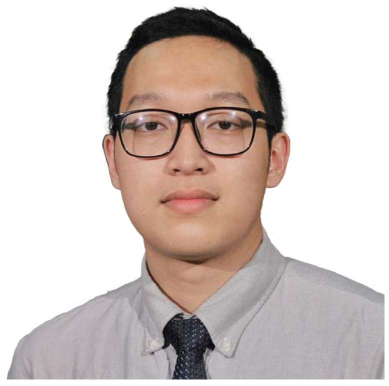
Intricacies of foreign exchange in M&A

Mergers and acquisitions have been emerging as an attractive channel for international investors in Vietnam. However, some barriers are restricting foreign investors from entering shared sales and purchase agreements with Vietnamese enterprises. **Le Gia Khanh** and **Nguyen Van Hai Dang** from law firm NHQuang & Associates analyse the restrictions and how Vietnam can welcome more foreign funds.



Corporation A is duly organised and exists under the laws of the United States. Company B is a company duly organised and exists under the laws of Singapore. The latter has invested in several countries, including Vietnam, where company B has cooperated with several Vietnamese investors to set up another enterprise, called company T, in which company B is the major shareholder with 90 per cent of the shares.

Meanwhile, corporation A aims to acquire company B, including its businesses worldwide. Accordingly, in Vietnam, corporation A plans to acquire all capital of company T, making it its sole owner. Corporate A negotiates with Vietnamese shareholders to buy their shares via a vehicle of company B as an existing shareholder of company T.

The M&A transaction is structured and conducted through two agreements – a shares purchase agreement between corporation A and company B (known as an overseas contract); and a share purchase agreement between company B and Vietnamese shareholders (domestic contract).

The transfer price of the whole transaction is quoted in US dollar. However, the parties must deal with Vietnamese regulations on foreign exchange where it requires them to negotiate the shares in VND, without any reference to foreign exchange of currency. This is potentially causing a different value or an inconsistency between the overseas M&A contract and the domestic one.

Strict regulations on foreign exchange

The Amended Ordinance on Foreign Exchange 2013 provides that, "Within the territory of Vietnam, all transactions, payments, listings, advertisements, quotations, valuations, price quoting in contracts, agreements, and other forms of transactions of residents and non-residents must not be expressed in foreign currency except for cases permitted following the regulations of the State Bank of Vietnam (SBV)."

Quoting VND with the equivalent foreign currency is also not allowed under legislation on foreign exchange. Via Circular No.32/2013/TT-NHNN, the SBV provides circumstances that allow the use of foreign exchange in the territory of Vietnam but does not mention any case of foreign investors purchasing shares of Vietnamese companies.

To reinforce these strict regulations on the use of foreign currency in Vietnam, Circular No.06/2019/TT-NHNN of the SBV provides that the "valuation and payment for the transfer of investment capital and investment projects between a resident and a non-resident shall be made in VND."

However, the regulation is ambiguous due to unclear stipulation on whether the "listing, quotation, price quoting in contracts" of the transaction can be made in foreign currency. In our example cross-border merger and acquisition (M&A) transaction, both companies did not risk denominating in US dollar in the contract, but in VND, for the share sale and purchase agreements in company T.

Rights of investors

According to the Law on Investment 2005, 2014, and 2020, foreign investors have the right to transfer funds into Vietnam via capital contribution or by purchasing shares in ongoing companies. They can use cash and assets for their investment, and there is no prohibition for foreign currency from investment legislation when the financing is made for implementing their planned project.

Moreover, the prescribed forms for investment registration procedures also require the investors to provide information related to the value of the capital in VND and the equivalent in a foreign currency. Some provincial departments request the applicants to provide certain information relating to the value of the investment capital in US dollar for statistical purposes.

When investing to establish a new economic organisation, foreign financiers do not face any obstacles from foreign exchange regulations. They can invest in foreign currency and the registration certificates recognise both their investments in VND at the rate determined by the investor at the time of the application submission and in the equivalent value of a foreign currency.

If there is an exchange rate difference between the time of submission and the time of transferring the investment, the investors are entitled to record such difference in their accounting system. Commercial banks within Vietnam will then allow the disbursement of the amount that investors transferred in accordance with the investment certificate.

For investments through the acquisition of capital, equity interests or shares of an existing company, the investment shall be made in the same form as the establishment of a new economic organisation if the share sale and purchase agreement is denominated in foreign currency or VND with the equivalent value in foreign currency.

In case the share sale and purchase agreement are quoted only in VND, the investment registration certificate also has only that one currency. It will be difficult for a foreign investor to arrange VND funds or an amount of foreign currency to fit with the value in VND.

If exchange rates between the time of application submission and the time of investment disbursement changes, the foreign investor and the Vietnamese party must sign an additional agreement to recognise the actual amount of VND in the direct investment capital account. However, signing an additional agreement is sometimes not that simple for large and listed companies.

How to welcome big eagles

An investment trend of large companies is to acquire ongoing companies via the purchase of shares or other kinds of capital. This form of investment assists large companies in gaining access to the market quickly. Restricting foreign investors from entering share sale and purchase agreements with Vietnamese enterprises in terms of foreign currencies presents difficulties for them to invest in Vietnam.

The current regulations restricting parties denominating foreign currency in the share sale and purchase agreement cause difficulties in investment procedures but also in drafting and enforcing agreements. Foreign investors, when deciding to invest, must decide on the currency which they use in their financial accounting system. The use of another currency requires the conversion value.

To ensure consistency, companies want the value stated in their investment decision or announcement to be consistent with the value stated in the contract and related permits. This demand requires regulations on foreign exchange management for capital contribution and share purchase in Vietnam to facilitate.■

Photo: Le Toan

Current regulations restrict parties denominating foreign currency in M&A agreements