SCMlegal

STEPS TO INVEST IN A MYANMAR BANK

Find a bank to partner with

- There are 25 privately owned Myanmar banks
- Many have invested heavily in upgrading their systems and developing their cross-border banking relationships

Carry out due diligence on the partner bank

- Is the bank complying with updated prudential requirements?
- Has the bank implemented adequate anti-money laundering processes?
- Has the bank taken steps to reduce it's portfolio of non-performing loans?

Negotiate terms of the investment

- Come up with an investment structure to execute the required investment
- Ensure that minority protections are in place
- Ensure that economic returns and influence over strategy and operations is maximised

Submissions to the Central Bank of Myanmar

- Submit the the necessary supporting documents to the CBM
- Submit an application of an approval of a substantial interest (if the investment is more than 10%)
- Submit the notice for the appointment of directors
- Submit an application for approval to amend the bank’s constitution

THE DOOR OPENS TO INVESTING IN A MYANMAR BANK

The Central Bank of Myanmar (**CBM**) issued notice CBM/Regulation/1(1/2019) on 29 January 2019 (**Notice**)allowing Myanmar private banks to accept up to 35% equity investment from foreign banks and financial institutions. While not a change in law, it marks a change in the policy of the CBM which until now had not permitted foreign investment in locally owned Myanmar banks.

This is good news for the local banks, many of whom need injections of capital, technology and knowhow to expand, and for foreign financial institutions too, who may now gain exposure to Myanmar's retail banking sector and strong corporate banking portfolios. It builds on other recent well designed reforms which will both strengthen and develop Myanmar's finance sector, such as the imposition of more stringent financial standards, licencing mobile financial service providers, expanding the services that foreign licenced banks are able to supply, development of a domestic market for Government issued bonds, permitting local banks to undertake unsecured lending, and allowing the use of Yen and Yuan/RMB for cross-border transactions.

This note explores some of the legal and commercial considerations in investing in a Myanmar bank, based on our experience in the sector and the intimate knowledge that comes with having drafted the applicable law.

1 INVESTMENT PROCESS – WHEN APPROVAL IS NEEDED

1.1 Who can invest

To take advantage of this opportunity the investor must be a foreign bank or financial institution. This includes foreign banks which already have a licenced branch operating in Myanmar.

The Notice does highlights the section of the Financial Institution Law 20/2016 (**FIL**) which restricts cross ownership of more than 5% between banks. Foreign banks, including those with branches in Myanmar, are exempted from this limit under another provision of the FIL. The purpose of including the reference to the cross-ownership restriction in the Notice is unclear, however in informal guidance to us the CBM stated that the intention is to limit the foreign investor from making an investment which exceeds 5% of the investor's capital.

1.2 Which Myanmar banks

There currently are 25 Myanmar banks with a banking licence. These are all eligible to partner with a foreign bank or financial institution.

Myanmar Citizens Bank Ltd	Asia Yangon Bank Ltd	Ayeyarwady Bank Ltd
First Private Bank Ltd	Tun Foundation Bank Ltd	United Amara Bank Ltd
Co-operative Bank Ltd	Kanbawza Bank Ltd	Myanma Apex Bank Ltd
Yadanabon Bank Ltd	Small & Medium Industrial Development Bank Ltd	Naypyitaw Sibin Bank Limited
Myawaddy Bank Ltd	Global Treasure Bank Ltd	Myanmar Microfinance Bank Limited

Yangon City Bank Ltd	Rural Development Bank Ltd	Construction and Housing Development Bank Limited
Yoma Bank Ltd	Innwa Bank Ltd	Shwe Rural and Urban Development Bank Limited
Myanmar Oriental Bank Ltd	Asia Green Development Bank Ltd	Ayeyarwaddy Farmers Development Bank Limited
Glory Farmer Development Bank Limited		

1.3 Is approval required for all investments

No, the FIL has no restriction on foreign investor investing in a Myanmar bank and the Notice only includes a requirement that a submission is made to the CBM.

Under the FIL, CBM approval is required where a "substantial interest" (10%) is being acquired in a Myanmar bank.

Approval must be granted before completion of the acquisition.

While there is no express provision under the FIL or Notice for the CBM to approve applications for investment under 10%, past CBM policy has been to require its approval. We anticipate that they may continue to seek to apply this.

1.3.1 The substantial interest test

If after the acquisition the investor will either: own more than 10% of the share capital in a Myanmar bank; control more than 10% of the voting rights; or control the management of the bank, then the investor will be considered as holding a substantial interest in the bank.

Before obtaining such substantial interest, an application must be made to the CBM to approve the investment. The policy is to ensure that the investor is "fit and proper". Accordingly, the CBM will assess the investment by carrying out background checks on the investor, and it may not approve the investment if it determines that:

(a) the investor, if an individual is not a fit or proper person;

(b) the investor, if a body corporate, has one or more directors or a CEO who is not a fit or proper person; or

(c) facts are known to the CBM to indicate that the person making the acquisition would exercise significant influence on the bank that would threaten the sound and prudent management of the bank.

The fit and proper person test is a review of the probity, integrity, diligence, competence, banking and business experience of the investor.

2 ACCESS TO NON-CORE BUSINESSES

2.1 Insurance or securities brokerage business

Banks in Myanmar are allowed, through a subsidiary, to operate insurance and security brokerage businesses. A foreign investor can indirectly gain exposure to an insurance business when investing in a bank. Indeed, several Myanmar banks have already established licenced insurance businesses.

Pursuant to announcement 1/2019 by the Ministry of Planning and Finance issued on 2 January 2019 it is already possible for foreign insurance companies to acquire a 35% stake directly in life and non-life insurers in Myanmar.

2.2 Investment banking

There are a number of restrictions under the FIL which curtail the ability of a bank to operate an investment banking business. Banks are only allowed to hold shares in a public company and it may not hold shares in a company to an aggregate value exceeding 10% of the unimpaired capital funds of the bank.

Banks may also not engage in a wholesale or retail trading businesses, and there are also restrictions on a bank's ability to buy and hold immoveable property (aside from standard security enforcement processes).

2.3 Mobile money business

With the approval of the CBM, banks may operate a mobile money service. This is either on a stand-alone basis or they may enter into an agreement with a service provider to provide mobile money services on its behalf.

3 PRUDENTIAL AND OTHER REGULATORY CONSIDERATIONS

Many regulatory provisions need to be understood and evaluated when conducting due diligence and planning future business operations.

3.1 Prudential standards

The CBM in July 2017 published a number of new prudential standards affecting Myanmar owned banks. These regulations in many cases were replacing prudential requirements which were over 30 years old. The prudential requirements required banks to quickly implement higher capital adequacy ratios, stricter treatment of non-performing loans, restrictions on overdraft lending and higher risk weightings on certain types of assets and loans.

Myanmar banks have found it challenging to adopt the new prudential standards, with the CBM giving banks leeway on the time by which full compliance with these new prudential requirements was required. Time is running out however and many banks face challenges to comply.

Foreign investors looking at investing in Myanmar banks should carry out detailed due diligence assessing the position of the banks and determine what is required to satisfy prudential standards.

Key prudential regulations:

Capital Adequacy Regulation	Asset Classification and Provisioning Regulation
Liquidity Ratio Requirement Regulation	Large Exposures Regulation

3.2 **Anti-money laundering**

Banks and financial institutions in Myanmar are subject to the Anti-Money Laundering Law 2014 (**AMLL**), putting in place a comprehensive anti-money laundering regime which needs to be adhered to by banks in Myanmar.

The AMLL requires that banks carry out detailed customer due diligence, have risk based anti-money laundering compliance mechanism, employ a dedicated compliance function and submit reports to the Financial Intelligence Unit. Compliance by banks and financial institutions is monitored by the Central Bank which has published the Directive for the CDD Measures, Directive No. (21 /2015) setting out the customer due diligence requirements.

When carrying out due diligence on banks it needs to be considered whether required procedures and processes are in place and the requirements of the AMLL are being complied with.

3.3 **Large exposures**

Banks are generally not permitted to take on a financial exposure with respect to a single or group counterparty which constitutes an aggregate liability of more than 20% of the core capital of the bank.

4 **NEGOTIATING THE VENTURE**

When negotiating with the chosen Myanmar bank, the foreign investor should ensure that it is happy with the level of control it gets and is comfortable with the protections it is afforded as a minority shareholder. The new Myanmar Companies Law, drafted by members of the SCM Legal team, provides a very high level of minority investor protection and also flexibility in structuring to allow for enhanced ownership and influence.

4.1 **Board of directors**

The foreign investor will be able to participate in the operational decision making of the bank by appointing directors. A bank may not have less than 5 directors. The directors must all satisfy the fit and proper person test (so this will need to be navigated by a new investor's nominee directors alongside the fit and proper person test that goes with becoming a substantial shareholder). The CBM will take a number of factors into consideration when determining the suitability of a director, including reviewing the proposed director's qualifications and past conduct.

30 days prior notice needs to be given to the CBM before a new director is appointed.

A bank must also provide 30 days prior notice to the CBM before appointing a new CEO.

4.2 **Minority protections**

As foreign investors will be allowed to only hold a 35% equity stake in Myanmar banks, understanding the protections available to safeguard the investment is an important consideration when making an investment. Investors may protect their investments in several ways.

4.2.1 **Myanmar Companies Law**

The MCL became effective on 1 August 2018 and includes a number of minority shareholder protections.

Shareholders' approval

The day to day operations of a bank are controlled by its directors, however a number of the important decisions which affect a company are reserved for the shareholders. Of these decisions most can be decided on a simple majority, however a few can only be passed by a special resolution which requires 75% approval. A foreign investor holding 35% of the voting shares in a bank will effectively be able to veto these decisions. These decisions relate to changing the share structure, rights of shareholders and constitutional documents of the bank. Other "super majority" matters could potentially be included in a bank's constitution too.

Oppressive conduct

If the majority shareholder acts in a manner which is considered oppressive to, unfairly prejudicial to, or unfairly discriminatory against the minority shareholder, the minority shareholder can bring a claim for oppressive conduct.

If courts find that oppressive conduct has occurred, they have a wide range of powers to halt the conduct, require that an action to be undone or award damages.

Derivative action

Leave to the court can be sought to bring an action on behalf of the bank. This may be used, for example, where a director may have breached their duties to the bank, but the board is unwilling to have the bank commence proceedings against the director.

The courts again have a wide range of remedies available to it, similar to those in the case of oppressive actions.

4.2.2 **Myanmar Investment Laws**

The Myanmar Investment Law 40/2016 (**MIL**) and the more detailed Myanmar Investment Rules affords a foreign investor in Myanmar a number of other important protections when investing in Myanmar. SCM Legal is pleased to have advised the Government on the drafting of the MIR and the implementation of the Law.

Discrimination

The MIL generally requires equal treatment of foreign and Myanmar investors, providing foreign investors with greater clarity on what they can do and more comfort that they will invest on a level regulatory playing field.

Fair and equitable treatment of investors is a feature of the MIL, giving investors the right to obtain information on any decisions made or measures taken by the authorities which affect them.

If investors have any regulatory grievances, they can now submit their grievances to the Myanmar Investment Commission which has procedures in place to assist investors if their rights are not respected. These will be further enhanced in coming months (we are currently advising the MIC on this project).

Capital remittances

The MIL guarantees the right of an investor to remit dividends offshore. This right also extends to management fees which a Myanmar bank may pay to a foreign shareholder which provides management or back office support offshore.

Expropriation

Investments in Myanmar are protected against expropriation, unless it is in the public interest and carried out in a non-discriminatory manner, in which case the investor is entitled to fair and adequate compensation.

4.2.3 **Contractual protections**

When agreeing the terms governing the relationship between the bank's shareholders, consideration should be given on whether to include any further minority protections. Topics which need to be addressed include:

(a) board control and whether board representation matches share ownership

(b) procedures controlling directors' meetings and voting

(c) future funding obligations

(d) entry of new shareholders

(e) dilution of shareholders' interests

(f) matters which need to be agreed by both shareholders

(g) exit mechanisms

(h) dividend policy

(i) dispute resolution process

(j) competition restrictions, to the extent allowed by law

5 STRUCTURING THE INVESTMENT

5.1 Additional investment

Foreign banks are currently limited to making up to a 35% equity investment in a Myanmar bank. If the bank requires additional capital, and the investor wants further exposure, then it may be possible to adopt hybrid and other more refined capital structures to meet those requirements. Including provisions to ratchet up ownership in line with further liberalisation of policy in this area could also be considered.

Stefan Chapman

WHO WE ARE

SCM Legal is an independent Myanmar law firm, owned and operated by the team who prepared Myanmar's new Companies Law and Investment Rules. Between them, the SCM Legal partners have over 50 years' experience in practicing law in Myanmar.

We have been involved in many 'first in kind' transactions in Myanmar giving us a thorough understanding of the regulatory landscape. Members of our team have been the lead legal advisors on the two key businesses law reform processes being implemented in Myanmar - the new Myanmar Companies Law and the Myanmar Investment Rules. Our team wants to help you and Myanmar grow and prosper.

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