New Draft Decree on Investment in Start-Ups

Recent developments

The Ministry of Planning and Investment ("MPI") is drafting a decree to regulate investment in innovative start-ups ("Draft Decree"), which is expected to create a legal framework for funding start-ups as well as policies to promote and support this type of investment activity in Vietnam. The first draft of this new decree is now open for public comments on the MPI’s website.

In particular, the Draft Decree (i) stipulates the investment vehicles (i.e. venture capital funds and venture capital firms) that can provide funding to start-ups and (ii) sets out conditions to establish and operate a venture capital fund or a venture capital firm.

We set out the key points of the Draft Decree below.

Two Investment Vehicles for Venture Capital Funding

Under the Draft Decree, venture capital funding can take the form of one of the following investment vehicles:

(i) Venture capital funds ("VC Funds"); or

(ii) Venture capital firms ("VC Firms").

VC Funds and VC Firms are defined as funds and companies that are established for the purpose of making investments in innovative start-ups. Both investment vehicles will be entitled to preferential treatment in terms of corporate income tax in accordance with the law on corporate income tax.

Both local and foreign investors are allowed to contribute capital into VC Funds and VC Firms. No foreign ownership limitation is currently imposed on VC Funds and VC Firms. However, the Draft Decree generally provides that "VC Funds and VC Firms having foreign investors must, during its course of investment, comply with relevant laws on foreign ownership limitation." This requirement suggests that VC Funds or VC Firms which are majority owned by foreign investors may be subject to certain market access restrictions/conditions if the target start-up operates in protected sectors.

Qualified Investors

In order to invest in a VC Fund or a VC Firm, investors must meet the following financial requirements (thereafter they will be considered a "Qualified Investor"):

(i) For individuals:

- have an average annual income of at least VND200 million (approximately US$8,800) in the two most recent years; or
- have total assets (including his/her spouse's assets) after deducting all liabilities (including his/her spouse's liabilities) of at least VND500 million (approximately US$22,000).

(ii) For institutional investors: have total assets of at least VND1 billion (approximately US$44,000) recorded in their latest financial statement.

**VC Funds - Conditions for establishment and operation**

VC Funds are subject to the following establishment and operation conditions:

<table>
<thead>
<tr>
<th>Phase</th>
<th>Conditions</th>
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<tbody>
<tr>
<td>Establishment of a VC Fund</td>
<td>(i) Total capital contribution must be at least VND1 billion (approximately US$44,000) and contributed in cash.</td>
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<td>(ii) The maximum number of capital contributors is 30 and all contributors must be Qualified Investors.</td>
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<td>(iii) A VC Fund's name must begin with “Venture Capital Fund.”</td>
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<td>(iv) The Charter of a VC Fund must include the following statement:</td>
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<td>&quot;This fund aims to invest in innovative start-ups. The investment in this fund is only suitable for investors who are willing to accept the high level of risk arising from the fund's investment. Investors of this fund need to carefully consider before making capital contribution and investment decision.”</td>
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<td>(v) A VC Fund’s assets will be deposited at an independent custodian bank. A VC Fund’s assets belong to the participating investors in proportion to their capital contribution ratios and will not be considered assets of the fund management company or the custodian bank. The fund management company may only use the VC Fund’s assets to fulfill payment obligations of VC Funds.</td>
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<td>(vi) State authorities are not allowed to make capital contribution into a VC Fund. Credit institutions, insurance companies and State-owned companies must comply with specialized laws when making capital contributions into a VC Fund.</td>
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**Establishment Procedures**

In order to establish a VC Fund, the fund management company or the VC Fund's director will prepare and submit an application dossier to the State Securities Commission ("SSC"). Within 15 days of receiving a complete and valid application dossier, the SSC will issue written confirmation on the establishment of said VC Fund. In the event of refusal, the SSC will respond in writing and specify its reasons.

**Operation of a VC Fund**

A VC Fund's operation must comply with the following conditions:
Phase | Conditions
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(i) | A VC Fund is only permitted to invest in innovative start-ups that have not made any public offers.
(ii) | A VC Fund can only hold up to 50% of a start-up's charter capital.
(iii) | The fund management company or a VC Fund's director must prepare said VC Fund’s internal investment rules, comprising the following:
   - a process to evaluate start-ups;
   - guidance to determine the value of start-ups;
   - a process to supervise and divest capital from start-ups; and
   - methods to identify the assets of a VC Fund and the assets of each investor.
(iv) | A VC Fund is not permitted to:
   - make capital contributions into any other VC Firm, securities company, VC Fund or securities investment fund;
   - invest in real estate businesses; or
   - use the VC Fund's capital and assets to give out loans or guarantee for loans to any third party.

VC Firms - Conditions for establishment and operation

VC Firms are subject to the following establishment and operation conditions:

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<th>Phase</th>
<th>Conditions</th>
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| Establishment of a VC Firm | (i) Charter capital must be at least VND500 million (approximately US$22,000) and contributed in cash.  
(ii) The maximum number of capital contributors is 30 and all contributors must be Qualified Investors;  
(iii) In addition to other requirements under the Enterprise Law,¹ a VC Firm’s name must begin with "Venture Capital";  
(iv) The Charter of a VC Firm must include the following statement:  "This company aims to invest in innovative start-ups. The capital contribution to establish this company is only suitable for investors who are willing to accept the high level of risk arising from the company's investment. Members / Shareholders need to carefully consider before making capital investments." |

¹ Enterprise Law No. 68/2014/QH13 adopted by the National Assembly on 26 November 2014 ("Enterprise Law").
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<td>(v)</td>
<td>VC Firm legal representatives must satisfy the following requirements:</td>
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<td>• have at least three (3) years of experience working as a manager or holding positions relating to investment activities at financial, banking or insurance organizations or in the accounting, finance or investment departments of other enterprises;</td>
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<td>• not concurrently being a legal representative of another company; and</td>
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<td>• have never been prosecuted or convicted, whether inside or outside Vietnam, of fraud, corruption, abuse of trust or any other crime relating to dishonesty.</td>
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**Establishment Procedures**
The establishment of a VC Firm will follow the procedures set out under the Enterprise Law.

**Operation of a VC Firm**
A VC Firm's operation must comply with the following conditions:

(i) A VC Firm is only permitted to invest in innovative start-ups that have not made any public offers;

(ii) A VC Firm can only hold up to 50% of a start-up’s charter capital; and

(iii) A VC Firm must prepare internal investment rules, comprising of the following:

• process to evaluate start-ups;
• guidance to determine the value of start-ups; and
• process to supervise and divest capital from start-ups;

(iv) VC Firms are not permitted to:

• make capital contributions to any other VC Firm, securities company, VC Funds or securities investment funds;
• invest in real estate businesses;
• take out loans in any form; or
• use the VC Firm’s capital and assets to give out loans or guarantees for loans to any third party.

**Right to transfer**
Investors of a VC Fund have the right to freely transfer capital contributions to a third party provided that (i) the transferee is a Qualified Investor and (ii) after the transfer, the VC Fund still maintains and satisfies all establishment conditions. Within 15 days after closing the transaction, the fund...
management company or the VC Fund's director must submit the following documents to the SSC:

(i) notification on the transfer of capital contribution, specifying the information of the relevant parties, the ownership ratio of each party (before and after closing) and the value of the transaction; and

(ii) a copy of the transfer agreement between the parties as certified by the fund management company or the VC Fund's director.

As for VC Firms, this Draft Decree is silent on the investors' right to transfer. In our view, VC Firm investors should be entitled to all the rights of members/shareholders as stipulated in the Enterprise Law, including the right to transfer their equity interests. The conditions and procedures for such transfer will, in such a case, follow the Enterprise Law and other laws on investment (if applicable).