

BUSINESS ISSUES BULLETIN

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THE REVISED DRAFT LAND LAW Implications for the Business Community

In the 10 years following its enactment in 1993, the Land Law has been revised twice in 1998 and 2001, and is currently undergoing its third revision; this revision is considered to be the most comprehensive attempt to bring the Law more in line with the practical requirements of a market-oriented economy while clarifying and strengthening the State's role in managing land resources. There are ongoing debates as to how the Law should be revised among various circles, due to its extensive impact on business activities as well as citizens' lives in general. Below is a summary of the major changes between the current Law and the proposed draft Law and their potential impact on business activities.

Mechanisms to determine the price of Land-Use Rights (LUR). Under the current Land Law, the prices of LUR are determined solely by the State. The revised draft Law allows for application of additional market-oriented measures to determine prices of LUR, including auction, competitive bidding, valuation by an external consultant, etc. On one hand, this is considered a positive development by the business community, as it creates a flexible legal framework in which the market rules of supply and demand apply to property transactions. On the other hand, it raises concerns among businesspeople in terms of how these different pricing mechanisms will be applied, and whether they will be consistent and fair. For example, the price that a company pays for LUR to the State through auction or competitive bidding or to individual transferors is the market price; however, if the company uses its LUR in a business transaction such as capital contribution in a joint-venture, as mortgage or as collateral, the price can be determined by the State framework, which might be significantly lower than the market price.

Ownership of land. The draft Land Law re-confirms public ownership of land, and the role of the State as the representative with the ultimate authority to dispose of and benefit from land. There is ongoing debate regarding this issue of ownership. There are some who argue that since the State recognizes a LUR owner's right to transfer land, lease it to another party and contribute it as capital for a joint venture, etc., in essence, this means that the State recognizes private ownership of land; thus contradicting the stipulation on public ownership of land. Others argue that the issue of public or State ownership is not the core problem, and that debating this point will not resolve the land issues in Vietnam. In a discussion forum on the draft Land Law, several participants stated that the core problems that need to be resolved are poor land planning and administration, and the lack of a thorough research effort to understand land issues (VNExpress 15 August 2003).

Authority of land planning, allocation, leasing and pricing. Under the current Law, the

power to allocate and lease LUR belongs to provincial authorities. Under the new draft Law, the authority to allocate and lease land to households and individuals is delegated to the lower level of administration [i.e. district, town or provincial-level city], but for businesses, that authority still remains at the province or central-level city. This new delegation of authority gives local government more power to decide on investment projects in their localities; however, it does raise the question as to whether the stipulation will hinder business growth, as some businesses may purposely remain small and informal (e.g. choose to remain household businesses rather than registering as companies) in order to gain easier access to LUR.

Under the draft Law, Provincial People's Committees are authorized to annually determine a pricing structure for LUR in their own province (based on the Central Government's framework). On one hand, this stipulation provides local authorities with flexibility in setting LUR prices to attract and encourage investment. On the other hand, it raises the question that if land prices are subject to change every year and can differ greatly between provinces, will businesses that have made long-term investments in infrastructure on land in particular provinces be at risk?

Rights of land-users under different leasehold terms. The draft Law stipulates that land-users who rent land on an annual basis will no longer have the right to transfer, sub lease, mortgage or contribute the LUR as capital, etc., whereas land-users who have been allocated land [and have paid a land-use fee] continue to have these rights. How will businesses that currently pay rent on an annual basis be affected if they lose these rights? Will those who have bought or inherited properties on short-term leasehold land be guaranteed first priority to continue renting from the State? If so, what will the rental price be? Moreover, the draft Law requires businesses that want to acquire LUR through allocation to pay the land-use fee up-front and in-full, which will certainly increase initial investment costs for all businesses. Will smaller businesses that do not have the capital to pay up-front be disproportionately disadvantaged?

Repossession of land by the State. The draft Law stipulates land will be repossessed if a proposed investment project does not put the land into use within 12 months of the date of allocation/lease approval, or falls over 24 months behind the original implementation schedule. Although the purpose of this stipulation could be to minimize the possibility of businesses speculating on land rather than using it for productive purposes, it also creates concern among businesses because there may be unavoidable delays in project implementation, businesses will lose a lot of the money they have invested for the LUR and on the land itself if the land is repossessed.

Capital gains tax on transfer of LUR. This tax will replace the current LUR transfer tax, and seems to be intended to reduce land speculation and increase the State's tax revenues. Businesses are justifiably concerned about the specific rate of this tax (which is not stipulated in the draft Law) and how the Tax Authority will determine the transfer price upon which the tax will be calculated.



The "Business Issues Bulletin" provides those interested in business issues with a short summary and analysis of a particular topic affecting the business environment in Vietnam, and exposure to different opinions held by various stakeholders on the topic.

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Mechanisms to determine pricing of Land Use Rights (LUR)

The draft Land Law allows for more market-oriented measures to determine the pricing of LUR, such as auction, bidding, self-determination and registration, etc. This being the case, why does the stipulation that the State determines land price still remain? Would this result in inconsistent implementation; for example land users pay land-use fees to the State based on market prices, but the State compensates land users at the State's determined price in the case of repossession? In addition, does the new stipulation that allows for all parties to negotiate and agree upon a price for the transfer of LUR create difficulties for State authorities in land repossession and site compensation for investment projects?



- The principle that the State determines land prices remains [in the new draft Law] in order to facilitate uniform government land administration. Also, when land price is not determined by measures such as auction and bidding, etc. the State regulated price will be applied. The draft Law stipulates that the State determines land price, but [I think] that price should be close to the market price. The allocation of land accompanied by the collection of land-use fees and land confiscation will utilize the same pricing mechanism. The stipulation that allows for negotiation on transfer price will benefit investors, especially SMEs, as it allows them to negotiate directly on LUR transfer prices, and to clear land for project implementation on their own, as long as the land is used for its approved purpose and is consistent with the State's land planning regulations. The State will only focus on site clearance for large investment projects.

◀ *His Excellency Dang Hung Vo - Vice Minister of Natural Resources and Environment, Member of the Land Law Drafting Committee*

- For businesses, I believe that the most transparent and fair way to determine land price is through auction or bidding, so I very much welcome this new stipulation [in the Law]. What's important is that the implementation of auction and bidding is serious and transparent, so as to ensure fair results.

Mrs. Ngo Thuy Hoa - Director, Thai Hoa Tea Company

Stipulations on ownership of land

The Law allows for transfer of land-use rights, and the draft Law accepts market rules in determining land price. Are these stipulations in conflict with the principle that land is publicly-owned?



- The root cause of many of the problematic issues relating to land law in Vietnam is the fact that notwithstanding the transition towards a more market-oriented economy in Vietnam, land is still considered as being administered/managed by the State on behalf of the people. This leads to a confused system of legal ownership of land and an unsatisfactory position with regard to the title to land. This conceptual problem results in confusion and has hindered the development of anything like a real property market in Vietnam. The government may consider addressing this by reducing the many distinctions between different types of land

holding in Vietnam, for example land allocation with or without payment of fees, land leases etc., and the varying rights pertaining to such land holdings. One can compare the confused system in Vietnam with the concept of land ownership in Hong Kong, for example, where although there is no outright freehold ownership of land, there is a simple system of leasehold title under which it is clear exactly what title you hold to land, for how long and for what purpose the land in question may be used. This provides the certainty that investors are looking for without the need to provide for outright freehold ownership of land.

Mr. John Hickin - Solicitor, Johnson Stokes & Master, Chairman of the British Business Group in Hanoi and Participant of the Property and Tourism sub-working group of the Vietnam Business Forum



- I think the State should recognize private land ownership, because in practice as well as in many legal stipulations, the State has already recognized many of the concepts of private land ownership, such as the right to transfer LUR, dispose of [LUR], or sell land through auction, etc. Therefore, the State might as well officially recognize private-ownership of land sooner rather than later.

Mr. Le Anh Tu - Director, Le Hiep Imexco Co. Ltd, Power Tube Manufacturing Factory

- It should be noted that the allocation of land by the State is accompanied by conditions related to the purpose and length of use, thus the transfer of LUR should maintain these conditions. In addition, "auction" should be understood not as the auction of land, but the auction of LUR with certain conditions; these are conditions related to the land, not related to the market. Therefore, there is no conflict between the concept of public-ownership of land versus the application of market tools and rules for economic development.

Vice Minister Dang Hung Vo

Rights of land users under different leasehold terms



- I think the stipulation that gives more rights to the land-user who is allocated land and pays a land-use fee compared to the land-user who rents land on an annual basis is fair, because in the former case, the land-user has to pay the entire fee up front for the entire lease period. The lease price in this case should be lower than, or at most equal to, the land-user who leases land annually. This way, businesses will be able to choose the type of leasehold they prefer, based on their own cash flow. Personally, I prefer land

allocation and paying the entire fee up-front; I just include that amount into calculating my initial investment, and then am able to proceed with my long-term investment plans with confidence. The State also benefits because it receives money quickly and can make long-term land plans.

Mrs. Ha Thi Vinh Director of Quang Vinh Ceramics Co. Ltd. (Simco)



- Both the current Law and the revised draft Law make stipulations on the various types of land allocation and land lease, with various rights and conditions attached. These stipulations are too complicated [to understand], even for government officials, and therefore create room for corruption in implementation. The State should consider adopting land lease as the single way for businesses to obtain land, and lessees in all cases should have the same rights with

regard to the land. In [remote] regions where there are economic development issues to consider, the State could adjust lease prices accordingly; for example, the rental price for agricultural land could be subsidized or even be nil [in remote areas].

Dr. Le Xuan Ba Vice Director, Central Institute of Economic Management

- **Position Paper on Land and Tourism submitted by the Land and Tourism Sub-group to the Vietnam Business Forum, June 2003:** All land users should have the same rights because even for those paying rent annually, if they sublease or contribute LURS as assets, the price would be adjusted by the parties in any case to take into consideration the annual rental.

Land-lease tenure



● The first major land-related issue for investors in industrial zones and export processing zones which we would like the draft Law to address is that of land-lease tenure. Investors in infrastructure development for EPZs and IZs are allocated land or given the right to lease land for a specific time period, usually 50 years. When these investors sub-lease land to [manufacturing] businesses that then build factories on the land, the maximum term of this lease can only be for the remaining period of the original lease, for example 35 or 40 years. However, the manufacturing businesses may have operating licenses that are valid for longer than [the 35 or 40 years], and are not guaranteed they will be able to continue leasing the land for the remainder of the validity of their operating license. In addition, this time gap creates difficulties in the calculation and payment of the rent.

◀ *Dr. Le Thai Hy - Head of Administrative Department of the Ho Chi Minh City Export Processing & Industrial Zones Authority ("HEPZA")*

● The State should allow longer land-lease tenures for foreign investors. Currently foreign investors are allowed to operate a business for 30 to 40 years on average, after which they have to transfer the infrastructure and facilities to the Vietnamese partner. In the real estate business, many joint ventures don't see a profit until this time period [of 30 to 40 years] is up.

Mr. Lai Boon Tuck - Director, Grand Horizon Joint Venture

● The Law allows a maximum land-lease tenure of 50 years, and we applied for a 50-year lease, but only got approval for a 30-year lease. At present, the specific regulations on lease-tenure are not clear. For a [manufacturing] business, a term of 30 years is too short. A short lease-term causes businesses to shy away from making large investments, speeds up depreciation which increases production costs, and reduces competitiveness; businesses are not comfortable to make long-term investments.

Mrs. Ngo Thuy Hoa



Site clearance costs and rent

● The other issue of concern for investors in EPZs and IZs is the fact that site clearance and compensation to displaced households is both time-consuming and expensive, which results in higher rents, affecting the overall business environment. Furthermore, because it is so expensive to clear land and compensate households, there is not enough money left to invest in necessary infrastructure, such as a good waste-water treatment system, plants and greenery, environmental protection...as a result, the quality of infrastructure of EPZs and IZs is very poor. We strongly believe that it should be the State's role to manage land planning and site clearance, so that businesses can focus on infrastructure investment, and the Law should address this thoroughly. [The State should also] make a distinction between true infrastructure developers and [short-term] real estate investors, and more favorable incentives should be given to infrastructure developers, which would help create a better investment environment.

Dr. Le Thai Hy

● Under current regulations, businesses incur many costs in addition to rent on land, such as compensation for site clearance, fees for changing land-use purpose, providing employment to displaced farmers, etc. that are unknown at the outset, making it impossible for a business to determine accurate total investment costs at the outset. There should be a way to price rent so that it accounts for these other costs, so that businesses can accurately estimate their costs.

Mrs. Ha Thi Vinh

Land planning, allocation, lease, pricing and LUR revocation



● The revocation of LUR (where land is not put into use within 12 months or the project's progress is more than 24 months behind schedule) may be appropriate for the objective of minimizing land speculation, but is inappropriate from a legal perspective. It is using an administrative measure to negate a legally accepted contractual agreement. For example, if an investor pays land-lease rental for 10 or 20 years, he should have the right to mortgage this land leasehold, and bankers should be legally allowed to take it as a mortgaged asset. When the State repossesses the land, how will the investor be compensated? And how will bankers' rights be protected?

Mr. Nguyen Duc Vinh - Chief Executive Officer, Techcombank

● The stipulation to revoke LUR (of land) that is not utilized within 12 months or where investment plans are delayed over 24 months is appropriate, because in practice a number of both local and foreign-owned businesses apply for land [to speculate] and sell rather than for actual manufacturing or investment purposes. There has been a lot of talk about how we expect transparency and honesty on the part of government officials, we should also talk about expecting integrity on the part of businesses. The only thing the draft Law still lacks [with regard to the issue of repossession] is clarification on how businesses that have already paid rent or land-use fees up-front would be compensated.

Dr. Le Xuan Ba

● I agree that the authority to allocate and lease land to businesses should lie at the provincial or city level, because management ability is still limited at the local [district and commune] level, not to mention the prevalence of corruption [at this level] is still high. What's most important is the strict and timely implementation of the decision that is made. Take my company's case as an example - we applied to lease land in Hung Yen province near our head office, and got approval quickly from the provincial authority. But it's been almost two years now, and the district and commune authorities have not yet implemented this decision, and we still have not been able access land for production [in Hung Yen province]. When we applied to lease land in Quang Ninh province, it was also approved quickly at the provincial level, and only five months later, we were able to access land and start our investment project.

Mrs. Ha Thi Vinh

Capital-gains tax

● I appreciate that the aim of this new tax is to reduce land speculation, which I think is good. However, how this tax is applied in practice needs to take into account the nature of the banking business. The primary objective of bankers when taking LUR as collateral is to have recourse in case the debtor defaults. Therefore, if a bank sells mortgaged land, the money from the sale would need to cover both the principal and interest owed on the loan, and only any profit on top of the recovered principal plus interest should be subject to capital-gains tax.

Mr. Nguyen Duc Vinh

Other specific recommendations

● With regard to land administration and land allocation and leasing, I believe the most business-friendly method would be a "one-stop shop" operated by a consulting or service company under the Department of Planning and Investment. Several provinces including Hung Yen and Phu Tho have adopted this method, and it is quite convenient for businesses. This idea should be replicated throughout the country.

Mr. Le Anh Tu

● Through the Vietnam Business Forum I have been involved in reviewing and making recommendations on the draft Land Law to the Government of Vietnam, and in general terms believe that the government has made some progress in improving the system of land legislation and the question of land administration. One recent specific example is the introduction of Circular No. 03/2003/TTLB/BTP-BTNMT jointly issued by the Ministry of Natural Resources and Environment and the Ministry of Justice on July 4, 2003, providing guidelines for the procedure and order for registering and providing information about mortgages and guarantees by way of land-use rights and/or assets attached to land. However, there are a number of fundamental issues of serious concern to investors that are not addressed by the revised draft Law. One of the main problems in Vietnam lies in the inconsistent and unpredictable application of the land law and its system of implementing regulations, which creates a business environment that is neither stable nor predictable. There are still too many inconsistencies in policy that plague land matters, as well as too many different ways to interpret and apply the various legal documents concerning land in Vietnam. The position would be improved dramatically if there were to be a more consistent and coherent body of law on land issues, and a single government agency in charge of land administration, unlike at present, where many different agencies and organizations including the Ministry of Natural Resources and Environment, People's Committees in each locality, etc. have responsibility and authority in land matters.

Mr. John Hickin

● The Draft Law lacks a stipulation on a statute of limitations for the State's land-use plans. Land plans are often announced but then not implemented for a long time, which makes it difficult for businesses and individuals who want to make investments to do so confidently. The Draft Law needs to specifically address this issue.

Mr. Le Quang Minh, National Assembly Delegate Can Tho Province

● The revised draft Land Law seems to have the immediate objective of cooling down the land fever; this phenomenon on one hand is not ideal, but on the other hand, it reflects the reality of the market. What is most important is that this Law affects almost every type of economic transaction, especially banking transactions. Approximately 40% of Techcombank's transactions are related to guarantee and mortgage of land-related rights and assets attached to land; this figure could be even higher in other banks. With the increasing development of new banking products and services such as mortgage lending, this ratio is likely to increase (elsewhere in the world, this ratio normally ranges from 50-60%). Therefore, lawmakers should think carefully about achieving an immediate objective at the expense of negatively affecting the much more important and larger business environment, or as we normally say, "killing the rat [but] breaking the jar in the process." An unstable business environment not only impacts foreign direct investment, but is also very bad for local businesses.

In my opinion, from a banking perspective, the top three issues that need immediate resolution in the legal framework pertaining to land-related transactions are: 1) the unclear legal definition of land-ownership and land-use rights, which results in the limited volume of land that can legally be utilized in economic transactions; 2) the fact that implementation of laws and regulations are poorly coordinated and inconsistent between ministries and localities; and 3) the implementation and enforcement of legal decisions is poor and therefore fails to provide confidence and security, especially for bankers and creditors.

Mr. Nguyen Duc Vinh

Other changes that positively affect business environment...

The draft Law also contains new stipulations that may help promote a healthy real estate market and create a better business environment, including:

- Regular periodic public announcement of State land-use plans and prices;
- Land that is used for infrastructure purposes in industrial zones will not be charged a land-use fee;
- More businesses will be able to apply for land allocation from the State. The current Law only allows businesses operating in infrastructure and residential construction projects to be allocated land; companies in other sectors must lease land. The revised draft Law allows for businesses of all types to choose between applying for land allocation [and paying a land-use fee] or leasing land on an annual basis.
- The revised Draft Law allows foreigners and overseas Vietnamese who have invested in Vietnam or who intend to reside long-term in Vietnam to obtain land-use rights or lease rights on terms and conditions that are almost on par with Vietnamese businesses.
- The limits on the amount of land for agricultural purposes that an individual or company may lease (in excess of allocated land) are lifted in the new draft Law. This new stipulation enables businesses and individuals to operate large agricultural and farming businesses.

Reference Information

The full text of the revised draft Land Law and the National Assembly's plan to gather feedback and recommendations was published on the 1 August 2003 issue of Nhan Dan (People) newspaper. Any individual or institution can send comments on the revised draft Land Law to the National Assembly Office at 37 Hung Vuong St., Hanoi, before 20 September 2003.

Feedback

What are your views? We welcome your comments and feedback. If you would like to comment on this Bulletin, suggest topics of future issues or request additional copies, please fill in this form and send it to: (or directly contact us at either of the addresses below)

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