14 April 2022

MYANMAR'S NEW FOREIGN CURRENCY RESTRICTIONS

Without warning on 3 April 2022 the Central Bank of Myanmar (**CBM**) issued notification 12/2022 and directive 4/2022 to impose foreign currency controls which will have a profound impact on businesses operating in Myanmar. This was followed up with directive 5/2022 and directive 6/2022 on 5 April 2022, and further announcements are expected as these major policy changes are worked through. The key implications of this volley of regulatory changes is below and summary of them is provided in the Annexure.

The aim of notification 12/2022 is to eliminate the domestic holding and use of foreign currency in domestic transactions. In addition, all foreign currency offshore remittances will be more closely scrutinised by the CBM, which will in effect further restrict the use of foreign currency. It achieves this through:

- requiring that any foreign currency which is received in Myanmar is immediately converted into Myanmar Kyat (**MMK**) at a rate fixed by the CBM (initially MMK1850 : USD1 – versus a market rate of around 2050:1 at the time of the announcement). The notification also required all existing foreign currency holdings in Myanmar bank accounts to be converted at the fixed rate, however not all banks have begun implementing this yet and there is some hope that revisions will be made to this element of the policy; and
- all offshore remittances will now require the approval of the Foreign Exchange Supervisory Committee (**FESC**), which is a new body established to supervise foreign exchange in Myanmar.

The changes are significant and will greatly affect all foreign and many Myanmar businesses, as well as having a large impact on the financial sector, making an already challenging operating environment more difficult.

1 BACKGROUND

The Myanmar financial sector has been through turmoil in the past 12 months, with banks affected by a severe liquidity crisis resulting in ongoing withdrawal limits, apparent shortages of foreign currency reserves and a major devaluation of the MMK which has been difficult to control.

The CBM has been trying to counter this by ditching the market-based exchange rate mechanism, which has led to the creation of an unofficial exchange rate generally used for currency exchanges outside of the Myanmar banking system. The CBM has also taken steps to try to bolster foreign currency reserves, when in October 2021 it forced exporters to exchange any foreign currency earnings into MMK within 30 days of their receipt.

This can be seen in the broader context of authorities in Myanmar trying to limit imports by banning the import of certain products via border trade and increasing the number of imported goods for which import licences are required. Reducing the depletion of foreign currency reserves is one of the likely goals of these import restrictions (while disrupting trade in the process).

In March 2022, in another attempt to reduce the pressure on the MMK, the CBM tried to limit the domestic demand for foreign currency by instructing banks to ensure that all domestic transactions were made in MMK.

The latest notification 12/2022 takes this policy one step further by requiring all domestic foreign currency holdings to be converted into MMK.

The underlying motives for taking these steps are likely:

- to relieve pressures which are devaluing the MMK;
- increase Myanmar's foreign currency reserves; and
- prevent the dollarisation of the economy.

2 EFFECT ON BUSINESSES

In theory, the effect of this new policy on businesses could be manageable. In the best-case scenario, the MMK1,850 peg to the USD will be maintained and businesses are able to easily buy USD at that rate from the banks in order to make all their required foreign currency payments, including paying for imports and offshore services, repaying offshore loans and distributing dividends. It could be beneficial if this meant that businesses are able to buy USD at the official CBM reference rate, rather than having to use the unofficial market exchange rates to buy their USD in an environment of low foreign currency liquidity.

There is however concern of the impacts of this policy within the wider business community because of the uncertainty it creates. This mainly relates to the potential of increased bureaucracy (and unpredictability) in carrying out any foreign currency transactions potentially instituting new capital controls and the uncertainty of how the new policy will be implemented. It is also the case that many routine domestic contracts and payments are denominated in USD, so a major adjustment will be required.

Based on the information made available by the CBM so far, and subject to exemptions yet to be announced, effects on businesses include:

- all domestic payments will need to be carried out in MMK, even if agreements stipulate settlement in foreign currency. This includes payments under service contracts, supplier payments and salaries;
- all foreign currency receipts into Myanmar bank accounts will be converted into MMK at the CBM reference rate;
- all foreign currency payments out of Myanmar will need to be for an approved purpose contemplated by the foreign exchange laws, properly documented and approved by the FESC, which could pose substantial red tape and delay;
- businesses currently purchasing foreign currency in Myanmar from exporters and other third parties will no longer be able to do so, but will only be able to make such purchases from

Authorised Dealer banks (i.e. banks which are licenced to engage in foreign currency and cross border transactions) at the CBM reference rate;

- the inability to hedge against the volatility of the MMK by keeping funds in foreign currency. This would not be an issue if the CBM reference rate remains unchanged at MMK1850 to the USD, but it will not be possible to hedge against any further devaluation. It should be noted that the CBM retains the discretion of changing the CBM reference rate;

- a reduction in foreign investment, at least in the short to medium term, as foreign investors assess the impact of the policy and how it affects the ability of businesses to remit funds back out of the country (eg to pay dividends, interest on loans and repayment of loan principal and returns of capital);

- the ability to obtain offshore financing if lenders are concerned of the risk that repayments will be held up by the newly implemented approval process and borrowers are unable to manage repayment obligations due to unhedged devaluations in the MMK;

- in an attempt to minimise the impact of the changes, businesses may shift part of their operations which are not country specific offshore. This could include the provision of services and certain back office functions and relocation of senior staff; and

- constraints on businesses operating within the country to import the necessary equipment and raw materials with the process of obtaining foreign currency and trade financing becoming more burdensome.

The extent to which these impacts will materialise will come down to how the new policy and procedures are implemented. This is still a work in progress. One key point to watch relates to whether exemptions are going to be granted from needing to comply with the requirement to convert foreign currency holdings into MMK. The FESC is authorised to issue such exemptions and several embassies have already approached the government requesting that investors and organisations from their respective countries are issued such an exemption. Wide ranging exemptions may soften the impacts of this policy, but run the risk of leading to a discriminatory investment environment, inconsistent application of regulations and more red tape.

3 REGULATOR

Cross border foreign currency transactions are principally regulated by the Foreign Exchange Management Law 12/2012 (FEML) and the Foreign Exchange Management Regulations 7/2014 (FEMR). Under the FEML it is the CBM which has the authority to regulate cross border foreign currency transactions. The administration of the law, particularly in relation to the monitoring and approving of foreign currency transactions, is the responsibility of the Foreign Exchange Management Department of the CBM.

The new regulatory regime introduced by notification 12/2022 empowers the new FESC to issue approvals for offshore remittances, issuing exemptions and monitoring compliance with notification 12/2022.

It is understood that the members of the FESC will include Minister level appointees and be chaired by a member of the State Administration Council (SAC – the peak authority formed by the Military following its re-assumption of political power in February 2021). It is expected that the FESC will report directly to the SAC and not sit under the CBM. As the FEML currently grants authority to the CBM to regulate cross border and foreign currency transactions, it is not yet clear how the FESC will exercise the legal authority to regulate foreign exchange and foreign currency matters.

Further clarification is also required on how the FESC will process the necessary approvals to allow cross border foreign currency transactions permitted by the FEML. It would be a momentous task for it to approve every single application to make offshore transfers. It may instead prescribe the approval criteria and delegate the task of issuing individual approvals to another authority, such as the Foreign Exchange Management Department under the CBM. This has yet to be seen, and a number of other legal and practical matters will need to be addressed for the new exchange restrictions to operate systematically.

4 CONSISTENCY WITH OTHER LAWS

Businesses operating in Myanmar have certain rights in relation to foreign currency transactions under existing laws. These are principally contained in the FEML and the Myanmar Investment Law 40/2016 (MIL) and the Rules made under them.

Under the MIL foreign investors have the right to transfer abroad:

- proceeds, profits from asset, dividends, royalties, patent fees, license fees, technical assistance and management fees, shares and other current income relating to the investment;
- proceeds from the total or partial sale or liquidation of an investment or property owned by an investor;
- payments made under a contract, including a loan agreement;
- payments resulting from any settlement of investment disputes;
- compensation received by an investor, including for expropriation; and
- salaries and other remuneration of foreign experts employed in Myanmar.

The circumstances in which these transfers may be prevented or delayed are limited to where the business has some outstanding obligations or is not operating compliantly - meaning that businesses should not otherwise be restricted from making these transfers (although the MIL does contain a proviso allowing restricted measures to be introduced in exceptional circumstances).

The MIL – which applies to both domestic and foreign investors - also contains a guarantee that investments will not be "expropriated" without due process and compensation being paid. Expropriation is defined broadly to include "indirect" expropriations, which could potentially include a loss of business or investment brought about by a change in law. Similar investment guarantees are found in investment treaties between Myanmar and other states, and it may be that some businesses who have had their domestic foreign currency holdings converted and their ongoing operations severely impacted examine these provisions to see if they provide any relief.

Under the FEML cross border transactions are divided into current account transactions and capital account transactions. Current account transactions are defined as transfers and payments made for trade, services, short term bank loans, interest on loans, income from investments and overseas family living expenses. Capital account transfers are defined as payments or transfers made for any other purpose.

The FEML requires that current account transfers should be able to be made without any direct or indirect restrictions. The process for making these payments is contained in the FEMR which include providing satisfactory evidence on the purpose of the transfer, if the documentation is satisfactory then the Authorised Dealer bank may execute the transfer.

Capital account transactions can generally also be approved by the Authorised Dealer bank however come under a heavier level of scrutiny and may require some prior approvals to be obtained.

The implementation of the policy and requirements under notification 12/2022 will ultimately determine whether these are inconsistent with the rights of investors under the MIL and FEML. Much will depend on the future direction of this policy to see if the issues raised so far can be resolved.

*** * * * ***

SCM Legal will continue to provide updates on the evolving situation. To receive these updates sign up to our mailing list at https://www.scm-legal.com/news-resources and please get in touch if you have any particular questions by emailing us at info@scm-legal.com.

About us

SCM legal is a leading independent firm in Myanmar owned and operated by the team who prepared Myanmar's new Companies Law and Investment Rules. We provide practical, correct and creative advice and insights to help investors succeed in this challenging market.

We are led by a diverse internationally and Myanmar qualified team of Partners with global law firm backgrounds and over 40 years combined experience in Myanmar.

We cover all areas of Myanmar commercial law and have completed transactions in almost all sectors, with real depth in the telecommunications, financial services, consumer goods, government, real estate and manufacturing sectors. We provide a range of other corporate services too including company formation and administration, accounts, payroll services and translations.

SUMMARY OF INSTRUCTIONS ISSUED BY THE CBM

Date	Instrument	Key points
18 March 2022	Letter FE-1/680	The CBM issued instructions to Authorised Dealer banks relating to the opening and operation of foreign currency accounts: • foreign currency accounts should only be opened where customers need to receive foreign currency in accordance with the nature of their business • when a customer receives foreign currency the bank must determine the legitimacy of the receipt of such foreign currency • domestic payments may only be in MMK and where the payment is made from a foreign currency account it needs to be converted into MMK before being transferred. Foreign currency is only to be used for offshore payments
3 April 2022	Notification 12/2022	• all foreign exchange earnings of residents must be sent to foreign currency accounts opened at an Authorised Dealer bank • all foreign exchange earnings received by residents must be deposited with an Authorised Dealer bank and exchanged into MMK within 1 working day. This requirement to exchange all foreign exchange also applies to foreign exchange currently held in foreign currency accounts on the date of issue of this notification (note that this requirement to exchange current foreign currency holdings has been rolled back for the time being) • all offshore remittances must be carried out by an Authorised Dealer bank and can only occur with the approval of the Foreign Exchange Supervisory Committee

Date	Instrument	Key points
		• the previous CBM notification 35/2021 has been revoked. This notification applied to foreign exchange export earnings which required that these earnings were sold within 30 days of receipt and that they were then to be used within a further 30 days, otherwise they were to be exchanged into MMK. These only applied to import earnings, whereas this new directive applies to all foreign currency
3 April 2020	Directive 4/2022	• starting from 4 April 2022 Authorised Dealer banks are required to convert any overseas earnings received by their resident customers from trading or non-trading activity into MMK within 1 day. There will be exemptions, however these are not yet announced • the exchange rate to be applied is MMK1850 per USD. The exchange rate is subject to change with notice of the CBM • Authorised Dealer banks may process offshore remittances subject to obtaining approval from the Foreign Exchange Supervisory Committee • Banks are required to convert foreign currency currently in foreign currency accounts into MMK, (this has been rolled back and is subject to further instructions of the Foreign Exchange Supervisory Committee)
4 April 2022	Letter FE-1/17	• the previous directive 18/2021, requiring that foreign currency exchanges must use an exchange rate of +/-0.5% to buy or sell foreign currency has been revoked (note that under directive 4/2022 a new reference rate has been set of MMK1850 per USD and that all exchanges should occur at this rate, with banks able to charge a service fee of MMK3 of each dollar exchanged)

Date	Instrument	Key points
4 April 2022	CBM responses	The CBM had a meeting with Authorised Dealer banks on 4 April 2022. After the meeting the CBM released responses to several questions which were raised at the meeting. Some of the key points included in the responses are: • for funds held in foreign currency accounts prior to 3 April 2022 it is not required to exchange all these funds into MMK within one working day. It is not clear whether these foreign currency amounts held in accounts can continue to be held indefinitely as foreign currency or whether they will eventually need to be converted into MMK • where a bank's customer has been accumulating foreign currency for the purpose of repaying a foreign currency loan, it is not required to convert these funds into MMK, however the bank must take steps to confirm that these funds are to be used to repay the loan according to the repayment schedule and if the loan is an offshore loan that the repayment needs to be approved • the banks customers are permitted to purchase foreign exchange to settle LCs which become due. Approval is required prior to transferring foreign currency abroad • where banks have entered into swap agreements with their customers, it is not required that foreign currency held by their customers are converted into MMK before the end of the swap. Furthermore, swap agreements are not covered under notification 12/2022. It should be noted that this may mean that it is possible to continue using currency swaps as a hedging instrument, however with little guidance from the CBM it has yet to be seen if this will work
5 April 2022	Directive 5/2022	Notification 12/2022 does not apply to foreign currency accounts held by the Union Government and Union Ministries.

Date	Instrument	Key points
5 April 2022	Directive 6/2022	• clarification that the requirement to exchange foreign currency received from offshore sources must be converted into MMK by the Authorised Dealer bank on the transaction date. The directive specifically confirms that this applies to export earnings, service fees, investment funds, disbursements of offshore loans and unilateral payments (these are transfers for the purposes of gifts, donations, maintenance charges, heritage works, receipts from the transfer of estates, and other allowances or aid) • offshore remittances require the approval of the Foreign Exchange Supervisory Committee. The directive specifically clarifies that this includes payments for imports, services, dividends and the repatriation of investment funds, offshore investments, repaying offshore loans and paying for expenses relating to overseas trips • once approval from the Foreign Exchange Management Department is obtained the bank can sell to its customer foreign currency for the approved transaction at the CBM reference rate and the bank is permitted to collect a service fee of MMK3 per dollar exchanged