
BANKING & FINANCE - VIETNAM

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Market structures & trends

In order to promote domestic and foreign investment, Vietnam has gradually developed its banking and finance regulatory framework since the introduction of its “doi moi” (renovation) policy in the late 1980’s. Despite recent reforms precipitated by the Asia crisis and moves towards joining the WTO, Vietnam’s banking and finance sector remains tightly controlled.

Domestic banking sector

Reflecting Vietnam’s socialist history, 4 large State owned banks dominate the banking sector, with 74% of the lending market (primarily to State owned enterprises (SOEs)). Joint-stock (shareholding) banks (JSBs) now number 34, after 3 years of rationalization at the directive of the State Bank of Vietnam (SBV), with 15% of the lending market (primarily to private Vietnamese companies). Co-operative banks and people’s credit funds enjoy a small market share.

No JSBs are currently listed on Vietnam’s stock exchange, which is still in its preliminary stage with only one Stock Trading Center open in Ho Chi Minh City and only 17 listed companies. An application for listing by Vietnam’s largest JSB, Asia Commercial Bank (ACB), is pending.

Foreign market participation

Reflecting the Vietnamese Government’s policy of protection of domestic companies, foreign participation in the banking and finance sector remains restricted.

Foreign shareholdings in JSBs are not generally permitted, with the case-by-case exception of several foreign investment funds since 1995. Vietnam Enterprise Investment Limited, managed by British firm Dragon Capital, currently holds shares in 3 JSBs and Vietnam Frontier Fund, managed by Thai firm Finansa, has recently sold

its shares in 2 JSBs (with ACB in both portfolios). Connaught Investors and LG hold shares in ACB only. No foreign shareholder currently holds more than 10% of shares in a JSB (with a 5-year restriction on transfer) but a number hold board positions.

Foreign market participation is largely limited to prescribed forms of direct investment. Currently, there are 4 joint venture (JV) banks, 27 foreign bank branches and 53 representative offices of foreign banks. Operations are small scale due to market size and operating restrictions. Most lending is to SOEs and foreign invested enterprises (FIEs), due to the scant (if any) credit history and lack of accountability of private Vietnamese companies. Increasingly, lending in Vietnamese dong (VND) is preferred over foreign currency lending due to restrictions by law on onshore foreign currency transactions by most borrowers.

There are only 2 foreign invested finance leasing companies and no foreign invested finance companies or securities companies yet established. There are 9 foreign invested insurance companies, with two further applications pending.

All FIEs operate as limited liability companies, in which the interest of the foreign investor is its share of capital contribution. A draft decree on foreign invested shareholding companies is currently under consideration by the Government, but it is currently unknown whether they will be permitted in the banking and finance sector.

Effective 10 December 2001, the US-Vietnam Bilateral Trade Agreement (BTA) commits Vietnam to a wide range of regulatory reforms, aimed at increasing trade between the US and Vietnam. With respect to banking and financial services, the BTA provides, *inter alia*:

- After 3 years, Vietnam commits to provide full national treatment with respect to access to central bank rediscounting, swap and forward facilities.
- Over the first 8-10 years, Vietnam will phase-in full national treatment with respect to the right of US bank branches to accept VND deposits from Vietnamese customers.
- US-invested financial institutions will be permitted to issue credit cards on the same basis as Vietnamese banks after 8 years.
- After 9 years, 100% subsidiary banks of US banks will be permitted to be established.

Despite a Vietnamese Government undertaking to provide to European investors (and expectations of investors from other jurisdictions to enjoy) equal treatment in all aspects of the BTA, there are some concerns that US financial service providers may enjoy preferential removal of restrictions on market access. In this respect, it remains to be seen to what extent the BTA represents the roadmap for liberalization of the Vietnamese banking and finance sector for all foreign investors.

Presumably, however, the terms of WTO accession (Vietnam hopes to join by 2004) will include (and possibly extend) the liberalization measures set out in the BTA.

Offshore loans obtained by Vietnamese businesses (including FIEs) remain subject to prescribed conditions, with SBV registration required for medium and long-term loans before drawdown.

The main regulatory bodies and their powers

The State Bank of Vietnam (SBV) is a Government body, responsible for State administration of monetary and banking operations. In addition to being the central bank of Vietnam, the SBV has the powers *inter alia* to issue legal instruments on currency and banking operations, issue and revoke licenses of credit institutions, authorize the dissolution, division or merger of credit institutions, inspect and control operations of credit institutions, and deal with offences.

The Ministry of Finance (MOF) is a Government ministry, responsible for State administration of insurance business, with the power *inter alia* to issue legislation relating to insurance business, issue and revoke insurance business licenses, inspect and control insurance operations, and deal with offences. The MOF also regulates financial regimes of credit institutions and participates in planning and policy for the Vietnamese financial system.

The State Securities Commission (SSC) is a Government body, responsible for State management of the securities market, including licensing of securities issues, trading and services, inspection of companies involved in securities activities, and dealing with securities offences.

Types of financial institutions and key legislation/regulatory developments

Each of the principal types of financial institutions - credit institutions, insurance businesses and securities businesses - is subject to a separate legislative framework, within which specific regulations govern foreign invested institutions.

Credit institutions

Credit institutions are governed by the Law on Credit Institutions 21 December 1997 (LCI) and subject to licensing by the SBV. Credit institutions encompass banks and non-banking credit institutions, such as finance companies and finance leasing companies (permitted to conduct a number of banking operations but not permitted to receive on-call deposits or provide payment services). Non-credit institutions may be licensed by SBV to conduct banking operations in limited circumstances only.

Under Decree 64 of the Government dated 20 September 2001 (updating the regime for payment operations), banks may now determine the procedures for opening bank accounts, provision of overdraft facilities is permitted, and international payment operations may be governed by international rules and practices (provided that they are not contrary to Vietnamese law). Provision of credit card facilities remains restricted.

Under Decision 1627 of the SBV dated 31 December 2001, the highly prescriptive regulations on bank lending have been relaxed. Banks may now make their own lending decisions (including form, purpose, term, security, interest rate, extensions of loans) subject only to broad conditions. Restrictions on unsecured lending remain. Recently updated regulations on inter-bank and syndicated bank lending also reflect this trend towards greater autonomy in lending decision-making.

Specific regulations on licensing and operating conditions for foreign credit institutions are provided under Decree 13 of the Government dated 17 March 1999.

Implementing Decree 13, Circular 08 of the SBV dated 4 July 2000 provides detailed guidelines on foreign bank branches and JV banks.

Foreign bank branches may be licensed for up to 20 years. JV banks (maximum 50% foreign capital for commercial banks) may be licensed for up to 30 years. Licenses are extended on a case-by-case basis.

The National Office for Registration of Security Transactions commenced operation in March 2002, finally allowing credit providers to register security agreements as required by law. However, credit providers remain wary, attaching little value to security over immoveable assets located in Vietnam, as recent attempts to enforce the step-in rights of lenders have not been encouraging.

Foreign bank branches and JV banks are subject to various restrictions designed to protect domestic banks. Branches may not receive foreign currency deposits from Vietnamese customers. Since November 2001, JV banks may accept foreign currency deposits from Vietnamese individuals, subject to a limit of 50% of capital (and interest rate caps). VND deposits are restricted to on-call accounts and subject to a limit of 25% of capital (anticipated to be relaxed to 50% this year under the BTA). As there is no inter-bank VND market, restrictions on VND deposits severely limit VND liquidity. De-regulation of VND loan interest rates (effective 1 June 2002) should assist VND liquidity. The inter-bank foreign currency market established in 1999 and de-regulation of foreign currency loan interest rates in mid-2001 has facilitated foreign currency (predominantly USD) liquidity.

Decree 16 of the Government dated 2 May 2001 and Circular 08 of the SBV dated 6 September 2001 provide specific guidelines on wholly foreign owned and JV (minimum 30% foreign capital) finance leasing companies, which may be licensed for

up to 50 years. No specific guidelines on foreign invested finance companies have yet been issued.

Securities companies

Securities companies (effectively stockbrokers), securities investment funds and fund management companies are governed by Decree 48 of the Government dated 11 July 1998 (Decree 48) and subject to licensing by the SSC.

Foreign investment in securities companies is limited to JVs (maximum 30% foreign capital). Decision 04 of the SSC dated 13 October 1998 (amended 29 December 2000) provides specific guidelines. Reportedly, the first application for a JV investment fund is currently under consideration by the SSC.

To conduct securities business, credit institutions must establish independent securities companies. Specific regulations on establishment of securities companies by foreign credit institutions are yet to be issued.

Insurance companies

Insurance companies and brokers are governed by the Law on Insurance Business 9 December 2000 (Insurance Law) and subject to licensing by the MOF. To conduct insurance business, credit institutions must establish independent insurance companies.

Wholly foreign owned or JV (minimum 30% foreign capital) insurance companies or insurance brokers may be licensed for up to 50 years. The type of insurance business (life and/or non-life) is prescribed in their licenses, and they are prohibited from providing insurance to SOEs.

Detailed guidelines for implementation of the Insurance Law were issued under Decree 42 of the Government dated 1 August 2001 and Circular 71 of the MOF dated 28 August 2001. Regulations on the financial regime for insurance business were issued under Decree 43 of the Government dated 1 August 2001 and Circular 72 of the MOF dated 28 August 2001.

Representative offices of foreign financial institutions may also be established but are not permitted to conduct business.

Establishing an operation

For foreign credit institutions, a standard-form application and supporting documents (including draft charter, 3 year business plan, details of capital contribution and financial status of investors) are submitted in duplicate, in Vietnamese and English, to the SBV. Similar licensing applications are submitted for securities business to the SSC and for insurance business to the MOF.

Licensing applications are subject to consideration by a range of relevant authorities and determined on a case-by-case basis depending on the requirements of socio-economic development and the financial market of Vietnam.

Statutory time-limits apply to processing of applications (90 days for credit institutions and securities companies, 60 days for insurance businesses). In practice, considerable consultation with local and central authorities prior to and during the application process is recommended to ensure timely licensing, as well as desired license details. Licensing fees are payable.

In the case of refusal, written reasons are required to be provided to the applicant but there is no formal appeal procedure.

After licensing and prior to commencement of operation, the licensee must carry out business registration at the relevant business registration office and advertise license details in central and local newspapers.

In the case of credit institutions, capital contributions in cash must be deposited into a frozen non-interest bearing account at the SBV for at least 30 days prior to commencement of operation. Evidence of legal ownership and value of any capital contributed in kind must be presented to the SBV.

Under Decree 89 of the Government dated 1 September 1999 (Decree 89), institutions accepting VND deposits from individuals must obtain deposit insurance from Vietnam Deposit Insurance (VDI). Registration with VDI must be completed 30 days prior to commencement of operation.

Circumstances for revocation of the license of a financial institution include: failure to commence operation within 12 months of licensing; bankruptcy; breach of licensing terms or necessary operating conditions; bankruptcy or dissolution of the foreign parent bank (for foreign bank branches); de-licensing of the foreign parent company (for foreign invested insurance businesses); engaging in short-selling, insider trading, and other prohibited activities (for securities businesses). License revocations must be publicized in the mass media. Operations must be suspended immediately upon license revocation.

Financial services online/e-banking

On-line financial and banking services are still in their infancy. State owned Vietcombank is the only bank to have developed an Internet banking platform. Several banks have developed point-of-sale systems.

Electronic transfer of funds has been recognized by law since the mid-1990's. Despite recent updating, the regulatory framework for electronic payments remains basic. Importantly, under Decision 44 of the Government dated 21 March 2002, electronic payment orders and electronic signatures are now expressly recognized as effective as hard-copy orders and signatures provided all statutory requirements for accounting source documents are satisfied.

Electronic payment service providers must ensure the confidentiality and integrity of information data during data processing, transmission and storage. When necessary (not defined by law), after payments have been made, electronic payment orders may be required to be printed and certified by the authorized person of the service provider. Further guidelines are expected to be issued by the SBV.

An Ordinance on E-Commerce is scheduled for drafting and possible consideration in late 2002.

Buying financial institutions

Opportunities to buy into domestic financial institutions are currently limited, as noted earlier.

Foreign entities may buy into foreign invested financial institutions by way of onshore acquisition of an interest (most commonly, a foreign investor's interest) in the legal capital of the financial institution or offshore acquisition of the foreign investor entity.

Onshore assignments of 10% or more of capital in foreign credit institutions and insurance businesses (and all assignments of capital in JV securities companies) are subject to approval by licensing bodies. Third party assignees must satisfy applicable licensing conditions. In the case of JVs, assignments are subject to agreement by the JV parties, statutory foreign capital limits, and a right of first of refusal in favor of the other JV party(ies).

The time-limit for consideration of applications for approval of assignments of capital are not specified, except for insurance businesses (30 days). In the case of refusal, written reasons must be provided but there is no formal appeal process.

The most straightforward option is an offshore acquisition of a foreign investor entity. However, some offshore acquisitions have been deemed by the authorities to trigger statutory rights of first refusal and to constitute assignments of the foreign investor's

onshore interests for the purpose of capital gains tax in Vietnam. Approval of licensing bodies will be required for any changes in project details, such as project name and senior management, consequent upon an offshore acquisition.

Competition regulations

Regulation of competition in Vietnam is in its infancy, developing from a historical context of State monopoly of all economic sectors.

The basic principle of lawful competition is enshrined in each of the LCI, the Insurance Law and Decree 48. Unlawful promotions, publication of misleading information, coercion, and speculation or conspiracy for the purposes of market control are expressly prohibited.

A generally-applicable Competition Law is currently under consideration, but not expected to be passed until late 2003. The following discussion is based on the latest draft finalized by the Ministry of Trade (MOT) in mid-April 2002.

A national competition commission (NCC) will be established (either as a new ministerial-level body or a subsidiary body under the MOT). Subject to limited exemptions, anti-competitive industry agreements, abuse of dominant or monopolistic position, predatory, misleading, unfair and dishonest market practices, and concentrations of economic power will be prohibited.

Welcome features are the requirement for disclosure by the NCC of information on exemptions, mergers, consolidations and acquisitions, and dominant and monopolistic enterprises and the prohibition on disclosure of business secrets obtained during enforcement of the competition regulations.

The time-limit for consideration of applications for exemption from the competition regulations will be 2 months (extended up to 4 months in complex cases). In cases of approval, a written permit will be issued. Dissatisfied applicants will be entitled to appeal to the NCC or institute court proceedings.

In cases of non-compliance or other breaches, the NCC will conduct a preliminary inquiry (up to 7 days) and, where an offence is found, an official inquiry (up to 40 days, or 90 days in complex cases). The NCC may require production of documentation and written information and carry out on-site investigations.

Offenders may be subject to administrative penalties or criminal prosecution and, where necessary, compulsory re-organization, public correction of false information, and removal of unlawful terms and conditions from contracts or transactions. Compensation will be payable for any damage caused. Sanctions for offences must be publicized. Rights of appeal are provided.

On-going bank supervision

Foreign bank branches and JV banks complain of onerous reporting obligations, to the extent of reporting on every customer's transactions every month. The SBV is currently reviewing periodical statistical and operational reporting obligations.

Audited annual financial reports must be submitted to the SBV within 90 days of the close of the fiscal year (31 December). Annual financial reports of the foreign parent bank must be submitted within 180 days of the close of the fiscal year.

Establishment of an internal inspection and audit system is mandatory. The selection of external auditors must be approved by the SBV.

Where deemed necessary, the SBV may inspect the operations of a bank and apply measures to prevent or deal with any breaches of laws on monetary and banking operations. Sanctions include administrative penalties (warning, fine, license revocation), criminal prosecution, and liability for compensation for damage. Rights of appeal are provided.

In the case of banks participating in deposit insurance, the SBV must notify the results of its inspections to VDI and banks must submit annual financial reports to VDI. VDI has powers of inspection of compliance with the deposit insurance regime.

Representative offices of foreign banks are only required to submit six-monthly reports on their marketing activities, as they are not permitted to conduct business.

Disclosure requirements

All significant changes in operations of financial institutions require written approval from licensing bodies, including change in general director (for all financial institutions), change in board of management and board of controllers (for JV banks) and change in board chairman (for insurance businesses).

Applications for approval of above changes must be processed within 30 days. In cases of refusal, written reasons must be provided but there is no formal appeal procedure. Upon approval, changes must be registered at the business registration body and advertised in central and local newspapers.

Any institution participating in deposit insurance must also promptly notify VDI upon any of the above changes.

Licensing bodies must be notified of any change in the head of a representative office, but approval is not required.

As noted earlier, changes in control of financial institutions are subject to approval by licensing bodies. In addition, foreign bank branches and JV banks must notify the SBV of any change in name, address or management or merger, demerger, consolidation, bankruptcy, liquidation or dissolution of a foreign parent bank. Similarly, foreign invested insurance businesses must notify the MOF of the de-licensing of a foreign parent company.

An authorized foreign regulatory body or the foreign parent bank is entitled to inspect the operations of a foreign bank branch, subject to prior written notification of inspection and subsequent notification of inspection results to the SBV.

When a bank becomes insolvent

The LCI makes specific provisions for dealing with insolvency. Insolvency risks must be promptly reported by banks to the SBV or may be independently identified by the SBV.

Under Decree 89, banks participating in deposit insurance must also promptly notify VDI, which may impose remedial measures. Where a bank is in danger of insolvency, but not to the extent of being put under special control, VDI may provide support (including loans or guarantees for loans to fund payment of insured deposits) if the continued operation of the bank is considered important for the security of the whole financial system and political and socio-economic stability. Where deposit insurance premiums are not paid for over 90 days, VDI may terminate insurance and request the SBV to prohibit deposit-taking from individuals.

Any bank deemed likely to become insolvent or having total accumulated losses in excess of 50% of its charter capital and other reserve funds will be put under special control by the SBV. Local competent bodies must be notified, but otherwise any decision on special control is confidential.

A special controlling board has considerable powers, including suspending particular operations and suspending authority of senior management. However, senior management remain responsible to manage the operations and maintain the assets of the bank (except where suspended).

Insolvent banks will be subject to bankruptcy proceedings under the Law on Business Bankruptcy 30 December 1993 (scheduled for amendment in late 2002). No bank has yet been formally bankrupted.

Statutory bankruptcy proceedings are generally consistent with international norms. After a 60-day claim period for creditors, a meeting of creditors will be convened to consider any bank restructure proposal or resolve the distribution of assets. Any resolution must be passed by more than half of the creditors representing at least two thirds in value of unsecured debts and acknowledged by way of court decision (which must be publicized). Where a restructure resolution is successfully implemented,

bankruptcy proceedings may be suspended. Otherwise, a declaration of bankruptcy will be made (subject to appeal by creditors or the bank to the People's Supreme Court of Appeal).

Secured creditors have priority only to the extent of the value of secured assets, and thereafter are ranked with unsecured creditors with respect to the remaining amount of secured debts. Where assets are insufficient to cover the debts of unsecured creditors, each creditor will receive a proportion of the amount owed (at a ratio determined by the court).

Under Decree 89, VND depositors are entitled to receive from VDI up to VND30 million, payable for all deposits (including principal and interest) at any one bank. Depositors are treated as unsecured creditors with respect to any amount over VND30 million.

Capital requirements & bank secrecy

All credit institutions are subject to minimum levels of legal capital (foreign bank branches: USD15 million; JV banks: USD10 million; foreign non-banking credit institutions: USD5 million). Changes in legal capital must be reported to the SBV. 5% of after-tax profits must be contributed annually to a 'charter capital supplementing fund' (up to amount of actual charter capital).

Under Decision 297 of the SBV dated 25 August 1999, the minimum capital adequacy ratio is 8%, the minimum liquidity ratio is 1, and the maximum ratio of medium and long term loans provided by use of short term funds is 25%.

The total amount of loans of a single credit institution made to (or guaranteed in favor of) a single client may not exceed 15% of equity of the credit institution, except in specified special cases. Where the total amount of loans of a single client reaches 5% or more of equity, the SBV must be notified. (Here, equity includes charter capital and the supplementing fund; and for foreign bank branches, means equity of the foreign parent bank.)

Decree 70 of the Government dated 21 November 2000 and Circular 02 of the SBV dated 4 April 2001 provide specific regulations on bank confidentiality. Banks are prohibited from disclosing information relating to deposits or assets of customers to third parties, except where expressly agreed by their customers, where requested by competent State bodies or where necessary in support of their internal activities. Internal bank regulations for compliance with confidentiality obligations and archiving of minutes for every case of disclosure are mandatory. Sanctions for confidentiality breaches include warning, fine or criminal prosecution.