. 3.2

[662] This tax is similar to individual income tax in other countries but does not apply to every individual having income. It applies only to individuals who have a high income.

[663] See Art. 4.

So, pursuant to *Decree 48/1998*, the concept of securities is not confined to papers that can be valued in cash but also covers book-entry records which might be stored either as hard copies or in electronic databases. The concept of securities under *Decree 48/1998*, therefore, does not fall within the connotation of the concept of asset under the *Civil Code*.

Another problem occurs with the definition of contracts for the custody over assets. Article 562, the *Civil Code* defines:

> *A contract for asset custody is an agreement between parties, pursuant to which, the custodian receives property from the depositor to look after the asset and will return the property itself to the depositor at the completion of the contract. The property depositor will have to make a payment to the custodian except for transactions in which such a payment is not required.*

In practice, when the property in question is securities, the above-mentioned provision would appear to be difficult to implement, since securities are special commodities which are often put in circulation. Usually on completion of a contract, the custodian can only return securities that are in the same group and have the same value, but not exactly the same securities certificates received from the owner at the time the two parties entered the contract.

8. Criminal law

Criminal law also plays an important role in ensuring a transparent and healthy securities market. This is because the market is so susceptible to manipulative and deceptive practices, and in such a market, not only investors but also traders are quite likely to be cheated and misled.

The *Criminal Code* was first enacted in 1985 and has been revised many times - in 1989, 1991, 1992, and 1997. It was drafted during the time of the old economic management mechanism, the centrally planned economy, and although has been revised from time to time, the Code still does not reflect the new tendency of the economic renovation. In the year 2000, the new *Criminal Code* was passed; but no provisions on securities crimes were made. The reasons for this omission has been ascribed to the process of researching, drafting, debating and enacting the Bill. This was done a long time ago, when an organized securities market had not yet been set up. It was hard for the lawmakers to foresee the complex transactions that might arise in this special market.[664]

Recently, the first Securities Trading Center of Vietnam was put into operation, and in the near future some others may be established. In the absence of statutory provisions

[664] See Vu Nam, "Trach nhiem Hinh su trong linh vuc Chung khoan vat Thi truong chung khoan" [Criminal Liabilities in Securities and Securities Markets], (2000) 7 *Tin thi truong chung khoan [Securities Markets Bulletin]* 1, (Dec. 21, 2000), 1. Hereinafter, Vu Nam.

concerning securities crimes (for example, insider trading, market manipulation, misinformation) and corresponding sanctions in the *Criminal Code*; a too simple provision concerning administrative, disciplinary, civil and criminal sanctions stipulated in *Decree 48/1998*[665] might threaten the transparency and healthiness of the newly emerging market. Thus, it is essential that provisions regarding securities crimes be inserted in the current securities regulation so as to create a legal basis that might ensure the transparency and safety of the markets. For the time being, there is merely a governmental-level legal document, *Decree 22/2000*, that provides for *'Administrative Sanctions in the Field of Securities and Securities Markets'*.[666] Civil sanctions and criminal sanctions could either be provided for in separate legal documents or be inserted into *Decree 48/1998* while revising this Decree.

Some commentators believe that provisions concerning crimes on securities markets should be embodied in the *Criminal Code*.[667] However, it often takes time to alter a code, since, to do so, a formal law-making process by the legislature is required. Experience from abroad shows that the securities crimes as well as criminal sanctions need not be inserted in the criminal code. Rather they can be part of the securities regulation. That is, such provisions should be inserted in a legal document governing securities and securities markets such as the current *Decree 48/1998*. Both Japan and the US are good examples in this area. The Japan *Securities and Exchange Law*, although it was first passed in 1948, still now preserves an entire chapter, Chapter VIII, for "Penal Provisions" spreading throughout 13 Articles from Article 197 to Article 209. Concerning criminal prosecutions, the US has Section 24 of the *Securities Act of 1933* and Section 32 of the *Securities Exchange Act of 1934* dealing with penalties to be imposed on willful violators of securities law. Violators can be punished either by fine or imprisonment depending on the seriousness of the violations.

II. THE NEED FOR A SYNCHRONOUS IMPROVEMENT OF THE ABOVE-MENTIONED LAWS

In the first section of this Appendix, positive and negative aspects of the current laws concerning the operation of securities markets have been discussed. This discussion has revealed that the *Constitution* has created a relatively good legal foundation for the establishment of securities markets; and the current tax laws perform very well in promoting such markets. The discussion however, has also shown the need for

[665] This provision was discussed in depth in Chapter III of this paper while discussing "Statutory Sanctions for Violations".
[666] See *Decree 22/2000*.
[667] See Tao Huu Phung, "Mot so van de ve xay dung van ban phap ly cho TTCK" [A Number of Issues That Need to Take Into Account in Making Legal Rules Governing Securities Markets] (2001) 1, *Chung khoan Viet nam [Vietnam Securities]* 28, 30; see also Vu Nam, above n. 664, 1.

synchronous improvement of other laws, along with the revision of the securities regulation, in order to make possible a transparent, fair and effective securities market.

Apart from the discrepancies that need to be eliminated, among those laws and the securities regulation, each law has its own impact on the effectiveness of the securities market along a different dimension, so to speak; and all should be improved accordingly, as part of a comprehensive reform to achieve optimally operational securities markets in Vietnam.

Enterprise law is very closely connected with securities regulation, and thus many provisions of the enterprise law directly influence the market operation. A comprehensive set of disclosure requirements entrenched in the enterprise law would be useful for, and would beneficially support, public investors in making prudent investment decisions. An improvement of the regulation of the equitization of state enterprises is also required to speed up the equitization process, which in turn can enrich dealing commodities for the currently quiet securities trading center. Furthermore, to avoid difficulties in enforcing the regulation of equity ownership by foreigners in Vietnamese securities markets, the ambiguous guidelines concerning the adjustment of the proportion of shares a foreign investor can purchase from one issuer when such an issuer goes public should be clarified.

Banking law also has its impacts on the operation of securities markets. Commodities for stock trading centers are more or less subject to the participation of banks as listed companies on trading floor. The question of the overlap between the powers of the State Bank of Vietnam and the SSC in granting issuing licenses for issuers, should also be dealt with, so as to avoid difficulties in supervising and managing markets. Perhaps such a power should be vested in the SSC only, so that the SSC could administer the whole regulation of public issuance as part of the securities regulations; and for its part, the State Bank could well concentrate on administering banking law.

Foreign investment law is another legal source that needs to be taken into consideration in this context. With a serious shortage of commodities for trade on the trading floor at the present time, a legal basis on which foreign invested enterprises can issue bonds is required. In the long run, perhaps the privatization of foreign invested enterprises is another issue that should also be deliberated.

The *Civil Code*, as earlier mentioned, conflicts with *Decree 48/1998* in defining the concepts of asset, of property ownership, and of contract for the custody of assets. Such conflicts should be eliminated to ensure that these legal texts will be implemented without difficulties.

The need to improve the *Criminal Code* mainly concerns the newly emerging crimes on securities markets. The importance of criminal sanctions imposed on securities crimes was well evidenced in the discussions on sanctions for violations in Chapter III of this work. Criminal sanctions should have a place in either the securities regulations or in the *Criminal Code*. Wherever they be, attention should be made to the levels of sanctions. That is adequate sanctions should be laid down for individual types of violation to ensure that such sanctions are truly effected in regard to the behavior of market participants.

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