

# Recommendation

## 4 CHAPTER

### 1. Overview

Based on the survey findings outlined in the previous sections of this report, we conclude with some policy-oriented recommendations to promote better corporate governance practices in Vietnam. These are broadly divided into regulatory and non-regulatory proposals. Before doing so, however, it should be recognized that the concept of corporate governance is a relatively broad one, and that it often seems to mean different things to different people. Also, in Vietnam, the concept is not well established or well understood. An all-out campaign by Vietnam to promote good corporate governance practices could require considerable claims on limited resources. It would probably be better for policymakers to identify specific issues within the broad umbrella of corporate governance where: i) there is the most pressing need for intervention and ii) the optimum gains of such interventions - or the returns on investment of effort - could be readily achieved.

#### 1.1 Areas for further research

As this is the first survey of its kind in Vietnam, we deliberately 'cast our net' widely, and tried to span most, if not all, of the corporate governance issues that one finds in the existing literature. In doing so, we hope we have been able to identify: i) some of the specific areas where there is greater need for interventions and initiatives; and conversely ii) some of the specific areas where existing laws and regulations are relatively robust and therefore need much less attention - to develop a baseline survey, if you will. But there is clearly a need for further, more focused diagnostic studies leading on from this initial foray. In particular, it would be worth taking a closer look at the more specific corporate governance problems faced by the SOE sector, such as potential conflicts of interest, related party transactions, and the rather confused director structures. Also, in the case of the non-state sector, other topics that would benefit from further research include the apparent weaknesses of Inspection Committees in many private firms as well as the considerable overlap that exists between

senior executives and Boards of Management. Deeper insights on these issues could then serve as useful inputs in the conceptualization and design of a focused corporate governance 'action plan' for Vietnam.

### 1.2 Focus on SOEs - for now

It is worth stressing that the large majority of companies in Vietnam remain small enterprises. Notwithstanding their future growth and sustainable development prospects, which depend partly on good corporate governance, their immediate need to improve such practices is clearly limited. Therefore, any efforts to improve corporate governance standards in Vietnam should almost certainly focus, at least initially, on larger business entities, the majority of which - but certainly not all - tend to be SOEs. As the private sector in Vietnam matures and burgeons, doubtless more non-state firms will develop into large corporate entities. But at present, it may be advisable to focus particular attention on SOEs.

### 1.3 Continue with equitization

In this regard, the pursuit of better corporate governance practices converges with the ongoing equitization campaign, particularly as the latter process shifts into higher gear and includes some of the largest enterprises in the state sector. Evidence that SOEs destined for equitization have introduced and are implementing good corporate governance practices will be a critical factor in attracting those investors, particularly the institutional ones, needed to make their divestments a success. Investors will be willing to buy shares of partially equitizing SOEs at valuations acceptable to the government only if there are improved corporate governance standards that better protect the interests of minority shareholders. As our survey results suggest, the equitization process does seem to be a vehicle for advancing good corporate governance standards within firms. This synergy provides Vietnam with a window of opportunity to push forward with the adoption of better corporate governance standards and practices.

## 2. Regulatory issues

### 2.1 Areas for reform

Our survey results suggest several areas for improvement in existing (or future) laws and regulations that deal with corporate governance issues, standards and practices. These include: i) greater disclosure requirements for Board of Management members and senior executives of firms; ii) greater clarification on the concept of the 'fiduciary

duty' so that Board of Management members and senior executives of firms are more cognizant of their legal roles and responsibilities; iii) strengthening of the Inspection Committees' authority so that they can better perform their assigned duties; iv) strengthening and better protecting shareholders' rights and equitable treatment, particularly for minority shareholders; and v) clearer and more stringent regulations to thwart related party transactions and avoid conflicts of interest. All of the recommendations were provided to the drafting team of the new Enterprise Law and were incorporated to some extent in the final law that was passed by National Assembly in late 2005. The recommendations are still relevant, however, to other existing related laws or new laws and regulations, e.g. the securities law, pertaining to corporate governance.

## 2.2 Resolving the agency problem

It would also be useful to introduce regulations that govern and help promote performance-based remuneration schemes, such as stock options, which better align the interests of senior managers the company's long-term success. They can encourage managers to implement strategies that will generate sustainable corporate profits and deter them from seeking to extract value from the company illicitly for personal gain. Such stock option schemes are quite common in many countries and foreign companies, but still rare in Vietnam, at least formally.<sup>15</sup>

## 2.3 Issues particular to SOEs

With specific regard to the SOE sector, there is clearly a need to better clarify and separate the regulatory and ownership functions of the state. There is also a need to better clarify and delineate the roles and responsibilities of those government agencies, and their mandated representatives, that are directly or indirectly involved in the governance of SOEs. Ultimately, one would wish to see the same laws and regulations on corporate governance issues relate to both SOEs and non-state firms, in as much as this is possible.

## 2.4 Implementation and enforcement

Needless to say, the usefulness of regulatory and legal changes that are intended to improve corporate governance standards and practices in Vietnam is contingent upon effective implementation and enforcement. Given the capacity constraints of the agencies and institutions responsible for these functions, this important precondition needs to be kept in mind, particularly when drafting new policies, laws and regulations.

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<sup>15</sup> Also see 'Introduction to Issuing Employee Stock Options in Vietnam'.

Clearly, there is a need to devise legal and regulatory interventions that are not only appropriate to Vietnam's current and specific needs, but are also practicable and 'implementable'. Conversely, the wholesale adoption of corporate governance laws and regulations from other countries, particularly the advanced industrialized economies, is unlikely to meet with much success. One leading expert has cautioned against

"importing governance structures or systems from foreign jurisdictions. Countries and corporations are best advised to start from where they are and to build on their existing structures and systems. Convergence is taking place, but it is convergence on standards of corporate governance, not necessarily on their form."<sup>16</sup>

This broad statement seems highly pertinent to the specific case of Vietnam.

## 2.5 Lessons from other countries

That said, there is much that Vietnam's policymakers and advisors can learn from recent experiences in promoting improved corporate governance practices in other developing Asian countries, as well in as the transitional economies of the former socialist bloc. They provide a relevant 'smorgasbord' of corporate governance interventions from which Vietnam, with the support and assistance of those members of the donor community with expertise in this field, can select those that seem most appropriate and effective. This is also true for non-regulatory initiatives, as discussed below.

## 3. Non-regulatory issues

### 3.1 A multidimensional approach

While there is clearly room for improving the policy, legal and regulatory framework in Vietnam so as to support the enactment of better corporate governance practices, the imposition of such measures alone will not be sufficient. The ability for companies to bypass laws and regulations, largely due to the capacity constraints faced by government institutions in enforcing them, means that a more multidimensional approach needs to be adopted.

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<sup>16</sup> Sir Adrian Cadbury in the foreword to 'Corporate Governance and Development', p. vi.

### 3.2 Raising awareness of the benefits of corporate governance

If it is widely perceived that new laws and regulations to promote better corporate governance practices just end up creating additional (and unnecessary) burdens for companies, then their effectiveness will be limited. Rather, in a bid to gain maximum traction, it is important that any drive to improve corporate governance practices seek to illustrate why the pursuit of better corporate governance practices can be of genuine and practical benefit to companies themselves. Anything less will run the risk of becoming a cynical exercise in box-ticking at best, and possibly mass avoidance at worst. But if managers of firms can see that improved corporate governance practices will lessen their exposure to various operational risks and improve business performance, and if shareholders can see that improved corporate governance practices will permit their investments to create greater value, then new laws and regulations are more likely to be embraced and genuinely internalized in the day-to-day operations of companies. This logic suggests that a consciousness-raising and advocacy campaign would be a useful complement and support to any regulatory initiatives.

### 3.3 Integrating corporate governance efforts with broader reforms

It also should be recognized that making substantive advances on some elements of the corporate governance agenda can not be done in isolation from other initiatives. Rather, any drive for better corporate governance practices needs to be an integral part of the wider economic reform and business liberalization process, whether it pertains to SOEs, equitized former SOEs, or private firms. On the specific issue of corporate transparency, for example, it is hard to envisage how companies will make major strides to improve the quality of their financial reporting without a marked improvement in the corporate income tax system. It also needs to be recognized that the corporate governance challenges facing SOEs tend to differ from those of most private companies, and arguably differ again (in some ways at least) from those of equitized former SOEs. Consequently, any concerted initiative to improve corporate governance practices across Vietnam's corporate sector would need to be multi-pronged.

### 3.4 Institutional coordination

For the same reason, we suggest that any concerted initiative to improve corporate governance practices in Vietnam will require the combined efforts of multiple government agencies and other relevant organizations, spanning: the Ministry of Finance, the Ministry of Planning & Investment, the State Securities Commission (SSC), the Ministry of Justice, the Vietnam Chamber of Commerce & Industry (VCCI), the Vietnam Association of Financial Investors (VFAI), some business associations, and so on.

### 3.5 Other initiatives

In addition to supporting the policy and legislative interventions that are intended to strengthen the legal and regulatory framework for corporate governance, there is a need to support such efforts with a range of other initiatives, including: i) advocacy work in promoting good corporate governance practices within the business community; ii) the provision of education and public awareness campaigns; iii) the provision of practical training on specific corporate governance themes and issues (e.g., auditing and accounting) for senior executives and members of both Boards of Management and Inspection Committees; iv) work to deepen the pool of qualified and capable individuals who can serve as members of Boards of Management;<sup>17</sup> and conceivably v) work with commercial banks and a credit scoring agency that can promote better corporate governance practices while also providing better access to finance.<sup>18</sup>

It is likely that different agencies or organizations would be asked to take the lead (and provide the principal inputs) on each of these non-regulatory initiatives, but as part of a relatively integrated and coordinated program. At this stage, the optimal approach would probably be to coordinate all such activities through a large-scale corporate governance initiative with multiple objectives - from raising awareness, to providing training, direct technical assistance, and capacity building for existing local institutions. In this regard, the IFC's large-scale corporate governance technical assistance work in Eastern European transitional countries serves as an approach that Vietnam might wish to consider following in its pursuit of improved corporate governance practices.

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17 There is little utility having Boards of Management if the members are not sufficiently skilled to perform their duties adequately. This capacity constraint is not uncommon. In 2003, Singapore found that a boom in initial public offerings had resulted in a shortage of board directors, with some individuals sitting on ten or more company boards (in addition to their full-time jobs). See *The Business Times* (Singapore), 19 November 2003.

18 A far better option than providing fiscal incentives to firms that pursue good corporate governance practices.