

VIETNAM BOND MARKET ASSOCIATION

Managing Legal Risk in Capital Market Transactions: Certain Emerging Issues

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Part I

Legal Risk
in
Capital Market Transactions

What is Legal Risk

- There is no concrete definition for “legal risk” and the term is used in different ways
- According to Basel II Accord, legal risk falls within the category of operation risk (footnote 97)

What is Legal Risk

- The risk that contracts are not legally enforceable or appropriately documented or duly executed
- The risk that the company is exposed to legal action or investigation

Legal Risk: Capital Market Context

- Contractual liability arising out of engagement letter
- Civil liability arising out of breach of disclosure obligations under securities law
- Criminal liability arising out of conviction of certain “business” offences under the Penal Code

Part II

Contractual Liability of the Arranger under Engagement Letter

Contractual Liability: Engagement Letter

- A contract of service between the issuer and the arranger
- The arranger may
 - a) act as financial advisor (i.e. to provide advisory services, “run the book” etc.); and
 - b) act as underwriter (i.e. to underwrite the proposed issue)

Contractual Liability: Underwriting

- Underwriting represents the underwriter's commitment to buy the bonds that are not sold
- Bond issues are underwritten on a bookbuilt basis
- The underwriter's obligation is subject to the absence of certain events

Underwriting: Common Misunderstanding

- The mechanism of securities underwriting is not well defined in the law
- From an Issuer's perspective, underwriting is commonly understood as "hard underwriting" (i.e. "bought deal")
- Underwriting mechanism needs to be spelt out in contract

Contractual Liability: Risk Mitigation

- Technical aspects of the deal are clearly and specifically defined in engagement letter
- The limitation of liability should be appropriately addressed
- The financial advisor's and underwriter's obligations are discharged or released following occurrence of certain specified events

Contractual Liability: Risk Mitigation

- The underwriter's obligations are discharged or released following occurrence of certain specified events (material adverse change in the issuer's business or financial conditions, adverse market conditions etc.)
- No commitment to buy bonds unless the issue is priced on a bookbuilt basis

Part III

Civil Liability Arising out of Breach of Disclosure Obligations

Disclosure Obligations: Issuer's Perspective

- Issuer's duty to disclose appropriately information in a timely manner under securities law in respect of private offerings (Art. 38.3, Decree No. 90/2011/ND-CP; Art. 5 Decree No. 58/2012/ND-CP; Circular No. 52/2012/TT-BTC)
- Information is contained in disclosure documents (such as offering circulars, information memorandum) or roadshow materials

Disclosure Obligations: Issuer's Perspective

- As disclosure obligations are statutory duties, the issuer is exposed to civil action initiated by investors if it provides false or misleading information pursuant to the 2005 Civil Code
- Regulatory action against the issuer may also be commenced by the regulators (i.e. the SSC, SBV or a local department of planning and investment)
- Criminal liability possibly arises if the breach causes serious damages or losses

Arranger's Liability for Issuer's Breach of Disclosure Obligations

- The arranger has contractual obligations pursuant to the terms of the engagement letter
- In principle, it would be construed that the arranger owes a strict duty of care to the issuer
- The arranger would be liable for the issuer's breach of its disclosure obligations if the arranger's act is also attributed to the issuer's default

Arranger's Liability for Issuer's Breach of Disclosure Obligations

- The arranger is exposed to contractual claim by the issuer which can be asserted by reason of the arranger failing to perform its contractual obligations
- The arranger is exposed to non-contractual claim by the investors which can be asserted in reliance of principles on non contractual liability and damages as laid down by the Civil Code

Disclosure Obligations: Risk Mitigation

- Due diligence on the issuer's legal, business and financial matter is required
- Appropriate disclaimer needs to be contained in the disclosure documentation
- Limitation of liability needs to be addressed in the engagement letter

Part IV

Criminal Law Implications of Capital Market Transactions

Elements of Crime

- An act or omission of the offender that causes a social harm
- Such act or omission is specified in the Penal Code
- The offender is capable of committing a criminal offence
- The offender is intentionally or, in respect of certain offences, unintentionally at fault

1999 Penal Code and Its Amendment

- Crime are defined in 1999 Penal Code
- There are a separate section dealing with “economic” crimes
- 2009 Amendment Law introduces new business crimes relating to the securities (Art. 181a, 181b, and 181c)
- 2009 Amendment Law also provides for a revised article on money laundering (Art. 251) and terrorist financing (Art 230b)

New Crimes Regarding Securities Business

- Provision of false or misleading information or hiding the facts in respect of securities (Art. 181a)
- Insider trading of securities (Art. 181b)
- Manipulation of price of securities (Art. 181c)

Certain Business Crimes Which are Sensitive by Nature

- Voluntary violation of regulations on economic management that causes serious effect (Art. 165)
- Reckless that causes serious effect (Art. 285)

Article 165 of the 1999 Penal Code

- Offender must hold a management position (i.e. any officer is exposed to the risk of committing this offence)
- Offender has intentionally failed to comply strictly with a specific regulation on economic management (being aware of non-compliance)
- Offence has caused a serious effect (difficulty of determining objectively)

Article 285 of the 1999 Penal Code

- Offender must hold a management position (i.e. any officer is exposed to the risk of committing this offence)
- Offender is negligent when exercising his or her management duty
- Offence has caused a serious effect (difficulty of determining objectively)

Criminal Liability: Risk Mitigation

- Management is frequently kept informed of new legal developments
- Compliance function is put in place and continuously operative
- Consultation with external counsel should be sought in respect of any sensitive cases

ANY QUESTIONS?

- Questions/points for discussion