The Banking Regulation Review

Third Edition

Editor
Jan Putnis

Law Business Research

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THE BANKING REGULATION REVIEW

Third Edition

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CONTENTS

Editor's Preface xvii
Jan Putnis

Chapter 1 **International Initiatives** 1
Jan Putnis and Tolek Petch

Chapter 2 **Argentina** 29
Santiago Carregal, Martín G Vázquez Acuña and Josefina Tobias

Chapter 3 **Australia** 41
Louise McCoach and David Landy

Chapter 4 **Austria** 76
Wolfgang Freund

Chapter 5 **Barbados** 86
Trevor A Carmichael QC

Chapter 6 **Belgium** 95
Anne Fontaine

Chapter 7 **Brazil** 107
José Eduardo Carneiro Queiroz

Chapter 8 **Cambodia** 113
Bun Youdy

Chapter 9 **Canada** 127
Scott Hyman, Carol Pennycook, Derek Vesey and Nicholas Williams

Chapter 10 **Cayman Islands** 143
Richard de Basto

Chapter 11 **China**..154
Wantao Yang, Emily Xiaoqian Wang and Carol Dongping Cao

Chapter 12 **Colombia**...175
Diego Muñoz-Tamayo

Chapter 13 **Denmark** 191
Tomas Haagen Jensen and Tobias Linde

Chapter 14 **El Salvador** 203
Aquiles A Delgado and Oscar Samour

Chapter 15 **European Union** 214
Jan Putnis and Benjamin Hammond

Chapter 16 **Finland** 236
Tarja Wist and Jussi Salo

Chapter 17 **France**...247
Olivier Saba, Samuel Pariente, Jennifer Downing, Jessica Chartier and Hubert Yu Zhang

Chapter 18 **Germany**..278
Thomas Paul and Sven H Schneider

Chapter 19 **Greece**...292
Dimitris Passas and Vassilis Saliaris

Chapter 20 **Guatemala** ... 312
María Fernanda Morales Pellecer

Chapter 21 **Guernsey** ... 325
John Lewis and Jeremy Berchem

Chapter 22 **Hong Kong** ... 337
Laurence Rudge and Peter Lake

Chapter 23 **Hungary** ... 353
Zoltán Varga and Tamás Pásztor

Chapter 24 **India** ... 366
Shardul Thacker

Chapter 25 **Indonesia** ... 379
Ferry P Madian and Yanny Meuthia S

Chapter 26 **Ireland** ... 398
Carl O'Sullivan, William Johnston, Robert Cain and Eoin O'Connor

Chapter 27 **Italy** ... 410
Giuseppe Rumi and Andrea Savigliano

Chapter 28 **Japan** ... 421
Hirohito Akagami, Toshinori Yagi and Wataru Ishii

Chapter 29 **Jersey** ... 432
Simon Gould and Sarah Huelin

Chapter 30 **Korea** ... 444
Sang Hwan Lee, Chan Moon Park and Hoin Lee

Chapter 31 **Latvia** 457
Armands Skudra

Chapter 32 **Luxembourg** 468
Franz Fayot

Chapter 33 **Malaysia** 485
Andri Aidham bin Dato' Ahmad Badri, Julian Mahmud Hashim and Tan Kong Yam

Chapter 34 **Malta** 495
David Griscti and Clint Bennetti

Chapter 35 **Netherlands** 506
Joost Schutte, Annick Houben and Mariken van Loopik

Chapter 36 **New Zealand** 519
Debbie Booth and Guy Lethbridge

Chapter 37 **Nicaragua** 533
Rodrigo Taboada R

Chapter 38 **Nigeria** 545
Adamu M Usman and Jumoke Onigbogi

Chapter 39 **Norway** 560
Terje Sommer, Markus Nilssen and Mats Nygaard Johnsen

Chapter 40 **Philippines** 571
Rafael A Morales

Chapter 41 **Poland** 586
Tomasz Gizbert-Studnicki, Tomasz Spyra and Michał Bobrzyński

Chapter 42 **Portugal** 600
Pedro Cassiano Santos

Chapter 43 **Romania** 615
Adela-Ioana Florescu and Diana-Maria Moroianu

Chapter 44 **Saudi Arabia** 626
Johannes Bruski and Julian Johansen

Chapter 45 **Singapore** 635
Elaine Chan

Chapter 46 **Slovakia** 649
Sylvia Szabó

Chapter 47 **South Africa** 663
Johan de Lange and Matthew Gibson

Chapter 48 **Spain** 677
Juan Carlos Machuca

Chapter 49 **Sweden** 699
Niclas Rockborn and Nils Unckel

Chapter 50 **Switzerland** 715
Shelby R du Pasquier, Patrick Hünerwadel, Marcel Tranchet and Valérie Menoud

Chapter 51 **Taiwan** 736
Chun-yih Cheng

Chapter 52 **Thailand** 749
Montien Bunjarnondha and Rahat Alikhan

Chapter 53 **Turkey** 763
Serdar Paksoy and Nazlı Bezirci

Chapter 54 **United Arab Emirates** 775
Amjad Ali Khan and Stuart Walker

Chapter 55 **United Kingdom** 783
Jan Putnis, Michael Sholem and Nick Bonsall

Chapter 56 **United States** 821
Luigi L De Ghenghi and Reena Agrawal Sahni

Chapter 57 **Vietnam** 887
Samantha Campbell, Pham Bach Duong and Nguyen Thi Tinh Tam

Appendix 1 **About the Authors** 907

Appendix 2 **Contributing Law Firms' Contact Details** 942

EDITOR'S PREFACE

Jan Putnis

When the first edition of this book was published in mid-2010, banking regulation seemed to be undergoing a transformation driven by a reasonably coherent international agenda. There were questions about how long it would be before nationalist and protectionist tendencies fractured the broad consensus that seemed to have built up on such issues as the need for more and better quality capital resources, liquidity requirements and the strengthening and reform of vital market infrastructure. However, there appeared to be a reasonable degree of certainty about the direction and speed of reform, at least among the G20 countries.

Events, as they always do, have since conspired to make the position considerably more complicated, in two separate ways. First, achieving many of the regulatory reforms agreed in principle at the meeting of G20 leaders in London in 2009 has proved to be a far more complex and difficult task than even those expert in the field of banking regulation had expected. Secondly, as concerns about solvency have spread to governments, sovereign debt has assumed centre stage. The eurozone crisis, as it has come to be known, rumbles on with no obvious short-term solution that would avoid significant economic and social upheaval in parts of the European Union. There is also the potential existential threat that sovereign defaults of eurozone countries would pose to banks that are either established in those countries or have significant exposure to banks or assets in those countries. Events in the eurozone have given the frenetic activity in the area of financial regulatory reform in the European Union a slightly surreal quality against the backdrop of the consequences of potential economic and financial upheaval in one or more eurozone countries. Meanwhile, in the United States, the rule-making process under the Dodd-Frank Act has continued, behind its original schedule, and banks continue to digest the consequences of the Volcker rule.

On both sides of the Atlantic the volume and complexity of new and proposed rules has continued to be a cause of criticism and frustration. A banking sector that was roundly blamed for creating the complexity in products, markets and business structures that exacerbated aspects of the financial crisis is facing the irony of a wall of

new regulation of such complexity that the complexity itself might end up being the main reason that the new regulation fails to achieve its objectives.

Separately, in many Asian financial centres reforms are underway but are, in general, far behind those proposed and enacted in the United States and the European Union. Many governments, regulators and bankers in Asia saw (and continue to see) the western financial crisis of 2007–2009 as exactly that, a western financial crisis, and view the gradual liberalisation of the Chinese banking system and greater convertibility of the renminbi as the greater challenge and opportunity.

If we set ourselves the task of summarising the positive things that have emerged for banking regulation from that western financial crisis, what would we say now, three years on? There is little doubt that there is now much greater awareness among policymakers and regulators in all major jurisdictions of two important factors that will probably dominate any future international banking crisis:

a Banks, however well capitalised, risk collapse in sufficiently extreme circumstances and the crisis demonstrated that those circumstances should never be regarded as too extreme to contemplate. Assumptions about the credit quality and liquidity of assets, and about withdrawal of sources of funding (including deposits), may cease to apply in stressed market conditions. That means that the maturity transformation role of banks ('borrowing short term and lending long term', as it is often simplistically described) makes them subject to existential threats that are, by their very nature, difficult to anticipate and address accurately.

b Contagion can spread through financial systems in unexpected ways, or at least in ways that are unexpected by governments and regulators. Studying the potential routes of contagion and considering whether there are ways of closing down those routes without adverse unintended consequences for economies that are recovering from recession is therefore an important aspect of regulatory endeavour.

It might seem incredible now that these points were not appreciated sufficiently by governments and regulators before the financial crisis first erupted in the United States in 2007 and then spread to Europe in the following year. But that was undoubtedly the case.

The past year has seen international banking groups grappling with the practical realities of regulatory reform. Doubts about the ability of some banks to raise the additional capital (particularly Tier I capital) that they will require in order to meet the gradually increasing capital requirements set out in the Basel III agreement are feeding concerns about the long-term viability of some banks' business models and, more generally, about previously long-held expectations as to returns on equity of banking groups. Banks have begun to respond to actual and prospective higher capital requirements, in some cases by raising equity with varying degrees of success (which has been difficult in the market conditions prevailing in most of the world in the past year) and in other cases by selling or preparing to sell assets and business units, or simply by closing down business lines.

Politics have intervened in banking in the past year in ways that have made the debate about the direction of regulatory reform in the banking sector more complicated. In some countries, concern about the remuneration of senior management of banking groups has reached fever pitch in the media while, at the same time, a less emotive and

generally more thoughtful debate has continued on the need for more financing for businesses, particularly small and medium-sized enterprises.

The apparent shortage of finance for businesses in many economies, coupled with expected further pressure on the ability of banks to provide that finance as their capital requirements continue to increase, has led to concerns about the development of other sources of finance. Is credit risk, and the contagion to which it can give rise if borrowers default, shifting in dangerous ways out of the banking sector into the so-called 'shadow banking sector'? The European Commission looks set to start investigating this topic in earnest in 2012. The consequences of regulatory intervention in this area are currently very difficult to predict, not least because any attempt to regulate non-bank sources of finance more heavily is bound to attract criticism from those who claim that it will only reduce further the sources of finance available to the 'real' economy.

Another area of regulatory reform that banking groups continue to grapple with in 2012 is transparency with regulators. There are various examples of the ways in which this is starting to affect the sector. The most immediate and relevant example concerns the work that many of the largest banking groups in the United States and Europe are currently involved in to draw up 'recovery plans' and to draw up, or to assist their regulators in drawing up, 'resolution plans', those plans being collectively (and somewhat misleadingly) referred to as 'living wills'. The phrase of the moment is 'barriers to resolution', describing factors that would prevent or inhibit the orderly resolution of a bank at or close to its collapse. Plenty of barriers to resolution are being identified as recovery and resolution plans are prepared. The second half of 2012 and 2013 will likely be an interesting period in which regulators ponder these barriers and deepen their discussions with banking groups as to what might be done about them.

Fears of enforced structural reorganisations and changes to business models have led some banking groups to spend considerable amounts of time and resources developing their own solutions to perceived barriers to resolution. More immediately, the process of preparing recovery and resolution plans has proved difficult, the main challenges including how to reconcile differences between the statutory resolution and insolvency procedures for banks in different jurisdictions and to understand the cross-border elements of those procedures. Fundamental questions about the availability of cross-border services to banking operations in a crisis, the treatment of banks' global hedging arrangements, and ultimately the resolvability of banking groups, are at stake. It seems likely that we are many years away from having recovery and resolution plans that carry the benefit of clarity around how regulators would operate them on a cross-border basis in a crisis. It also remains to be seen whether cross-border cooperation between regulators would work in such circumstances given the significant differences between national resolution and insolvency procedures and the desire in many jurisdictions to protect local depositors. Another major area of uncertainty concerns the proposals by some regulators that debt issued by banking groups be 'bailed in' (i.e., written off or converted into equity) in a crisis and how that could happen without spreading contagion through the banking system and the wider economy via the holders of that debt.

Meanwhile, scrutiny of the structure of banks themselves has continued in some countries. The likely implementation in the United Kingdom of proposals to require the 'ring-fencing' of retail banking activities within banking groups may be the start of a trend that spreads to other countries. Despite the prevalence of 'universal' banks,

combining retail and investment banking activities in single legal entities in many of the other Member States of the European Union, the European Commissioner for the Internal Market has commissioned a study into the structure of banks with a remit to consider ring-fencing of retail banking.

Liquidity has remained a central concern for many banking groups in the past year. Short-term liquidity problems at banks (arising, in particular, from concerns about the strength of some banks as counterparties) have resulted in an increase in the range of funding for which banks generally are now expected to provide collateral. This trend is expected to be exacerbated by longer-term developments such as the Basel III requirements on liquidity and the proposed introduction of depositor preference in some countries for the first time. Liquidity pressures have led to many banks engaging in new types of transactions, such as so-called 'liquidity swaps', to increase the amount of high-quality collateral that they have available for their funding operations. This ongoing search for liquidity, and for the collateral required to obtain liquidity, has made some financial regulators concerned about the potential spread of contagion within the banking sector and from the banking sector to other sectors. For example, some liquidity swap transactions have involved banks receiving liquid assets from insurers in return for assets that are less liquid.

This third edition of *The Banking Regulation Review* updates the position on important aspects of banking regulation in the countries covered, in most cases to February 2012. While the book is aimed principally at staff in the legal and compliance departments of banks, it is to be hoped that senior management also find it helpful. The book focuses most closely on the deposit-taking activities of banks. The constraints of space and time mean that it will never be possible to do full justice to all of the subjects covered in each chapter, but readers are of course welcome to contact me if they have any suggestions for future editions.

Preparing successive editions of this book continues to be an onerous task for the busy lawyers who contribute the chapters and who are otherwise much in demand. My thanks go to them for their dedication to the task. Significant changes to a book such as this also mean much more work than would otherwise be the case for the publisher. I am therefore very grateful to the publisher's team for their understanding, hard work and patience with a group of authors who often have many other commitments.

Finally, I would like to thank the partners and staff of the financial regulation group at Slaughter and May for appreciating this book's value and for encouraging our involvement in it for a third successive year.

Jan Putnis
Slaughter and May
London
April 2012

Chapter 57

VIETNAM

Samantha Campbell, Pham Bach Duong and Nguyen Thi Tinh Tam[1]

I INTRODUCTION

Vietnam's current banking system can be traced back to 1988 when four state-owned banks, the Bank for Foreign Trade of Vietnam ('Vietcombank'), the Vietnam Bank for Industry and Trade ('Vietinbank'), the Bank for Investment and Development of Vietnam ('BIDV') and the Bank for Agriculture and Rural Development of Vietnam ('Agribank'), were separated from the State Bank of Vietnam ('SBV') with a mandate for commercial banking activities.

The public banking sector, composed currently of five state-owned commercial banks ('SOCBs', commercial banks in which the state retains an interest greater than 50 per cent), still dominates the market.

Since Vietnam's accession to the World Trade Organization ('WTO') effective 1 January 2007, the government has been pursuing a policy of partial privatisation (known in Vietnam as 'equitisation') of some of the state-owned banks with a view to opening up and attracting funds to the banking sector. To date, three SOCBs have been equitised (Vietcombank in 2007, Vietinbank[2] in 2008 and BIDV in 2011) with the state retaining up to 90 per cent of shares in each bank following the initial public offering, although sales of significant shareholdings to strategic foreign investors occurred in 2011. Mekong Housing Bank also received SBV approval to equitise but the process is generally perceived to be proceeding more slowly than investors had hoped, due in part to the global financial crisis and serious difficulties encountered by the domestic banking

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1 Samantha Campbell is a resident partner and Pham Bach Duong and Nguyen Thi Tinh Tam are senior associates at Gide Loyrette Nouel AARPI.

2 In January 2011, the International Finance Corporation ('IFC') and its affiliate subscribed up to 10 per cent of the shares of Vietinbank. This is the first acquisition of a participation by a foreign investor in a SOCB. In September 2011 Mizuho Bank acquired 15 per cent of the shares in Vietcombank.

system in 2011. Agribank, the largest of the five SOCBs by assets, given its broader social mission was transformed into a one-member limited liability company with the state being the sole member.

Another trend in Vietnam is the deepening presence of a number of global banks. In 2009, following a change in legislation,[3] the SBV granted five licences permitting HSBC, Standard Chartered, ANZ Bank, Korea's Shinhan Bank and Malaysia's Hong Leong Bank to establish entirely foreign-owned subsidiary banks incorporated in Vietnam. Most of them announced good results in 2011 despite a difficult international and domestic environment.

Foreign banks have also, sometimes in parallel with other forms of local presence, acquired minority 'strategic stakes' in most of the important Vietnamese banks.

The Vietnamese banking sector, which seemed to have weathered the global financial crisis relatively well, started to feel its impact in 2011. The relative isolation from the international financial markets has not protected the country from growing liquidity problems. The widely praised short-term fiscal stimulus package and an interest rate subsidy scheme adopted as a quick response to the crisis did limit the impact of reduced international demand for Vietnamese exports but has led to macro-economic imbalances. The most serious of them are extremely high inflation peaking at 23 per cent per year in August (the highest rate in South East Asia) and a large trade deficit. Memories of an inflation rate of up to 28.3 per cent witnessed in August 2008 are still vivid. The government and the SBV had to adopt a series of strong measures aimed at re-stabilising the economy. The fight against the inflation became the top priority of the government which was prepared, for the first time since the start of the country's economic reforms, to sacrifice the country's economic growth. The flurry of new regulations significantly restricted banking activity in 2011, leaving many smaller commercial banks in serious difficulties. These measures are expected to be maintained until early 2013.

Currently Vietnamese banks are principally lenders to large corporations, including a high proportion of state-owned enterprises ('SOEs'), although the sector remains relatively unsophisticated. Consumer banking is still in its early stages and remains undeveloped.[4] Low market penetration is viewed as providing potential for expansion into lending to smaller enterprises and consumer banking as income levels rise. GDP growth achieved in 2011 was lower than the initial projections but was still almost 6 per cent, which maintains the Vietnamese banking sector's attractiveness from an investment perspective, with Vietnamese and foreign banks vying for market share.

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3 Decree 22/2006/ND-CP dated 28 February 2006 issued by the government of Vietnam on organisation and operation of foreign bank branches, joint venture banks, banks with 100 per cent foreign-owned capital and representative offices of foreign credit institutions in Vietnam ('Decree 22').

4 As of December 2009, an estimated 20 per cent of Vietnam's population had bank accounts and around half of those with accounts actively used consumer banking services (*Vietnam Financial Review*, 'Vietnam's Retail Banking Report', 12 January 2011).

Although the Vietnamese banking and finance sector is growing rapidly, there is still a significant lack of know-how, management experience and enforceable governance controls.

II THE REGULATORY REGIME APPLICABLE TO BANKS

Banking activity in Vietnam is governed by the Law on the State Bank of Vietnam ('the SBV Law') and the Law on Credit Institutions ('the LCI') both passed on 16 June 2010 and effective from 1 January 2011,[5] as well as a number of implementing decrees, circulars and decisions issued by the government, the SBV and the Ministry of Finance.

The cross-border supply of banking services into Vietnam is heavily restricted by Vietnamese law. Offshore banks may generally not provide services to Vietnamese entities, with the notable exception of hard currency loans (which are subject to strict exchange control regulations).

The SBV performs the traditional role of a central bank and regulates the banking system in Vietnam by working closely with the Ministry of Finance and the SBV's network of provincial branches. Through its Banking Inspection and Supervisory Agency,[6] the SBV is the authority empowered to grant establishment and operating licences to banks in Vietnam. The State Securities Commission ('SSC') regulates all securities activity in Vietnam, including securities activities carried out by commercial banks.

The scope of a credit institution's permitted activities is specified in its banking licence. Banks may only participate in the domestic and international foreign exchange and gold markets, including in respect of international payment services, upon receiving specific permission from the SBV.[7]

A commercial bank may undertake deposit-taking activities, provided it opens its own deposit account at the SBV with the minimum compulsory reserve level. After unsuccessful attempts to control escalating deposit interest rates fuelled by illiquidity through voluntary agreements between the SBV and the Vietnam Banking Association,[8] the SBV finally decided to use strong administrative measures to enforce its interest rates policy. SBV Circular 02/2011/TT-NHNN dated 3 March 2011, replaced later by Circular 30/2011/TT-NHNN dated 28 September 2011, imposed strict fines on banks that do not comply with the deposit interest ceiling of 6 per cent on deposits under one month and of 14 per cent on deposits over one month.

Banks may also, of course, conduct lending activities and, with effect from April 2010, the statutory ceiling on the interest rate (fixed by the Civil Code at 150 per cent

---

5 The new laws replace the Law on the State Bank of Vietnam and the Law on Credit Institutions adopted in 1997 and amended in 2004.

6 Established by Government Decree No. 96/2008/ND-CP dated 26 August 2008 ('Decree 96').

7 As from 31 July 2010, banks and gold traders are no longer permitted to trade gold on onshore and offshore accounts under Circular 01/2010/TT-NHNN dated 6 January 2010 as amended by Circular 17/2010/TT-NHNN dated 29 June 2010.

8 Official Letter of the Vietnam Banking Association number 250/HHNH dated 15 December 2010.

of the basis rate announced by the SBV, and lifted in 2009 with respect to consumer-lending activities only) was removed with respect to all forms of bank loans in local currency.[9] Since February 2012, Vietnamese banks may lend to offshore affiliates and subsidiaries of Vietnamese companies subject to registration with the SBV.[10] Lending to other offshore entities remains subject to specific SBV approval, rarely granted on a case-by-case basis.

Banks are also not permitted to provide loans to enterprises that they control and that operate in the securities sector, nor are they permitted to provide unsecured loans for investment in any business in the securities sector.[11]

As well as the usual deposit-taking and lending activities, a commercial bank may also act as a custodian bank for securities following receipt of a registration certificate from the SSC with the function of providing depository services and supervising the management of public funds and securities investment companies.[12] The assets that the bank manages as custodian must be held separately from its other assets. The duties of a custodian bank can also include the certification of reports prepared by a fund management company or securities investment company (as applicable).

A commercial bank may operate as an agent to provide insurance products and services for Vietnamese customers through its banking channels with the approval from the SBV.[13]

Banks established in Vietnam must operate under one of the following permitted forms:

a state-owned commercial bank established and organised in the form of a one-member limited liability company where 100 per cent of the charter capital is owned by the state;[14]

b joint-stock commercial bank (i.e., a company limited by shares);

c joint venture commercial bank established and organised in the form of a limited liability company;[15] and

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9 Circular 12/2010/TT-NHNN of the SBV dated 14 April 2010 replaced Circular No. 07/2010/TT-NHNN dated 26 February 2010 which at the time only partially removed the cap on dong lending interest rate for commercial medium and long-term loans to borrowers operating in the areas of 'production, business, services and investment for development'.

10 Article 8 of Circular 45/2011/TT-NHNN dated 30 December 2011 on the foreign exchange control applicable to lending and collection of loans outside Vietnam by credit institutions.

11 Article 126.4 of the LCI.

12 Article 98.2 and Article 6.14, Law on Securities.

13 Article 106 of the Law on Credit Institutions; as an example, Standard Chartered Bank was licensed in January 2010 to provide insurance agency services.

14 Once the equitisation of SOCBs is completed as currently envisaged by official decisions there will remain only one wholly state-owned commercial bank. SBV Decision 214/QD-NHNN dated 30 January 2011 approved the transformation of the Agribank into a one member limited liability company owned by the state and there are no plans currently for it to equitise.

15 There are currently only four joint venture banks in Vietnam: Indovina Bank Limited, Vietnam Russia JV Bank, VID Public Bank and Vinasiam Bank.

d entirely foreign-owned commercial bank established and organised in the form of a limited liability company.[16]

Mutual structures are contemplated by law and exist most commonly in rural areas under the similar forms of cooperative banks and people's credit funds. Limited liability micro-finance institutions can also be established to provide credit services to individuals, households and micro-enterprises.

i Restrictions on foreign ownership in Vietnamese banks and foreign banks

Despite the liberalisation of the banking sector, the acquisition by foreign entities of a shareholding in a Vietnamese commercial joint-stock bank is still subject to significant restrictions. All such acquisitions must be approved in writing by the governor of the SBV.[17]

As a rule, the total aggregate shareholding of foreign investors in a Vietnamese bank may not exceed 30 per cent of its 'charter capital'.[18] The total aggregate shareholding of a foreign credit institution and its affiliated persons must not exceed 10 per cent,[19] and the shareholding of any single foreign investor and its affiliated persons (not being credit institutions), may not exceed 5 per cent[20] of the charter capital of a Vietnamese bank.[21]

However, the law does permit a foreign 'strategic investor'[22] and its affiliated persons to acquire up to 15 per cent[23] of the charter capital of a Vietnamese bank, subject to a longer lock-in period from the acquisition (five years against three years for other foreign credit institutions).[24] A number of foreign banks and financial institutions have,

16 Banks established offshore may operate in Vietnam through a wholly owned subsidiary and/or branches or representative offices with a more limited scope of permitted activities. Unlike its predecessor, the new LCI does not consider foreign bank branches as a form of credit institution. This has created a number of issues in relation to the interpretation of the scope of current banking regulations which referred to foreign bank branches as credit institutions authorised by the SBV to operate in Vietnam (Article 4.8 and 4.9 of the LCI).

17 Article 5 of Decree 69/2007/ND-CP dated 20 April 2007 and issued by the Government of Vietnam on foreign investors purchasing shares of Vietnamese commercial banks ('Decree 69').

18 Article 4.1 of Decree 69.

19 Article 4.3 of Decree 69.

20 Article 4.2 of Decree 69.

21 Article 4 of Decree 69.

22 Defined as 'a reputable foreign credit institution with financial capacity and the ability to provide assistance to a Vietnamese bank during the development of banking products and services, raising managerial and executive capability, and applying modern technology, and which has strategic advantages connected with the strategy for development of the Vietnamese bank, which satisfies the specific criteria stipulated by the Vietnamese bank'.

23 Article 4.4 of Decree 69.

24 Article 13.1 of Decree 69.

in the past five years, made such acquisitions.[25] In special cases, the prime minister, based on the proposal of the governor of the SBV, may permit a foreign strategic investor to purchase up to 20 per cent of the charter capital of a Vietnamese bank.[26] Foreign strategic investors in SOCBs undergoing equitisation must also go through a special SBV approval procedure set out in Circular 10/2011/TT-NHNN dated 22 April 2011 of the SBV on providing the criteria for selecting strategic shareholders to the equitised state-owned commercial banks.

Since 1 April 2007 – and in accordance with Vietnam's WTO accession undertakings – entirely foreign-invested banks, in which one of the foreign shareholders is a 'parent bank' holding a majority equity interest, may be established in Vietnam.[27] The parent bank must have total assets of more than US$10 billion at the end of the year prior to application. Entirely foreign-owned banks must comply with Vietnamese prudential requirements on a stand-alone basis.

Foreign banks may also open branches as subsidiary units with no separate legal status.[28] The parent bank must have total assets of more than US$20 billion at the end of the year prior to application. A foreign bank branch may not open transaction points at locations other than its registered branch office, which, in practice poses real practical problems for the expansion by foreign banks of their activities in Vietnam.

Some foreign banks operate through representative offices, which are prohibited from conducting commercial operations in Vietnam.[29] A representative office merely acts as a link between the parent bank and their clients in Vietnam. As such, its activity

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25 At the current time:

a Standard Chartered Bank: 15 per cent of Asia Commercial Bank (ACB);
b HSBC: 20 per cent of Vietnam Technological and Commercial Bank (Techcombank);
c United Overseas Bank: 20 per cent of Phuong Nam Bank (Southern bank);
d Sumitomo Mitsui Financial Group: 15 per cent of Export Import Bank (Eximbank);
e Malayan Banking Berhad: 20 per cent of An Binh Bank (AB Bank);
f Societe Generale Bank: 20 per cent of Dong Nam A Bank (SEA Bank);
g BNP Paribas: 20 per cent of Phuong Dong Bank (Oricombank);
h Deutsche Bank: 10 per cent of Hanoi Building Bank (Habubank);
i Oversea-Chinese Banking Corporation: 15 per cent of Vietnam Prosperity Bank (VP Bank);
j Commonwealth Bank of Australia: 20 per cent of Vietnam International Bank (VIB);
k International Finance Corporation (IFC): 10 per cent of Vietinbank; and
l Mizuho Bank: 15 per cent of Vietcombank

Of note, ANZ has recently completed its divestment in Sacombank (15 per cent, the bulk of which was sold to Eximbank, a large local commercial bank).

26 On 17 August 2008, HSBC was the first foreign bank to increase its interest in Techcombank to 20 per cent. Many other foreign banks followed suit (see footnote 23).

27 Article 5.4 of Decree 59.

28 Article 7.4 of Decree 22.

29 Article 7.7 of Decree 22.

is generally limited to market research and the promotion and follow-up of the offshore parent entity's activities involving Vietnamese credit institutions or companies.[30]

III PRUDENTIAL REGULATION

i Relationship with the prudential regulator

The SBV controls the banking activities of all banks licensed to operate in Vietnam through the delegation of specific powers to internal departments of the SBV. The Banking Inspection and Supervisory Agency of the SBV is specifically designated to examine the operations and activities of credit institutions.[31]

All banks must send a vast number of periodic reports to the SBV, varying from those required on a daily basis to those required on an annual basis. This is regarded as contributing to an unwieldy and ultimately costly banking environment. In addition, banks must immediately report to the SBV irregular developments that are adverse to the business operations of the bank or major changes to the organisational structure of the bank.[32] Notwithstanding the volumes of reporting required, there is a clear lack of sophisticated information disclosure relating to the activities of banks, in particular from an accounting perspective.

A bank is required to obtain written approval from the SBV prior to making any changes to its corporate identity, including a change to its name, capital, location, scope of business, and management, listing on offshore stock exchanges (although this has not yet occurred), as well as significant changes to its shareholding structure.[33]

ii Management of banks

The laws and regulations concerning the management of commercial banks as well as the role and responsibility of the shareholders[34] are now detailed in the new LCI. Provisions of Decree No. 59/2009/ND-CP dated 16 July 2009 on organisation and operation of commercial banks ('Decree 59'), adopted shortly before the new LCI was passed, are also applicable to the extent they are not contrary to the LCI.

The management structure of an entirely state-owned bank, a joint venture bank or a bank with entirely foreign capital (as opposed to a bank which is a company limited by shares or a joint-stock commercial bank) corresponds to that of a limited liability company and is constituted by the members' council, the board of controllers and the general director.[35] In relation to a joint-stock commercial bank the board of management is responsible to the shareholders for the operation of the bank. Both the members council and the board of management should consist of between five and 11 members.[36]

30 Article 62 of Decree 22.

31 Decree 96.

32 Article 141 of the LCI.

33 Article 29 of the LCI.

34 Articles 66 and 70 of the LCI.

35 Article 32 of the LCI.

36 Article 62.1 of the LCI.

For joint-stock commercial banks, at least half of the members must be independent and members who are not executive officials of the credit institution.[37] In both types of structure, the board of controllers is constituted by at least three members, at least half of whom must be full-time.[38]

Subject to the decisions that are reserved at law or are in the bank's charter for decision by the owners (in limited liability structures) or shareholders, the members council or the board of management has the authority to make decisions in the name of the bank and to exercise the rights and obligations of the bank, in particular with respect to investment and asset acquisition decisions with a value of more than 20 per cent (for limited liability banks) and 10 per cent (for joint-stock commercial banks) of the charter capital of the bank.[39] The general director has authority for transactions of lesser amounts.

The shareholders of a joint-stock bank must by law approve investments and acquisitions and sales valued at more than 20 per cent of the bank's charter capital and contracts with a value of more than 20 per cent of the bank's charter capital between the bank and its management (members of the board of management, or of the board of controllers, or the general director), or between the bank and major shareholders (i.e., shareholders holding at least 5 per cent of the bank's charter capital), or their respective related parties and between the bank and its affiliates.[40] In a limited liability bank all transactions of the bank with the members of the members council or its top management, or both, must be approved by the members council.[41]

The board of management, the members council or the owner (in case of a one-member limited liability bank) may appoint one of its members (if applicable) or employ another person as the general director. The general director manages the daily business of the bank, supervised by the board of management or the members council and the board of controllers and is responsible to the board of management or the members council.

Each of the board of management or the members council, the board of controllers and the general director acts for a term of five years and may be reappointed for an unlimited number of terms. The election and appointment of the chairman and members of the board of management or the members council, the head and members of the board of controllers, and the general director of a bank must be pre-approved by the governor of the SBV, and their duties and powers must be specified in the charter of the bank.

Any individual or any institutional shareholder represented by an individual who is a member of the board of management or the members council, board of controllers or a general director may not, while he or she is in office, sell his or her shares. This provision in the new LCI varies from the previous rule under Decree 59 which required the retention of only 50 per cent of the total number of shares owned when elected or

37 Article 62.1 of the LCI.

38 Article 44.2 of the LCI.

39 Article 63.8 and 67.2 of the LCI.

40 Article 59.2(p) and (q) of the LCI.

41 Article 67.2(l) of the LCI.

appointed to the relevant managerial position during the term of service and for a period of one year thereafter.[42]

A foreign bank branch in Vietnam may be managed by only one general director who may not be a manager or executive of any other credit institution or economic institution in Vietnam.

Adopted on the background of a global financial crisis, which was blamed in large part on the management of commercial banks, the LCI introduced the prohibition (which is in line with the generally applicable Vietnamese Law on Enterprises) on the increase of remuneration, or salary of, and the payment of bonuses to the members of the board of management or the board of members, members of the control board, the general director, the deputy general directors, and the chief accountant of the credit institution suffering losses.[43] The prohibition does not seem to be strictly enforced.

iii Regulatory capital and liquidity

Vietnamese legislation does contain prudential requirements and separate debt provisioning guidelines.[44] However, the SBV does recognise that Basel II (not to mention Basel III) is far from being implemented in Vietnam and it aims for gradual implementation over the coming years.

Capital adequacy

In 2010, consistent with its stated intention to tighten prudential requirements, the SBV raised the minimum capital adequacy ratio ('CAR') of credit institutions (excluding foreign bank branches) to 9 per cent from the previously applicable 8 per cent. The ratio is calculated as the percentage of 'equity' over 'total assets in credit at risk'.

For the purposes of this capital adequacy test, 'equity' comprises: Tier I capital, including charter capital, the reserve fund for supplementing the charter capital, the professional development investment fund, the investment and development fund, retained profits, shares issuance premium received and added to the capital less the amounts used to repurchase shares (as the case may be); and Tier II capital, including 50 per cent of the additional value of fixed assets following their revaluation, 40 per cent of revalued financial assets, financial reserves, long-term unsecured subordinated convertible bonds and other deeply subordinated debt instruments. Tier II equity cannot exceed Tier I equity.[45]

42 Article 56-1 of the LCI and Article 36.4 of Decree 59.

43 Article 38.8 of the LCI.

44 Circular 13/2010/TT-NHNN dated 20 May 2010 ('Circular 13') replaced the Regulations on Prudential Ratios in Operations of Credit Institutions issued with Decision No. 457/2005/QD-NHNN of the Governor of the SBV dated 19 April 2005 (Decision 457), as amended by Decision No. 03/2007/QD-NHNN of the SBV dated 19 January 2007, Decision No. 34/2008/QD-NHNN dated 5 December 2008 and Decision 493/2005/NHNN on classification of debts ('Decision 493'). Circular 13 was amended by Circular 19/2010/TT-NHNN dated 27 September 2010.

45 Article 5.3 of Circular 13.

Items that must be deducted from the equity of a bank include: (1) in relation to Tier I capital only, good will, operating losses including accumulated losses, contributions to the capital of other credit institutions or subsidiaries, significant investments over 10 per cent of the total of all components of Tier I capital after deduction of all preceding items, and investments over 40 per cent of the total of all components of Tier I capital less all preceding deductions;[46] (2) the reduced value of fixed assets following their revaluation by the bank; and (3) the total amount of the reduced value of all types of financial assets following their revaluation.[47]

'Total assets in credit at risk' comprises the value of assets in credit of a bank which are adjusted at risk levels ranging from zero to 250 per cent[48] plus off-balance sheet undertakings which are adjusted at risk levels from zero to 100 per cent.[49]

In addition to the individual bank's capital adequacy ratio, the LCI now requires banks having subsidiaries to calculate a consolidated capital adequacy ratio for the group using a similar methodology.[50]

Large exposures and related party transactions

A commercial bank's total credit exposure (including guarantees)[51] to a single borrower is limited to 15 per cent of its equity.[52] The LCI subjects foreign bank branches to the same restrictions by imposing that the single borrower limit calculation be based on the branch's allocated onshore capital instead of the parent bank's equity (as was the case under the previous regime). Only those foreign banks committed to investing in

46 Article 5.2 of Circular 13.

47 Article 5.4 of Circular 13.

48 Article 5.5 of Circular 13. There are six categories of assets in credit depending upon the level of risk: (1) cash and gold or equivalent: zero per cent; (2) debt recoverable from other credit institutions or equivalent: 20 per cent; (3) investments in projects under finance companies and claims secured by immoveable property: 50 per cent; (4) paid-up charter capital in subsidiary companies and affiliates, claims on non-OECD governments and financial institutions: 100 per cent; (5) loans to non-securities trading subsidiaries and affiliates: 150 per cent; and (6) loans made for investment in securities and real estate: 250 per cent.

49 Article 5.6 of Circular 13; the risks co-efficient of the value of off-balance sheet undertakings are: zero per cent for an undertaking guaranteed by the government or the SBV, fully secured by cash or by savings accounts or deposits of valuable paper issued by the government or the SBV; 50 per cent for an undertaking secured by immoveable property; 100 per cent for interest rate and currency transactions and other off-balance sheet undertakings.

50 Article 6 of Circular 13.

51 'Credit exposure' includes loans, discounting, finance leasing, factoring or bank guarantees, investment in bonds issued by a client and other forms of extension of credit (Article 4.14 and 128 of LCI). Therefore, going forward bank guarantees are also included in the 15 per cent single borrower limit while previously the maximum aggregate exposure in loans and guarantees to a single client was 25 per cent of a credit institution's equity. This significant tightening was strongly debated prior to the adoption of the new LCI.

52 Article 128.1 of the LCI.

Vietnam in the long term while remaining in the branch form have made provision for such change to the single borrower limit calculation by allocating additional capital to the relevant branch in order to comply with the new prudential ratios.[53] Other foreign banks have chosen either to transfer to their offshore entities the loans exceeding the cap.

The aggregate amount of credit exposure to a group of related clients must not exceed 25 per cent of a commercial bank's or foreign bank branch's equity.[54]

The above limits do not apply where loans are extended under trust lending arrangements whereby the bank acts as an agent for on-lending of funds provided by other organisations or where the borrower is a credit institution.

In exceptional cases, the prime minister can authorise the above single borrower and related borrowers credit exposure caps to be raised to up to 400 per cent of the equity of the credit institution or foreign bank branch.[55]

The total amount of credit exposure by a credit institution to any single enterprise or all enterprises that such credit institution controls[56] must not exceed 10 or 20 per cent, respectively, of the credit institution's equity.[57]

Use of short-term funds

A commercial bank may only use 30 per cent of its short-term mobilised funds (i.e., that are repayable within one year) to finance medium and long-term loans.[58]

Liquidity ratio

The minimum liquidity ratio that a commercial bank must maintain in respect of each type of currency and gold is 15 per cent of defined liquid assets (including cash and cash equivalents) over liabilities due immediately. This ratio increases to 100 per cent of liquid assets in dong, US dollars, euros and British pounds being claimed within seven business days against liabilities payable within that time period and the aggregate amount of certain contingent liabilities payable within the subsequent seven business days. [59]

53 In late December 2010, the SBV approved capital increases for Huanan Commercial Bank Ltd Ho Chi Minh City ('HCMC') branch from US$15 million to US$65 million, Chinatrust Bank HCMC branch from US$15 million to US$50 million, and Mizuho Corporate Bank Hanoi and HCMC branches from US$15 million to US$133.5 million each.

54 Article 128.1 of the LCI.

55 Article 128.7 and 128.8 of the LCI.

56 These include subsidiaries or affiliated companies of the credit institution or an enterprise controlled by the credit institution (Article 127.1(e) of the LCI). Control is defined as 'an investment accounting for more than 50 per cent of the charter capital or voting shareholding capital of any one enterprise, or another investment sufficient to control decisions of the general meeting of shareholders or members' council' (Article 4.25 of the LCI).

57 Article 127.4 of the LCI.

58 Circular 15/2009/TT-NHNN dated 10 August 2009.

59 Article 12 of Circular 13.

Equity investments

Under the LCI, commercial banks must establish or acquire subsidiaries or associated companies to carry out underwriting of securities issues, securities brokerage, management and distribution of securities investment fund certificates, securities portfolio management and sale or purchase of shares, finance leasing and insurance.[60] They may not exercise these activities directly. However, with the exception of finance companies, the creation or purchase of such subsidiaries, or even the exercise of their control by the bank, seems to be quite restricted due to the cap on the maximum level of investment that a bank and its subsidiary and affiliated companies can make in an enterprise operating in such sectors as insurance, securities, management of security assets, foreign currency remittances by Vietnamese residing abroad, trading in foreign exchange or gold, factoring, issuance of credit cards, consumer credit, payment services or credit information or investment fund or investment project. This cap is set by the law at 11 per cent of the enterprise's or fund's charter capital or 11 per cent of the value of the investment project. The total investment made by a credit institution (including its subsidiaries and affiliated companies) must not exceed 40 per cent of its own charter capital and its reserve fund.[61]

The underwriting by commercial banks,[62] the most active participants in Vietnam's nascent corporate bond market, of convertible bonds is now clearly permitted by the SBV.[63]

Loss provisioning and debt classification

Decision 493 imposes loss provisioning requirements on commercial banks and a debt classification regime. This piece of legislation introduced for the first time the possibility for a credit institution to classify debt on a qualitative basis, based on its own, SBV approved, internal credit risk-rating systems ('ICRS'). In view of the lack of guidance regarding the establishment of ICRS, each credit institution is establishing its own system and there is a consequential lack of consistency in the classification of debts and in the establishment of prudential ratios. The SBV is preparing a draft circular to replace Decision 493 with a view to providing consistent guidelines on ICRS.

iv Recovery and resolution

As in other countries, failure of credit institutions represents a high systemic risk and is politically sensitive. The LCI provides that bankruptcy procedures can be declared against a credit institution only after putting it under SBV special control aimed at redressing its situation, and only when such special control has failed.[64]

60 Article 103.2 of the LCI.

61 Article 129.1 and 129.2 of the LCI.

62 But not by foreign bank branches.

63 Article 1.1(a) and 7.3 of Circular 28/2011/TT-NHNN dated 1 September 2011 of the SBV providing for the purchase of enterprise bonds by credit institutions, foreign bank's branches.

64 Articles 145 and 155 of the LCI.

The detailed bankruptcy procedures are provided in a special government Decree No. 05/2010/ND-CP dated 18 January 2010 Regulating Application of Law on Bankruptcy to Credit Institutions. At the end of the bankruptcy procedures the credit institution's license will be revoked by the SBV in accordance with the procedures set out in a recent SBV Circular No. 34/2011/TT-NHNN dated 28 October 2011 guiding the order and procedures for revoking licences and liquidating assets of credit institutions and foreign bank branches, representative offices of foreign credit institutions and other foreign institutions engaged in banking activities.

IV CONDUCT OF BUSINESS

In order to protect depositors, a commercial bank must maintain compulsory deposit insurance with Deposit Insurance of Vietnam, which is a state financial institution, in respect of Vietnamese dong deposits and transactions.[65]

The LCI prohibits banks from disclosing any details relating to a client unless it is requested by customers, by the general director of a deposit insurance organisation, or by a state body during an inspection or for the internal activities of the bank.[66] Banks can also disclose information when they participate in a merger or acquisition or with customer consent. However, the banks' capacity to do so may be restricted if the relevant information is classified as 'state secrets'. The scope of the application of state secrecy rules in banking and finance is not well defined.

Without the consent of depositors, a bank cannot carry out investigations into deposits or to freeze a deposit, deduct from or transfer deposits, except in the limited case of being requested to do so by a competent court or a judgment enforcement authority.[67]

A bank must not conceal or provide services in respect of money that has an illegal origin and must immediately notify the competent state body (the Anti-Money Laundering Agency under the SBV) as soon as they are aware of such circumstances.[68] Under new detailed legislation effective from 1 January 2010,[69] banks must put in place internal anti-money laundering rules on customer information, reporting suspicious transactions and coordination with law enforcement agencies. The new regulations also contain internal training and annual audit requirements. A new department under the Banking Inspectorate at the SBV has been established to take charge of all matters

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65 Decree 89/1999/ND-CP dated 1 September 1999 on deposit insurance ('Decree 89') amended by Decree 109/2005/ND-CP dated 24 August 2005 ('Decree 109'). The government is currently planning to upgrade the current deposit insurance regulations into a law replacing Decrees 89 and 109.

66 Article 5 of Decree 70/2000/ND-CP dated 21 November 2000.

67 Civil Proceeding Code and Law on judgment enforcement.

68 Article 11 of the LCI.

69 SBV guidance for the implementation of money-laundering measures (Prevention and Combat). Circular No. 22-2009-TT-NH dated 17 November 2009.

regarding money laundering.[70] A bank violating the money-laundering regulations may be subject to administrative sanctions ranging from a warning to a monetary fine of up to 30 million dong.[71] Individuals committing money-laundering offences may be subject to criminal sanctions, including prison terms of between one and 15 years.[72]

Depending on the nature and seriousness of other banking violations, a bank may be subject to administrative penalties which range from a warning or a fine up to 70 million dong, or suspension of operations, with or without a specified time limit (e.g., withdrawal of the operation licence).[73] There is no publicly available information relating to the imposition of any such sanctions to date.

V FUNDING

Joint-stock banks in Vietnam frequently raise funds by share or convertible bond issuances.[74] Under the LCI, Vietnamese banks may also finance their operations through 'mobilised capital', which may consist of: (1) cash deposits; (2) borrowed capital from domestic and foreign credit institutions (sometimes by way of repurchase agreements); (3) funds raised via the issuance of valuable paper, such as time deposit certificates or bonds; and (4) borrowed capital from the SBV via securities lending or through open market operations.

As the central bank, the SBV may refinance commercial banks by re-lending in accordance with credit contracts, discounting or rediscounting valuable paper or by granting loans guaranteed by pledges of valuable paper.[75] The SBV's refinancing policy is one of the ways in which it supplements short-term capital and provides payment means for commercial banks.

In extraordinary cases for the purpose of stabilising the monetary market, the SBV may grant special loans to commercial banks that may be insolvent causing a threat to the stability of the banking system.[76] During the financial crisis, the SBV has not officially granted any special loans to a bank on this 'emergency basis', although it did in January 2010 inject 15,000 billion dong in open-market transactions to improve the liquidity of commercial banks.

70 Decision 1654/QD-NHNN dated 14 July 2009 on functions, duties, powers and organisational structure of the anti-money laundering department.

71 Article 24 of Decree 74/2005/ND-CP dated 7 June 2005 on anti-money laundering.

72 Article 251 of the Criminal Code of Vietnam.

73 Decree 202/2004/ND-CP on administrative offences in the field of money and banking.

74 By way of example, most recently Saigon Thuong Tin Bank (Sacombank) increased its charter capital from 5,115 billion to 6,700 billion dong and Export-Import Bank (Eximbank) increased its charter capital from 7,219 billion to 8,800 billion dong through share issuances.

75 Article 11 of the SBV Law.

76 Article 24.2 of the SBV Law and Article 151 of the LCI. The SBV refinanced a private bank, Asia Commercial Bank ('ACB') when there was a run on the bank in 2003 resulting from rumours that the general director had absconded.

VI CONTROL OF BANKS AND TRANSFERS OF BANKING BUSINESS

i Control regime

Other than in the case of state-owned banks, entirely foreign-held bank subsidiaries and joint venture banks, Vietnamese law prohibits any shareholder that is an organisation from holding, directly or via proxy, more than 15 per cent, and any individual from holding, directly or via proxy, more than 5 per cent, of a bank's charter capital.[77] The combined shareholding of shareholders and their related parties is also limited to 20 per cent.[78] In special cases in the national interest, the prime minister may, at the SBV's request, permit shareholdings in commercial banks that exceed the statutory limitations.[79]

The governor of the SBV must provide prior written approval of: (1) the purchase and sale transactions of 'significant shareholdings' (defined as 'a level of shareholding of 5 per cent or more of the voting share capital of a bank'); and (2) purchase and sale transactions of an amount of shares that results in any shareholder holding more than a significant shareholding or any shareholder no longer holding a significant shareholding.

The SBV may not approve such a transaction if it considers that it may lead to 'instability in banking operation'.[80] Since this term is not defined and is potentially broad, the SBV has, in practice, a fairly wide discretion in approving transactions. Note also the restrictions on foreign ownership in Vietnamese banks set out in Section II, *supra*.

The SBV last year issued Circular 04[81] governing the merger, consolidation and acquisition of credit institutions, which replaced prior legislation that was narrower in scope.

Circular 04 permits the merger of commercial banks into an existing entity, and the consolidation of commercial banks into a new entity, subject to prior written approval of the Governor of the SBV.[82] The SBV will evaluate the file and the opinions of the local SBV branch and the people's committee of the province or city where the relevant banks have their head office. Factors taken into consideration when considering whether to approve or refuse the merger, consolidation or acquisition plan will be the current organisational and operational status of the banks and the impact of the merger or consolidation (as the case may be) on 'social stability' within the locality.[83] Any merger or consolidation is also subject to competition approvals and the satisfaction of minimum capital and prudential requirements.

77 Article 55.1 and 2 of the LCI.

78 Article 55.3 of the LCI.

79 Article 34.4 of Decree 59.

80 Article 36 of Circular 06/2010/TT-NHNN dated 26 February 2010 guiding organisation, management and executive operation, charter capital, assignment of shares, and amendment of and addition to licence and charter of commercial banks ('Circular 06').

81 Circular No. 04/2010/TT-NHNN dated 11 February 2010 on mergers, consolidations and acquisitions of credit institutions ('Circular 04').

82 Article 34 of the Law on Credit Institutions.

83 Articles 10.4, 14.4 and 18.4 of Circular 04.

Circular 04 is still a rudimentary framework for mergers and acquisitions in banking. It does not provide for a possibility to use special purpose vehicles to acquire target banks. The circular is silent on the possibility for the target bank to provide guarantees covering the purchaser's repayment of the acquisition finance. It has also left out a significant part of bank mergers and acquisitions outside its scope by not providing any guidance as to how bank mergers and acquisitions implemented outside Vietnam could affect foreign bank branches, subsidiaries or affiliates in Vietnam.

ii Transfers of banking business

Other than through the merger or consolidation activity previously described, a bank cannot transfer its clients' bank deposits to another entity without receiving specific approval from the SBV.

It may however assign its loan arrangements to a foreign or domestic purchaser (subject, in the case of an assignment to a foreign entity, to compliance with exchange control procedures). The terms of any such assignment are freely negotiable with the sole exception that certain 'group 1 standard debts', being very well-performing loans, may only be sold at the value of the debt.[84]

The debtor and any guarantors must unconditionally accept the assignment of the creditor's rights from the seller to the buyer of the debt.[85] The security for any transferred debt will also follow the debt to the benefit of the assignee, without the need for borrower consent (unless the security contains specific transfer restrictions), although the re-registration of the security may sometimes be problematic from a practical perspective.

Decree 59 also contains a special control and bankruptcy regime applicable to all forms of commercial banks, including state-owned banks, which allows the SBV to appoint a special committee to oversee a bank experiencing financial difficulties. The appointment of such a special committee is not automatically disclosed to the public. The SBV also issued further specific guidelines on bankruptcy procedures applicable to credit institutions, which took effect on 15 March 2010.[86] This provides that a credit institution that is incapable of repaying its due debts upon the request of its creditors only be subject to insolvency procedures after the SBV has determined to terminate the special control regime in writing. The same approach was adopted by the authors of the new LCI.

VII THE YEAR IN REVIEW

i Slower growth and persistent inflation

Vietnam has managed to maintain a relatively high 5.9 per cent growth rate of the country's GDP in 2011. The impressive growth rate by global standards was still the

84 Article 7.1 of Regulation on purchase and sale of debts by credit institutions issued by Decision 59/2006/QD-NHNN dated 21 December 2006 ('Decision 59').

85 Article 16.2.a of Regulation on purchase and sale of debts by credit institutions issued by Decision 59.

86 Decree No. 05/2010/ND-CP dated 18 January 2010.

lowest achieved since 2000 (excluding 2009's financial crisis-related growth of 5.3 per cent) and lower than the country's 2010 performance. The macroeconomic imbalances remained the main challenge for the authorities. Inflation remained one of the highest in the world peaking at 23 per cent in August 2011, although it decreased to 18.1 per cent in December 2011 and further to 17.3 per cent in January 2012.

If at the beginning of 2011, the new anti-inflationary monetary policy was still aiming at stabilising prices without jeopardising growth, the government progressively shifted its priority to fighting inflation even at the expense of the economic growth during the second half of the year.

Growing concerns over the state of the Vietnamese economy, exacerbated by the failure of Vinashin, the Vietnamese state-owned shipbuilding company, to repay foreign debt obligations, and the deterioration of the situation of many large state-owned companies such as the Electricity of Vietnam (EVN), which was ordered to withdraw from and transfer its telecommunications business to Viettel, another large state-owned telecommunications company.

ii Reduced credit growth

The government has embarked on a process of tightening economic policy in a difficult global environment. The SBV aggressively pushed up its policy rates in an attempt to slow the expansion of credit. It also imposed strict targets for domestic credit growth this year from 20 per cent in 2011 to 17 per cent in 2012.

In March 2011 the central bank declared it would double reserve requirements for banks that fail to reduce the ratio of lending to non-productive activities (as a percentage of total lending), to below 16 per cent by the end of 2011. The overall annual credit growth was only 10.9 per cent in 2011 against 29.81 per cent in 2010. This represents a marked reduction in comparison to the 45.6 per cent growth experienced during 2009 and is largely under the target maximum credit growth rate set at 20 per cent for 2011. The deceleration was also explained by very high interest rates discouraging the potential borrowers.

iii Tightened FX control regime

The foreign exchange market remained highly volatile for the most of 2011 but started to stabilise in the last quarter. In February 2011 the SBV had to devalue the Vietnamese dong against the dollar for the fourth time since November 2009.[87] This was followed by restrictions on individual's capacity to purchase foreign currency.[88] The government then

87 An effective devaluation of 9.3 per cent in February 2011 following official depreciations of 3.36 per cent in February 2010, 2.1 per cent in mid-August 2010 and 5.44 per cent in November 2009.

88 Circular 20/2011/TT-NHNN dated 29 August 2011 of the SBV providing for the purchase, sale of foreign currencies in cash between individuals and authorised credit institutions.

significantly increased administrative penalties for breaches of foreign exchange control regulations.[89]

In response to the instability of gold markets and the weakening Vietnamese dong, the SBV first adopted Circular 11/2011/TT-NHNN dated 29 April 2011 on termination of mobilisation of deposits and provision of loans in gold by credit institutions (Circular 11) effectively banning deposits and loans made in gold. A few months later, the SBV adopted Circular 32/2011/TT-NHNN dated 6 October 2011 amending and supplementing Circular 11. Banks were allowed to convert gold deposits into currency by selling it to the public. These measures follow those adopted in 2010 to control the gold market (closing of gold trading floors nationwide as of 30 March 2010 and of offshore gold trading accounts by 30 June 2010).[90] In October 2010, the SBV also limited the retention and use of gold deposits by commercial banks.[91]

The removal of the interest rate caps and the issuance of Circular 13 (replacing Decision 457) on prudential ratios in 2010 gave credit institutions greater flexibility in setting interest rates, but at the same time rendered interest rates unbearably high to businesses. Although the SBV frequently makes declarations to the commercial banking sector urging restraint on the application of high interest rates, the hope is that the provisions of Circular 13 will allow Vietnamese banks to price risk more effectively and make credit available to smaller companies whose risk profiles would not have supported a lower prescribed rate. The SBV must now concentrate its efforts on using market mechanisms to reduce the high lending interest rates.

VIII OUTLOOK AND CONCLUSIONS

At a macro level, it is expected that the SBV will continue using the intervention powers confirmed in the new SBV Law to continue to tighten monetary policy and intervene in foreign currency matters. The SBV plans to reduce inflation down to 8 to 8.5 per cent in 2012 and thus reduce the fund raising rate will fall to 10 per cent annually. Achieving this target will be quite challenging in the context of imminent electricity price hikes, as well as an oil import tax increase (up from zero to 4 per cent in December 2011).

The SBV will continue its tight credit policy by setting the maximum credit growth rate at 15 to 17 per cent for 2012. The SBV has, following market pressure, for the first time adopted a more fine-tuned approach in allocating credit growth caps to individual credit institutions based on their rating by the SBV.

89 Decree No. 95/2011/ND-CP dated 20 October 2011 amending Decree No. 2002/2004/ND-CP dated 10 December 2004 on administrative sanctions applicable to breaches of monetary and banking regulations.

90 SBV Circular No. 10/2010/TT-NHNN dated 26 March 2010 amending Articles 2.2 and 2.3 of Circular No. 01/2010/TT-NHNN dated 6 January 2010 which repealed Decision No. 03/2006/QD-NHNN dated 18 January 2006 on gold trading on offshore accounts and Decision No. 11/2007/QD-NHNN dated 15 March 2007.

91 SBV Circular No. 22/2010/TT-NHNN dated 29 October 2010.

At the same time, in an effort to support agriculture exports, which performed well in 2011, the SBV lowered the reserve requirements to 3 per cent for VND and 8 per cent for USD for less than one year for five credit institutions (Central People's Credit Fund, Vietnam Bank for Agriculture and Rural Development, Mekong Joint-Stock Commercial Bank, Mekong Housing Joint Stock Commercial Bank (MHB), Lien Viet Post Joint Stock Commercial Bank), which have a high proportion of agricultural and rural loans on 2 February 2012. This is seen as part of the government's effort to support the agricultural sector and rural areas, as well strategic economic segments.

The NPLs increased sharply from 2010 to 2011 due to a combination of tight monetary conditions and the sluggish domestic and global economy. According to the SBV, NPLs accounted for 3.4 per cent of total outstanding loans from 2.5 per cent in 2010 and is under the safe level of 5 per cent. However, actual NPLs could be higher than the official statistics.

The SBV will continue its efforts to promote non-cash payments (bank cards, cheques, bank transfers) in Vietnam from 2011 to 2015.

In terms of policy, the hope is that Vietnam will continue to move towards the strengthening and reorganisation of credit institutions in line with international standards and increased transparency of banking operations. There is a clear need for the continuing development and refinement of regulations relating to more sophisticated offerings, such as derivatives (including with respect to confirming the enforceability of set-off).

The SBV will also likely to strengthen its foreign exchange control policy. Gold trading will also likely be further regulated through the encouragement of gold deposits in banks, which may even be insured by a deposit insurance scheme.

The requirement for joint stock banks to increase their minimum charter capital to 3,000 billion Vietnamese dong by 31 December 2011 (an increase from 1,000 billion Vietnamese dong in 2009),[92] together with serious liquidity shortages at a number of smaller banks will lead to further consolidation of the private bank sector.

The SBV indicated that there could be five to eight banks that will merge in the first quarter in 2012 in addition to the three already merged[93] at the end of 2011. The hope is that the merger would create a stronger bank that would be able to overcome difficulties that otherwise would be hard to do if the three banks operated as smaller individual banks. However, there still seems to be very few signs of any progress in terms of transparency and bad debt settlement following the merger.

From a regulatory perspective, the emphasis will continue to be on the issuance of implementing guidelines for the two new banking laws (the SBV Law and the LCI) to create a solid and consistent legal framework for banking activities, although concerns remain over practical monitoring and enforcement at the initial stages.

A new circular (initially expected to be issued in early 2011), replacing the current Decision 493 on loan classification and provisioning, is expected to bring Vietnam's

92 Decree 10/2011/ND-CP dated 26 January 2011 amending Decree 141/2006 dated 22 November 2006 on banks' charter capital.

93 First Bank, Tin Nghia Bank, and Saigon Commercial Bank.

practice closer to internationally recognised standards and should provide a more accurate reflection of the quality of the bank portfolios. With tighter loan classification, resulting in higher reported NPL ratio and provisioning, credit institutions will also face greater challenges in meeting the CAR, among other requirements. However, while the revised regulations might adversely affect the profitability of the banking sector in the short term, they are expected to contribute to the safety, stability and reliability of the financial sector in the medium term.

Updated trust loan regulations are also currently being discussed by the SBV, which, it is hoped will add clarity to this funding structure using intermediary banks.

Appendix 1

ABOUT THE AUTHORS

SAMANTHA CAMPBELL

Gide Loyrette Nouel AARPI

Samantha Campbell is an English-qualified solicitor. She is the resident partner heading Gide Loyrette Nouel's ('GLN') practice in Vietnam and divides her time between GLN's offices in Hanoi and Ho Chi Minh City. Before joining GLN in Vietnam in 2009, Samantha was at a top-tier US law firm in London for nine years, prior to which she practised at a leading English law firm.

Ms Campbell's experience includes advising on numerous international finance transactions, including general bank lending work (secured and unsecured), capital markets issuances, asset-based financings, acquisition financings and debt restructurings. Her practice has an emphasis on highly structured project development and financing matters including the negotiation of project documents with host governments, state-owned companies and other counterparties. Her work to date has involved transactions around the world in both developed and emerging economies, including in Asia, the CIS, sub-Saharan Africa, Europe and South America.

In Vietnam, Ms Campbell regularly advises international banking clients on the regulatory framework applicable to their activities, including in developing sectors such as consumer financing and derivatives. She also represents international lenders in connection with financing the activities of Vietnamese institutions.

Ms Campbell has been named as a leading individual for banking and finance by *Chambers Asia 2012* for her work in Vietnam.

PHAM BACH DUONG

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Pham Bach Duong specialises in banking and finance law and compliance in Vietnam and South East Asia.

He has a strong track record in loans and trade finance involving international companies operating in Vietnam, as well as Vietnamese state-owned enterprises and private borrowers. Duong also has in depth experience of Vietnamese securities issuances, custody services and derivative products, as well as the corporate aspects of transactions involving credit institutions and governance and compliance issues.

He is a graduate of the Sorbonne University – Paris I and the Moscow State Institute of International Relations, and speaks fluent Vietnamese, English, French and Russian. Prior to joining GLN in 2010, Duong was head of legal for the Standard Chartered Bank in Vietnam and the Mekong Region for almost six years.

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Nguyen Thi Tinh Tam joined GLN in 2008 prior to which she practised at Vilaf Hong Duc and PBC Partners for six years.

Ms Nguyen's areas of expertise include advising on all aspects of foreign investment in Vietnam, including in relation to corporate, tax and labour issues. She also regularly advises on the banking and the capital markets regulatory environment. Her clients include major international banks and financing institutions, both inside Vietnam and abroad, with Vietnamese activities or interests. Specifically, Ms Nguyen has recently advised a consumer-financing subsidiary of a major European bank in relation to the scope of its activities in Vietnam and a number of banks on their activities in the Vietnamese securities sector.

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