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Analysis of Recent Legal Developments in Southeast Asia

c o n t e n t s

Regulations for Foreign Banks in Cambodia, Laos, Myanmar, and Vietnam

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The rapidly growing middle class in Southeast Asia is bringing with it increased household wealth, increased consumption, and increased investment. With that increase, the commercial banking sector has seen a boom in the more economically developed countries of Southeast Asia—especially in Thailand. A select few foreign banks have been very successful in Cambodia, Laos, Myanmar, and Vietnam (CLMV) for many years, but as many banks seek to replicate their Thai success in these new markets, the field looks likely to become much more crowded in coming years. Six major Thai banks are active in at least one other jurisdiction in mainland Southeast Asia, with some already operating across them all, and many larger international banks also beginning to take note.

Amid that background, this article examines the legal frameworks for banks seeking to operate in those jurisdictions, and addresses some current and upcoming developments that investors should note.

Cambodia

Cambodia's legal framework is very favorable for foreign investors seeking to invest in the country's banking sector, as there are no restrictions on foreign ownership. Therefore, banks and other financial institutions can be 100% foreign owned.

Foreign investors/banks may structure their banking investments/expansion in Cambodia by way of a subsidiary, a branch, or a representative office. Subsidiaries and branches are both permitted to engage in banking activities in Cambodia, and, for a subsidiary, a foreign investor could incorporate a bank in Cambodia and own 100% of its shares, or acquire the shares of an existing bank. Representative offices, however, are only allowed to conduct market research and other activities that do not generate income or profit.

Cambodian law allows for the formation of commercial banks (which may be structured as either subsidiaries, locally incorporated banks, or branches), specialized banks, and microfinance institutions. Commercial banks are legal entities licensed to carry out banking operations, including (1) credit operations for valuable consideration, (2) the collection of non-earmarked deposits, and (3) the provision of means of payment to customers and the processing of payments in Khmer riel or foreign exchange. Specialized banks, on the other hand, are banks that only operate one of the above activities (typically lending, and without accepting deposits from the public).

Microfinance institutions (MFIs) provide financial services, such as loans and deposits, to poor and low-income households and to micro-enterprises. In general, MFIs are not permitted to collect deposits unless they obtain a separate license from the National Bank of Cambodia (NBC).

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Regulations for Foreign Banks (from page 1)

All banks operating in Cambodia must comply with the minimum capital requirements below.

Type of Bank	Minimum Capital
Commercial bank locally incorporated or incorporated as foreign subsidiary	KHR 300 billion (approx. USD 75 million)
Commercial bank registered as branch of foreign bank	
If parent bank has investment grade rating	KHR 200 billion (approx. USD 50 million)
If parent bank does not have investment grade rating	KHR 300 billion (approx. USD 75 million)
Specialized bank	KHR 60 billion (approx. USD 15 million)
Microfinance institution	
Non-deposit taking	KHR 6 billion (approx. USD 1.5 million)
Deposit taking	KHR 120 billion (approx. USD 30 million)

Establishing a bank and obtaining a banking license is a two-step application process at the NBC—first, an application for in-principle approval from the NBC, and then upon satisfying certain conditions, an application for final approval. Application review and approval takes approximately six months. If the NBC grants the banking license, this will be published in the NBC bulletin and the Official Gazette of the Kingdom of Cambodia.

Laos

The main relevant legislation is the Law on Commercial Banks No.56/NA, as amended, dated December 7, 2018. This addresses a number of issues with regard to operation of commercial banks in Laos.

Minimum Registered Capital

The minimum registered capital for commercial banks does not differ for local or foreign commercial banks to set up a bank in Laos and is currently set at LAK 500 billion (approx. USD 58 million), while the minimum registered capital for foreign commercial banks seeking to establish only a branch is LAK 300 billion (approx. USD 34.5 million). In-kind value may account for up to 10% of the registered capital. Capital-in-kind can be immovable property or movable property in Laos used in the operation of the business of the commercial bank.

Internal Governance

A board of directors with at least five members must be created. The term is three years, and members can be re-elected for up to three consecutive terms. The board must include at least one external member—someone who is not an employee of the commercial bank and who has no family connections or contractual relationship with, or business benefits related to, a shareholder or executive of the commercial bank. This prohibition extends to other business interests unrelated to the bank. For example, an external member cannot be employed even on a temporary or ad hoc basis by a bank shareholder's other company. Internal governance also relies on three required committees—(1) the Governance Committee, (2) the Risk Management Committee, and (3) the Audit Committee—with the option of creating additional committees if desired. Eventually, a directors' council consisting of the director and the deputy director must also be set up. Appointment and dismissal of executives must receive consent from the Bank of Laos (BOL), which is responsible for supervising commercial banks.

Banking Activities

The law permits commercial banking activities, which generally encompass the typical services provided by a commercial bank—including the sale and purchase of foreign currency, as well as an allowance for the BOL to approve specific activities that are not listed in the law.

A commercial bank investing in another company that is not in securities businesses, insurance businesses, or financial businesses as further discussed below can invest only up to 10% of the registered capital of the commercial bank and cannot end up controlling more than 20% of the total shares having voting rights in the target legal entity. Commercial banks can either set up their own entity or hold shares in securities businesses, insurance businesses, financial leasing operations, or other types of financial business upon the BOL's approval.

Foreign Financing of Commercial Banks

On December 10, 2019, the BOL issued Notice No. 684/BOL prohibiting financial institutions from obtaining loans from foreign legal entities or individuals that are not financial institutions or are not approved by the relevant authority of the country of origin for providing loans.

Myanmar

The Central Bank of Myanmar (CBM), the financial authority for the banking industry in Myanmar, has implemented a step-by-step approach toward modernization and development of the banking industry in Myanmar. This has moved from permitting only local entrepreneurs to set up banks, to allowing foreign bank operators to open bank representative offices, and then to allowing foreign bank branches to provide onshore wholesale banking services. Finally, on November 7, 2019, the CBM announced a new round of foreign bank licensing that will involve the opening of the retail banking market to foreign banks at the beginning of 2021.

The CBM is currently requesting expressions of interest for a new licensing round. This round of foreign bank licensing will be open to foreign banks with representative offices in Myanmar, and will make two license types available: branch licenses and subsidiary licenses.

With a branch license, foreign banks will be able to engage in onshore wholesale banking business, as was already permitted for foreign bank branches in Myanmar. These branches require a minimum paid-in capital of USD 75 million for operation, of which USD 40 million must be locked-up for two years with the CBM. Apart from onshore wholesale banking, foreign bank branches are permitted, under Directive 9/2017 of the CBM, to provide export financing and related banking services for export financing to local companies.

However, with a subsidiary license, from January 1, 2021, foreign banks will be permitted, with a minimum paid-in capital of USD 100 million, to conduct onshore retail banking activities. This will permit the establishment of up to 10 places of business or off-site ATMs—a huge development and major liberalizing step in the Myanmar banking sector.

Existing foreign bank branches will be permitted to convert to subsidiaries from June 2020, provided they have operated as a branch in Myanmar for at least three years.

A more recent change—with effect as from January 1, 2020—is that foreign ownership in a Myanmar bank exceeding 35% of the capital of the domestic bank is now permitted with the approval of the CBM on a case-by-case basis. Equity investment exceeding the 35% cap by foreign banks or financial institutions was previously outlawed by the CBM (under Circular 1/2019). However, the Myanmar Companies Law 2017 states that a local Myanmar company can only accept foreign equity investment of up to 35% without changing the status of the company to be "foreign owned." Though there has not yet been clarification, it seems likely that, to be consistent with the Myanmar Companies Law, local banks would have to change their status to be foreign banks after accepting foreign investment of more than 35% of the bank's capital (as calculated after the capital injection).

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Rules for Foreign Banks in CLMV (from page 2)

Vietnam

Vietnam is fairly open in terms of market access in the banking sector. Foreign investors may set up a commercial presence or purchase shares of an existing financial institution in Vietnam. A new commercial presence may be (1) a representative office, (2) a branch of a foreign bank, (3) a wholly foreign-owned commercial bank, (4) a finance company, (5) a financial leasing company, or (5) a microfinance institution.

While both foreign banks and other financial institutions may establish representative offices to carry out activities that do not generate income or profit, only foreign banks are permitted to set up branches to engage in banking activities such as lending, taking deposits, and account opening. Neither representative offices nor branches of foreign banks are considered legal entities, so foreign investors must take full responsibility for the activities of their representative offices or branches.

In theory, foreign investors may establish a wholly foreign-owned commercial bank under Vietnamese law. As of June 30, 2019, the State Bank of Vietnam (SBV) had licensed nine wholly foreign-owned banks. However, the issuing of new licenses for such banks will likely be limited or possibly even discontinued in the future. Thus, foreign banks may find it easier to set up a branch or a representative office.

As for purchasing shares of existing local banks, a foreign investor together with its affiliates must not exceed 20% ownership of the charter capital of a local commercial bank, and the aggregate ownership of all foreign investors in a local commercial bank is capped at 30% of its charter capital. The scope of operation of commercial banks in Vietnam includes a wide range of products and services, from traditional financial products to fund management and securities business.

In contrast, foreign investors may own 100% of the shares of a finance or financial leasing company in Vietnam. The company may engage in certain banking activities but cannot take deposits from individuals or provide payment services via clients' accounts.

Microfinance institutions mainly provide services such as taking deposits from low-income individuals and households and micro-enterprises. As of June 30, 2019, there were only four licensed local microfinance institutions in Vietnam.

In order to set up a commercial presence in Vietnam, foreign investors must satisfy, among other conditions, the minimum legal capital requirement as follows:

Type of Presence	Minimum Capital
Representative office	N/A
Branch of foreign bank	USD 15 million
Commercial bank	VND 3,000 billion (approx. USD 129 million)
Finance company	VND 500 billion (approx. USD 21.5 million)
Finance leasing company	VND 150 billion (approx. USD 6.5 million)
Microfinance institution	VND 5 billion (approx. USD 215,000)

To engage in banking activities, a foreign credit institution (e.g., banks, branches, and finance/financial leasing companies) must obtain an establishment and operation license upon satisfying conditions on legal capital and so on. The statutory timeline for issuing a banking license is approximately seven months, but in practice it often takes much longer. If the SBV grants the banking license, this will be published on the official website of the SBV and in three consecutive issues of a local daily newspaper (including online news).

Conclusion

The countries of mainland Southeast Asia offer good opportunities to foreign banks and investors looking to gain or strengthen their presence in the region. Banks currently in different stages of expansion in these countries—as well as those ready to embark on expansion in the region—should consider the various issues related to setting up, licensing, capital and operational requirements, permitted and restricted activities, and so on, as detailed in this article, to determine the relative ease of market entry and operation versus the potential risks and rewards of doing so. With careful planning and foresight each of these markets offers attractive opportunities for banking sector operators looking to expand.