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Forecast for Vietnam's Foreign Investment Policies in 2013

Foreign direct investment (FDI) in Vietnam has dropped sharply in recent years. After peaking in 2008 at a record high of USD 64 billion, registered FDI capital fell to approximately USD 13 billion in 2012. In a country where FDI plays an important role for growth, a dramatic decrease in FDI undoubtedly raises concerns for the Vietnamese central government.

Further headaches are caused by the so-called "evil phenomena" allegedly brought by FDI enterprises: questionable losses recorded on the books, tax-dodging transfer pricing, and heavy reliance on loan capital (both offshore and onshore loans). An article in the *Saigon Times* reported that about 50 percent of all FDI enterprises in Ho Chi Minh City have declared losses for four consecutive years. In 2011, the reported losses were 3.5 times higher than in 2010. However, upon inspection by the authorities, such losses appeared to be forged. In fact, the authorities claimed such losses were linked to transfer pricing practices of FDI enterprises.

Thus, it seems the government of Vietnam faces a dilemma. On the one hand, it needs to regain the trust of foreign investors reinvesting into Vietnam. On the other hand, it needs to curb the perceived "evil practices" of FDI enterprises. In tackling these issues, the Prime Minister of Vietnam issued Decision No. 1601/QD-TTg dated October 29, 2012 (Decision 1601) on his approval of the plans to enhance the management of FDI capital in Vietnam, including investment incentives and state control plans. Though Decision 1601 has set these changes in motion, further instructions and clarifications will be necessary in 2013.

Plans for Boosting FDI

Regrettably, Decision 1601 fails to give any specific solutions for encouraging the return of FDI capital to Vietnam. It generally states that the country needs to improve its investment environment and the effectiveness of FDI in Vietnam to align with other goals for economic stability and growth of the country. The most visible action is, perhaps, the requirement for governmental agencies to make a clear definition of FDI and foreign indirect investment (FII) which, the government asserts, will help improve the legal system regarding FDI and FII (and consequently clear the legal procedures for investment by foreign investors). This action is unlikely to bring about any real incentives for FDI, as the decrease in FDI is due mainly to burdensome administrative procedures and corruption issues (in addition to macroeconomic factors), rather than the distinction between FDI and FII.

The Ministry of Planning and Investment is reportedly drafting a proposed plan for enhancing the attraction, use, and management of FDI for the period of 2011–2020. However, it is not yet publicly known if this plan contains any clear government policies for attracting FDI back to Vietnam.

Plans for State Controls over FDI

While incentives for FDI are opaque, the state controls over this area are quite visible, with the following key control measures that the government is likely to impose on FDI enterprises in the near future.

Stricter control over the loan capital of FDI enterprises

If the loan capital of FDI enterprises in Vietnam makes up a high percentage of their investment capital structure (constituted of equity capital and loan capital), it may cause problems related to:

- Transfer pricing (via the payment of high-interest amounts for loans granted by the foreign parent to the Vietnam-based subsidiary)
- Capital flight (via the possible sudden withdrawal of foreign loans, causing the national foreign reserve to collapse)
- Abuse of domestic loans (via loans borrowed from local banks that undermine the meaning of foreign investment)

Thus, the State Bank of Vietnam (SBV) may impose further restrictions on the borrowing of money by FDI enterprises. In particular, the licensing body may reject the incorporation of an FDI enterprise that is thinly capitalized.

In addition, further conditions may be added, such as a minimum ratio between the equity capital and loan capital of an FDI enterprise.

Control over capital contribution

The government will revise the law on the inflow and outflow of money of FDI enterprises, including the provisions on:

- Which assets constitute FDI capital
- The time of contribution of equity by foreign investors
- Which expenses, incurred by a foreign investor before the issuance of the FDI project license, will be calculated as capital contribution

Examination and oversight of FDI projects

The Vietnamese government is also likely to tighten the management of FDI projects. In particular, Decision 1601 provides for regular and sudden examination of the contribution of equity, remittance of profits, and even payment transactions of FDI enterprises by authorities such as the SBV.

In addition, the Ministry of Planning and Investment (MPI) is drafting a circular stipulating the examination and oversight of FDI projects in Vietnam. Under this draft circular, state agencies may conduct regular or sudden examination and oversight of the implementation of FDI projects by foreign investors. The list of competent agencies includes the MPI, other ministerial-level agencies (such as the SBV and other ministries), the people's committee, and the MPI branch of the city or province where an FDI project is located. The scope of examination and oversight is broad. It covers the legal compliance of FDI enterprises, their commitments to the government, and the actual implementation of their projects.

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