Legal Update on the New Financial Institutions Law

ASEAN PATH Issue # 11, May 2016

WELCOME

Welcome to the eleventh edition of DFDL's ASEAN Path!

Following the seventh edition of the ASEAN Path on Foreign Ownership of Financial Institutions, our Myanmar team saw major developments in the financial sector in the last few months. These developments are about to be introduced in Myanmar with the enactment of the New Financial Institutions Law. This issue outlines the important updates on the matter and the changes and their practical consequences in comparison with the former regime.

I invite you to contact any of the DFDL partners across our network or myself if you should have any comments or questions.

Martin Desautels
Managing Partner
m (Cambodia): +855 12 805 552
m (Vietnam):+84 983 977 053
e: martin.desautels@dfdl.com

DFDL
2015 constituted another exceptional year for DFDL especially for our office in Myanmar which received the title of National Law Firm of the Year by IFLR. It drives us to achieve more.

ASEAN PATH is a series of white papers prepared by DFDL's experts aiming to assess, in more depth, compelling issues arising from the regional economic integration under the auspices of the Association of Southeast Asian Nations ("ASEAN") Economic Community Blueprint. The articles are based on an in-depth legal analysis of the local and ASEAN legal framework from the perspective of a practitioner assisting foreign and ASEAN investors in their investments and operations throughout various ASEAN Member States. All articles are accessible on our website: www.dfdl.com.

INTRODUCTION

The long-awaited new set of rules on banks and financial institutions in Myanmar has been listed as a government priority since the current legal framework is outdated. In short, it evidences loopholes in many concerns such as transparency, content, and structure. Statistics from the United Nations Capital Development Fund are speaking for themselves. Currently, the Myanmar banking system is undeveloped despite the fact that since 2011, credit to the private sector is growing by average of 50% per year. In 2015, the IMF reported that deposits are equivalent to 32.5% of GDP while the credit to the private sector amounts to 16 % of GDP.[1]

"More reforms to the regulatory framework, together with continued macroeconomic stability, would be key to attracting further foreign and domestic investment." - IMF

[1] Myanmar: Selected issues, IMF Country Report No. 15/268, March 2015.

Moreover, no more than 5% of the adults in the country hold a bank account (see Figure 1). Then, only few Burmese are holding basic banks accounts. Consequently, an even smaller fraction borrows money from the bank according to the World Bank (see Figure 2 and Figure 3). One may expect these numbers to substantially change with the implementation of the new Financial Institutions Law ("**NFIL**"). For instance, the IMF expects the country's economy to grow by 8.5 percent in 2016.[2]

Figure 1: Glimpse of the Current Banking Situation

Less than 50% of the population has access to financial services

30% are using unregulated services

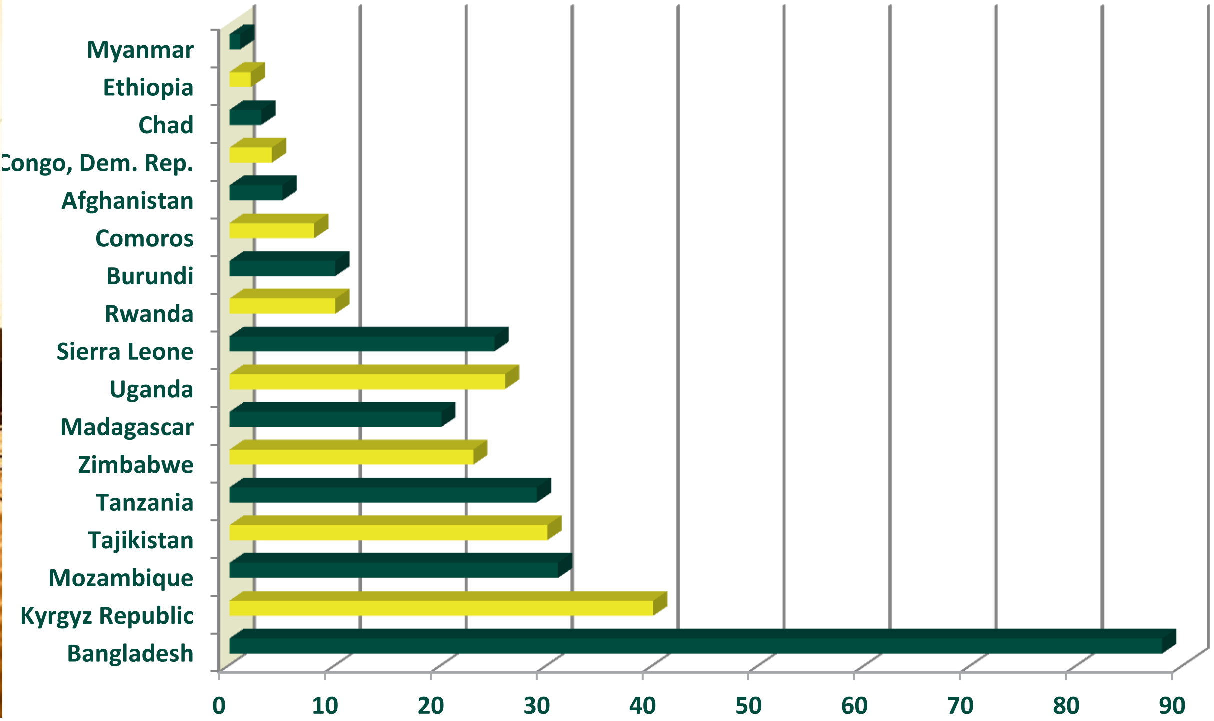
20% have access to regulated financial services

Only 5 % of adults have a bank account

From the above 5%, only 6% use more than one financial service

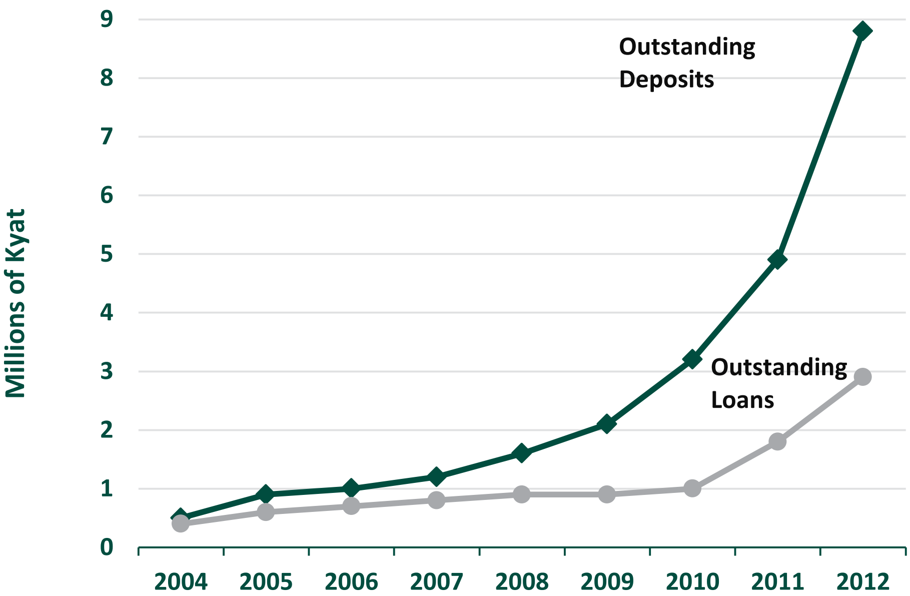
[2] IMF, Myanmar's Growth Momentum Strong, but Maintaining Stability Is Key (18 September 2015) online:http://www.imf.org/external/pubs/ft/survey/so/2015/car091815a.htm.

Figure 2: Borrowers from Commercial Banks (per 1,000 adults): Low Income Countries



Source: World Development Indicators and Carnegie Endowment for International Peace (data from 2012) 2014

Figure 3: Outstanding Loans and Deposits of Commercial Banks in Myanmar



Source: World Development Indicators and Carnegie Endowment for International Peace (data from 2012) 2014

LEGISLATIVE BACKGROUND

The banking and finance legal framework in Myanmar was established by the Financial Institutions Law ("**FIL**") of 1990 has changed with the enactment of the NFIL on 25 January 2016. The NFIL is part of the comprehensive structural legal reform undertook by the Government since 2010, which is aiming to create favorable conditions to attract greater foreign investments to the country. This tremendous liberalization is carried out in order to establish a functional financial system, which is a prerequisite for sustainable growth and development of any State economy in modern times.[3]

Prior to the banking system modernization, the Government did revise many of its related laws. The enactment of the Foreign Exchange Management Law ("**FEML**") on August 1, 2012 constitutes a key milestone, being the pillar of the banking sector reform by allowing clients to open an account in foreign currency and local currency. From this date, it became possible for clients to open an account in foreign and local currency. The Central Bank of Myanmar Law ("**CBML**") promulgated in 2013, granted more independence to the body having a key role regarding the application and the adoption of regulations pursuant to NFIL provisions.

The former FIL has been first promulgated in 1990 by the State Law and Order Restoration Council and has been subject to numerous amendments ever since, but generally its scope of application was limited to local financial institutions and its provisions were broadly drafted. This time, a diversified round table including IMF, World Bank, bilateral donors assisted by the Government and Central Bank of Myanmar ("**CBM**") economists have drafted the new NFIL. Hence, the NFIL has introduced most financial supervision standards prescribed by the World Bank and aligned Myanmar banking and finance legal framework to the best international practices.

[3] OECD, OECD Investment Policy Reviews: Myanmar 2014 (1 March 2014) online: http://www.oecd.org/countries/myanmar/investment-policy-reform-in-myanmar.htm.

Overview of the Current Banks and Financial Institutions Situation in Myanmar

Type of Business Organizations	State-Owned Development Banks	Private Banks	Representative Offices of Foreign Banks	Foreign Banks Branches	Finance Companies
Number of entities	4	24	49	9	11
List	• Myanmar Economic Bank (MEB) • Myanmar Agriculture and Development Bank (MADB) • Myanmar Investment and commercial Bank (MICB) • Myanmar Foreign Trade Bank (MFTB)	• Myanmar Citizens Bank Ltd • First Private Bank Ltd • Yadanabon Bank Ltd • Myawaddy Bank Ltd • Yangon City Bank Ltd • Yoma Bank Ltd • Myanmar Oriental Bank Ltd • Asia Yangon Bank Ltd • Tun Foundation Bank Ltd • Kanbawza Bank Ltd • Small & Medium Industrial Development Ltd • Global Treasure Bank Limited • Rural Development Bank Limited • Innwa Bank Ltd • Co-operative Bank Ltd • Asia Green Development Bank Ltd • Ayeyarwaddy Bank Ltd • United Amara Bank Ltd • Myanmar Apex Bank Ltd • Myanmar Microfinance Bank Limited • NaypyitawSibin Bank Limited • Construction and Housing Development Bank Limited • Shwe Rural and Urban Development Bank Limited • Ayeyarwaddy Farmers Development Bank Limited (A Bank)	• DBS Bank Limited • National Bank Limited • First Overseas Bank Limited • CIMB Bank Berhad (New License for Name of Change) • Bank for Investment and Development of Vietnam • Arab Bangladesh (AB)Bank Limited • Siam Commercial Bank Public Company Limited • Maruhan Japan Bank PLC • Krung Thai Bank Public Company Limited • United Bank of India • Kasikornbank Public Company Limited • Woori Bank • Vietin Bank • Korea Development Bank • Standard Chartered Bank • Shinhan Bank • Industrial Bank of Korea • First Commercial Bank (New License for Change of Management Office) • E.SUN Commercial Bank, Singapore Branch • Bank of India (BOI) • Kookmin Bank • Export-Import Bank of India • The Export-Import Bank of Korea • Eastern Bank Limited • Bank of Ayudhya Public Company Limited • RHB Bank Berhad • Commercial Bank of Ceylon PLC • State Bank of India • Cathay United Bank • State Bank of Mauritius • BRED BanquePopulaire • Busan Bank Co., Ltd • AEON Credit Service Company • PT. Bank Negara Indonesia (Persero)Tbk • Bank of Taiwan • Taishin International Bank Co., Ltd • Taiwan Shin Kong Commercial Bank Co., Ltd • CTBC Bank Co., Ltd • Yuanta Commercial Bank Co., Ltd • Taiwan Cooperative Bank Limited • Taiwan Business Bank Limited • Mega International Commercial Bank Co., Ltd • Ho Chi Minh City Development Joint Stock Commercial Bank • Qatar National Bank • Sampath Bank PLC • Bank of China • KEB Hana Bank (New License for Change of Name) • BTMU Leasing (Thailand) Co., Ltd • ACLEDA Bank Plc.	• The Bank of Tokyo-Mitsubishi UFJ, Ltd • Oversea-Chinese Banking Corporation Ltd • Sumitomo Mitsui Banking Corporation • United Overseas Bank Limited • Bangkok Bank Public Company Limited • Industrial and Commercial Bank of China • Malayan Banking Berhad (Maybank) • Mizuho Bank Limited • Australia and New Zealand Banking Group Limited	• Oriental Leasing Company Ltd • Myat Nan Yone Finance Company Ltd • National Finance Company Ltd • Ryuji Finance Company Ltd • Mahar Bawga Finance Company Ltd • Jewel Spectrum Company Ltd • Century Finance Company Ltd • Win Progress Services Company Ltd • Z Corporation Company Ltd • Global Innovations Finance Company Ltd • Mother Finance Company Limited

Source: Central Bank of Myanmar (May 2016) online: http://www.cbm.gov.mm/content/1228.

WHAT THE LAW SAYS

The NFIL introduces two types of amendments, in some cases we may observe simple tweaking of general rules, while in other instances; completely new rules were adopted.[4] Since the former Burmese legal framework is evidencing a huge disparity with the actual international best practices, some chapters cannot find immediate application. Some entities or concepts do not exist in the Myanmar banking sector yet, such as guidelines regarding non-bank financial institutions or electronic evidence. One may argue that the more significant provisions are in respect with the updated duties of the CMB: having now oversight and revision role, money laundering,[5] lending to related parties,[6] and measures ensuring liquidity and solvency. Concerning the latter, as it appears from the NFIL text, it complies with most of the standards of the Third Basel Accord ("**Basel III**") aiming to strengthen bank capital requirements; even some standards are even enhanced. Lenders have to keep 5 percent of customer deposits as cash with the CBM respecting the general objective of Basel III of increasing bank liquidity and decreasing bank leverage. In the same vein, the NFIL establishes a new minimum capital requirement of 20 billion Kyat[7] for a local bank incorporated in Myanmar while the previous requirement was 30 million Kyat. In addition, banks were previously required to hold at least 10 percent of their demand deposit and 5 percent of their time deposits as reserve. 75 percent of the aforementioned deposits could have been made up of Treasury bonds. The NFIL specifies that banks shall maintain a reserve fund and annually transfer 25 percent of their net profits to a general reserve fund.

Furthermore, the NFIL provides for the possibility, with the approval by the CBM, for banks including foreign banks to acquire the business or substantial part of the business of another bank or to sell its entire business or substantial part of its business to another bank. Under the NFIL a bank,[8] not including foreign banks and their representative offices, shall not acquire or hold shares in any company or enterprise to an aggregate value in excess of 10 percent of the capital fund of the bank,[9] while it can acquire or hold the shares of another bank or any company or enterprise carrying on non-banking and financial institutions (**"NBFI"**) business up to a value of 5 percent of the capital funds of that other bank or company or enterprise carrying on NBFI business.[10]

Modernization of Myanmar banking system is indisputably a great step forward, bringing the country closer to its ambitious goal of opening its doors. For now, traditional transactions such as deposits, lending and moneys transfers are the only source of revenues for banks, because sophisticated banking products cannot be supported by the actual banking system. Several essential components of a viable banking system are implemented by the NFIL such as: clearing houses,[11] Central Credit Bureau,[12] etc. Recently, electronic funds transfer at point of sale ("**EFTPOS**") has also been introduced, allowing clients to use electronic payment instrument and electronic payment system. Then, Myanmar's antiquated manual clearing system has been sidelined and replaced by a new consistent payment system.[13] Moreover, the NFIL introduces a chapter on E-Money, E-Banking and Mobile Banking.[14]

[4] Article 48.
[5] Article 60.
[6] Article 61.
[7] Article 136.
[8] Articles 142 and ff.
[9] Chapter 19.
[10] Chapter 18; The Central Bank of Myanmar has issued on 30 March 2016 the Regulation on Mobile Financial Services (FIL/R/01/03-2016).
[11] Chapter 22.
[12] Article 68.
[13] Articles 64 and ff.
[14] Article 34(a)(1), may increase according to new regulations (Article 35).

SANCTIONS, OFFENCES AND PUNISHMENTS

The wide range of sanctions from the CBM for a failure to comply to the provisions of the NFIL or its related regulations are potentially severe; warning, fines, orders including those restricting the operations of financial institution to the temporary suspension or termination from duties in financial institutions. These are laid out by Chapter 24, but will only be gradually applied according to U Mya Than, chair of Myanmar Oriental Bank. The reality exposed by the actual banking sector calls for an adjustment period and warnings will be prioritized over stronger enforcement penalties.[15]

More drastic actions can be found in Chapter 25 regarding prohibition, which could give rise to punishments under Chapter 26. As for example, a non-compliant, which provides any fraudulent fact and information when making an application to the CMB can be punished of an imprisonment for a minimum of 2 years in addition to a 500 million Kyat fine. Therefore, a correct understanding of the new provisions and the extent of their application is required.

RECENT DEVELOPMENTS

Since June 2014, a branch or subsidiary of a foreign bank that is satisfying the USD75 million minimum capital requirements[16] can operate in the country if the Foreign Bank Licensing Committee ("**FBLC**") grants them the registration certificate valid for a sole branch.[17] This said license has one-year duration and does not allow the entity to engage itself in retail banking in the local market or lending to local companies. It only allows lending and exchanging foreign currencies to foreign companies and local banks. Hence, foreign authorized banks are not allowed to carry out the same operations than a bank incorporated in Myanmar (see Figure 4). In the case of a non-bank financial institution, it could eventually be involved in one or all of the following businesses:[18]

(a) Financial Company Businesses;
(b) Leasing Businesses;
(c) Factoring Businesses;
(d) Credit Cards Businesses;
(e) Financial Services Businesses;
(f) Such other Credit service Businesses as may be prescribed by the Central Bank; or
(g) Such other Businesses as may be permitted accordingly by the Central Bank.

[15] Aye ThidarKyaw, Parliament passes Financial Institutions Law, (28 January 2016) online : http://www.mmtimes.com/index.php/business/18698-parliament-passes-financial-institutions-law.html
[16] Article 34(a)(2).
[17] Article 25.
[18] Article 23

Figure 4:Comparison between Foreign Authorized Branches and Local Banks

Activities	Foreign Authorized Banks	Local Banks
Credit to foreign companies and local banking institutions	✓	✓
Retail banking		✓
Direct lending in local currency		✓
Lending limit	✓	
Minimum asset(reserve fund)	✓(25 %)	✓(25 %)
Minimum amount of assigned capital to be maintain in the country	✓ (amount to be determined by regulations)	N/A

It has to be noted that defined businesses[19] of each license may differ and its content is to the CBM discretion, rules and regulations to be disclosed.[20] Its issuance is conditional to fulfillment of the 3 criteria namely:[21]

- Promoting financial stability and financial system soundness;
- Influencing the credit situation for the interest of the Union; and
- Protecting the interest of the public relating to business operations or activities carried out by the non-bank financial institution or the representative office.

The year 2015 witnessed two waves of authorizations, introducing foreign entities for the first time in 50 years. Perhaps, in the near future, more foreign banks representative offices are expected to be granted the necessary licenses to operate in Myanmar. In 2015, nine reputable foreign financial institutions were granted foreign bank licenses by the FBLC to open a branch and conduct onshore wholesale banking business in Myanmar.

Foreign financial institutions with foreign bank licenses
ANZ Bank (Australia)
Industrial and Commercial Bank of China (China)
Bank of Tokyo-Mitsubishi UFJ (Japan)
Sumitomo Mitsui Banking Corp. (Japan)
Mizuho Bank (Japan)
Malaysia's Malayan Banking Berhad (May Bank)
Bangkok Bank (Thailand)
Overseas-Chinese Banking Corporation (Singapore)
United Overseas Bank (Singapore)

For 2016, three representative offices of foreign banks are most likely to be allowed to conduct activities in the country, according to the FBLC and the CBM shall announce annually a list of non-bank financial institutions and representative.[22] Two CBM directives have been issued along with a letter[23] in 2015, restricting all persons and companies from withdrawing foreign currency sums over USD 5,000 and limited to 2 times maximum per week. It constitutes a step backwards for Myanmar, as previous Central Bank Directives No. 10/2012 and 13/2012 were allowing two withdrawals per week of maximum USD10,000.

[19] Article 23.
[20] Article 26.
[21] Article 29(a) (1) to (3).
[22] Article 30.
[23] Central Bank Directive No. 16/2015 and 17/2015.

WHAT REMAINS THE SAME

Lending Limits

Some provisions remain unchanged such as the maximum amount a financial institution can lend to individual, enterprise, or economic group. It cannot exceed 20 percent of its capital, including reserves. Interestingly, this limitation does not apply to state-owned banks and this is contrary to the guiding principles of the World Bank.

Minimum Assets to be Maintained by all Regulated Entities

Similarly to the FIL of 1990, the NFIL prescribes that a bank shall maintain a reserve fund and transfer 25 percent out of the net profits of each year to the general reserve fund account annually as long as the amount of the reserve fund is equivalent to one hundred percent of its paid up capital.[24] This provision applies to commercial banks, development banks and branches of foreign banks. This ratio is also subject to CBM decision and may be reviewed from time to time. Related regulation yet to be published will also specify the minimum of liquid assets a bank has to maintain at all time in Myanmar[25] and a minimum amount of assigned capital to keep for foreign bank branches.[26]

Constitution Requirement

The law requires banks to become limited liability companies pursuant to provisions from the Myanmar Companies Act of 1914 and the Special Company Act of 1950.[27]

Figure 5: Main New features Introduced by the NFIL

	The old FIL	The new FIL	
		Financial Institution	Branch or Subsidiary of Foreign Institution
Reserve funds minimum requirement	10% of demand deposit and 5% of time deposit (comprising up to 75% of treasury bonds)	25% of its net profits	
Minimum capital requirement	MMK30 million	MMK20 billion	USD75,000,000
Lending limit	Unchanged (maximum 20% of the entity capital)		
Lending limit to individuals	5%	unavailable	unavailable
Licensing time limit	Any	Any	1 year for foreign institution

[24]Article 35.
[25]Articles 36 and 37.
[26]Article 38.
[27]Chapter 3, previously ruled by Article 3 of The Financial Institutions of Myanmar Law of 1990.

CONCLUDING THOUGHTS

From the above, Myanmar banking and finance system is undergoing a reform process where the CBM plays a major role. Opening doors to foreign entities in a restrictive way has two main objectives: (1) to protect local financial sector; (2) to encourage the transfer of knowledge and best practices. Myanmar wishes to reintegrate with regional and global markets by allowing foreign entries without prejudice to local entities' effective growth. Some economists are also pointing out that such a colossal reform has to be carried out carefully. Otherwise, distortions may occur if the credit is extended too quickly and the reform could be harmful to Myanmar's economy.[28] According to the Asian Development Bank, other ASEAN transitional economies can act as models for Myanmar because they went successfully through the same process in recent time: Vietnam (1990s), Cambodia (1995-1999) Lao (1980s).[29]

A combination of great diversity of natural resources and a strategic geographical location at the crossroads of China and India predicts a promising future for the country as long as the development and the promotion of the CBM's market-based policy tools remain a priority. The stage has been set for progress like the IMF's mission chief for Myanmar, Yongzheng Yang said "Myanmar has made impressive strides in economic reform, including in the dismantling of trade barriers and the opening of the banking sector".[30] Now it only remains to expect supplementary legislative amendments aiming to fully reach this goal of implementing a sound and trusted banking system. Finally, more details are yet to come and will be released by way of CBM regulations. In sum, paying a close attention to updates and following closely the implementation of the new regulation are the best way to take advantage of the revamped NFIL.

[28] GIZ, Myanmar's Financial Sector: A Challenging Environment for Banks (2013) online: https://www.giz.de/en/downloads/giz2013-en-financial-sector-myanmar.pdf

[29] ADB, Monetary Policy and Foreign Exchange Management: Reforming Central Bank Functions in Myanmar, Working Paper No. 431 (May 2015).

[30] IMF, Myanmar's Growth Momentum Strong, but Maintaining Stability Is Key (18 September 2015) online: http://www.imf.org/external/pubs/ft/survey/so/2015/car091815a.htm.

Milestone Dates of the Banking and Finance System of Myanmar

1990

- Central Bank of Myanmar Law (CBML) - creation of the CBM
- Financial Institutions of Myanmar Law (FIL)

1992

First Private Bank Licenses Issuance

2002

Control of Money Laundering Law and Regulations

Banking Crisis

2003

2004

Instructions regarding anti-laundering matters (AMT/CFT)

2005

Microfinance Law on microfinance operations and interest rate caps

2009

Myanmar agrees to open to regional foreign banks by 2015

2011

- Citizens Investment Law (CIL)
- The New Securities Exchange Law
- The New Central Bank of Myanmar Law

2012

- Foreign Exchange Management Law (FEML) – Managed Floating System
- New Foreign Investment Law (FIL) – 2012

2013

Drafting of the new Myanmar Foreign Investment Law – Combination of the CIL and FIL

2014

2015

- The NFIL awaiting the President’s signature
- Myanmar agrees to open to regional foreign banks

2016

- Myanmar Stock Exchange
- Release of the draft of the Regulation on Mobile Banking

CONTRIBUTORS

L-Martin Desautels
Managing Partner
Head of Banking and Finance Practice Group
Martin.Desautels@dfdl.com

William D. Greenlee, Jr.
Partner and Managing Director, Myanmar
William.Greenlee@dfdl.com

Lee-Dia Chaput
Legal Adviser
Lee-Dia.Chaput@dfdl.com

MarMar Aung
Legal Adviser
Marmar.Aung@dfdl.com

DFDL offices:

Bangladesh
Dhaka
bangladesh@dfdl.com

Myanmar
Naypyidaw
Yangon
myanmar@dfdl.com

Lao PDR
Vientiane
laos@dfdl.com

Singapore
Singapore
singapore@dfdl.com

Thailand
Bangkok
Samui
thailand@dfdl.com

Phuket
phuket@dfdl.com

Vietnam
Hanoi
Hanoi@dfdl.com

Ho Chi Minh City
hcmc@dfdl.com

DFDL collaborating firms:

Indonesia
Mataram Partners, Jakarta
indonesia@dfdl.com

Cambodia
Phnom Penh
cambodia@dfdl.com

Philippines
Ocampo & Suralvo Law Offices, Manila
info@ocamposuralvo.com