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Insolvency 2021

Myanmar: Trends & Developments
Christopher Hughes, Stefan Chapman
and Min Min Ayer Naing
SCM Legal

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Trends and Developments

Contributed by:

Christopher Hughes, Stefan Chapman and Min Min Ayer Naing
SCM Legal see p.8



Overview

A decade of rapid growth, internationalisation, law reform and democratic transition came to a shuddering halt in Myanmar with the re-assumption of full political power by the military (*Tatmadaw*) in February 2021. The effects of the coup were compounded by a devastating third wave of COVID-19 from around June, which is only just beginning to come under control.

Myanmar is once again in the league of pariah States – the subject of critical resolutions by the UN Security Council; targeted sanctions by the USA, UK, EU, Canada and others; condemnation from many other governments who had been providing significant financial and technical support for the transition; cut-off from direct support by multilateral organisations and development finance institutions; and even effectively excluded from some significant meetings of ASEAN, the most important regional political and economic grouping for Myanmar.

Conditions on the ground remain volatile, with periodic outbreaks of rebellion followed by violent suppression as the *Tatmadaw* seeks to consolidate its political authority around the country. COVID continues to be a significant threat to lives and livelihoods and poverty is rising.

A number of high-profile multinationals have either left or announced their intention to exit their Myanmar investments, whilst many more have put investment plans on hold while they assess the long-term outlook.

Implementing an efficient and responsible voluntary exit from the country is a complex and time-consuming exercise, however, with myriad regulatory, financial, and social factors to be managed. For example, Telenor – the Norwegian telecommunications company that did as much as anyone to unleash the digital revolution in Myanmar, and which in doing so became a darling of responsible investment and business for human rights organisations both in and outside of Myanmar – has faced significant criticism of its decision to exit Myanmar from previously supportive groups, including formal complaints to the OECD. The approval it requires to complete its exit has been pending for several months and a number of its foreign managers located in Myanmar have been required to remain in the country while the matter is considered.

For those forced to wind-up their businesses due to the adverse economic conditions the position is even more complex, with the heightened risks that go with an uncertain and volatile regulatory and political environment. Creditors have had to show much flexibility and forbearance, in part because the legal framework to support their rights to recover debts is not operating as it should. Simply repatriating funds offshore has become a very onerous process.

Creative and practical strategies are needed to work in these conditions, based on a thorough knowledge of the relevant institutions and their key personnel. With the political and economic crisis giving rise to a significant brain drain on top of everything else there are significantly few-

er people in country who can help devise and implement these strategies.

Market Conditions

Market conditions are unprecedented, with political, economic, and social challenges of immense scale converging to make ordinary business activity near impossible for many firms. The twin factors of the coup and the COVID-19 third wave severely interrupted operations as workers stayed at home and businesses were required to close, compounded by supply chain interruptions, restrictions on telecommunications and implementation of de facto capital controls. Some of these constraints continue, while the legacy of others is still to be reckoned with.

Economic challenges

Myanmar has done a 180-degree turn – from being among the fastest growing countries in the region (and the world), it is now facing the largest forecast decline in GDP growth in ASEAN. The World Bank recently downgraded its forecast to anticipate an 18% economic contraction in FY21, with an expectation that up to 1 million jobs will be lost. Further, the IMF has now forecast no or very low growth through to 2026.

The Myanmar Kyat has depreciated substantially against the USD and other exchangeable currencies too, forcing prices of imported goods up and exposing those servicing offshore borrowings with domestic earnings to particular problems.

Official figures are that foreign direct investment fell by 22% in the year to September, the lowest figure in eight years, with the majority of new projects being approved in the quarter prior to the Tatmadaw's takeover. Commitments to many existing projects have been paused or scaled back and development finance – critical in Myanmar's emerging economy – has effec-

tively been switched off as multi-lateral and other development finance institutions paused their operations.

At the same time, government revenues are significantly lower, with the tax to GDP ratio now said by senior government officials to be down to around 5-6%, leaving little room to fund recovery measures, especially with the security situation and consolidation of political power being the main policy priority. Unemployment has risen steeply.

Political situation

With the *Tatmadaw* continuing to aggressively seek to exert control across the country, and the opposition movement becoming increasingly militant, some commentators have ventured that Myanmar may be moving towards “failed state” status. This may be overstating the situation, however, the political situation continues to weigh heavily on business.

The government touches almost every aspect of business life in Myanmar, and the responsiveness and capacity of government has greatly diminished, and the predictability of administrative decision making has declined. Previously routine processes – such as licence applications and requests for approvals – have become complicated and time-consuming (falling from an already low base).

Many businesses and their management have felt the effects of the political opposition too, with an active “social protest” movement inspiring consumer boycotts and other actions against businesses and staff seen as supporting or legitimising the government at home, and pressure from human rights and other advocacy groups abroad causing many to rethink their approach to doing business in Myanmar.

Sanctions

The UK, USA, EU and other governments have imposed “targeted” sanctions against a number of *Tatmadaw* and government officials, military linked enterprises and other parties. While these may not have directly impacted many transactions, they are exerting a chilling effect on investment more generally, making it harder for Myanmar companies in particular to access markets, partners and finance. Many foreign investors and managers are even meeting officials on routine or administrative matters.

Capital controls

The Central Bank of Myanmar and private banks have implemented a range of measures to limit the amount of money that business and personal customers can withdraw from banks, while at the same time exerting greater control over outbound currency remittances. The severe devaluation of the Myanmar Kyat has also led to restrictions on the availability and use of US dollars in the domestic market.

Regulatory responses to the currency crisis have proven somewhat inconsistent and ineffective, and it is worth noting that many of the most senior and expert financial regulators and advisers have been detained or removed from office since the coup, with many mid-level officials also taking extended industrial action.

With many businesses having a significant part of their cost base denominated in US dollars whilst earning the bulk of revenue in Myanmar Kyat the twin pressures of a falling exchange rate and reduced US dollar liquidity is causing a greatly increased risk of insolvent trading, even when the firm’s Myanmar Kyat reserves may be otherwise adequate.

Without injections of new US dollar equity some firms will be unable to service their offshore debt or pay their overseas suppliers, however, the

business case for an investor to put more equity at risk in Myanmar is a very difficult one to make.

Access to finance

The local debt market has become very constrained with bank balance sheets under immense pressure. While the imposition of stricter prudential controls on local banks has been deferred, banks are finding it very difficult to make new credit available given their capital constraints, greater numbers of customers seeking to withdraw their deposits and increased numbers of distressed borrowers seeking to reschedule their existing loans. The risk of a crisis in the local banking sector is real.

International banks active in the country are generally looking to limit exposures, for both economic and reputational reasons, and new development finance has all but dried up. With trading conditions in most sectors extremely challenging many businesses are in distress.

Insolvency Issues

Business landscape

With the business outlook so negative, off the back of an already difficult 2020, many more firms are at or near insolvency and desperately seeking accommodations from their lenders and suppliers. Others are simply closing their doors - most involuntarily, with a very small number exiting the market for reputational and other strategic reasons. Doing so in a compliant fashion is not an easy process.

Status of the Insolvency Law

A new Insolvency Law and Rules took effect, with limited pre-planning or warning, in early 2020. Their preparation was sponsored by the Asian Development Bank as part of a program of significant business law reforms that began in around 2013-14. Specialist insolvency practitioners from Australia acted as lead advisers on the project and the law draws on concepts and

processes present in the Australian system and in other developed common law jurisdictions.

The Insolvency Law also has interesting features aimed at enhancing effectiveness in Myanmar's emerging market context, particularly its simplified provisions for managing the insolvency of micro and small to medium sized enterprises. The rules for personal bankruptcy are also contained in the law, which effectively displaced the previous framework that existed under the Companies Law and older insolvency acts.

An important aspect of the new law is the process for corporate rehabilitation and rescue, similar to the process of corporate administration under Australian law. This allows for flexibility in the approach to restructuring a company, with a view to preserving as much of the business as is viable as an alternative to its liquidation.

While the law itself marked a significant advance in technical terms, the regulatory system and professional know-how needed to support it has not yet been developed. This has resulted in an unfortunate situation where the old laws no longer apply, while the new law is largely unable to be used in practice – even for the voluntary winding up of companies.

It should also be noted that the Insolvency Law does not apply to banks, which are instead regulated under the Financial Institutions Law. While the Central Bank of Myanmar is the agency responsible for overseeing bank insolvencies, detailed rules for this have not been developed. With not even a framework for an orderly restructuring, and the government itself having limited financial reserves or access to liquidity to support banks which may become distressed, a large-scale crisis in the financial sector is possible.

Regulatory challenges

The institutional apparatus for the predictable and efficient restructuring or winding up of an insolvent business in accordance with the new Insolvency Law does not yet exist, and the capacity of regulators and insolvency practitioners to apply and adapt the law in a practical fashion is also limited. Disruptions to the regulatory bodies and the professions due to COVID-19 and the political situation have compounded the problem, as has the effective withdrawal of technical assistance to support the implementation of the law and the development of regulatory capacity by Myanmar's development partners.

The new insolvency law framework relies on the courts to oversee and apply the law, which is new in many fundamental respects. Judges and court staff have received little external training in the application of this law and specific Court procedures are still to be developed.

The Insolvency Practitioners Regulatory Council is the authority responsible for the licensing and regulation of the Insolvency Practitioners who are empowered to conduct insolvency proceedings under the law. It is also responsible for setting professional standards and other functions relevant to the conduct of proceedings. There has been significant turnover in the membership of the Council and other constraints on its operation, which has meant that no Insolvency Practitioners have yet been licensed to practice - more than 18 months after the Insolvency Law came into effect. Without licensed insolvency practitioners it is not possible to conduct insolvencies in the manner contemplated by the law.

DICA, the corporate regulator, has an important role in the administration of the Insolvency Law too, particular in the maintenance of registers where insolvency related filings must be made. Licensed practitioners must also be registered

with DICA. These registers have not yet been established.

Foreign creditors face particular regulatory challenges in the context of insolvencies and restructurings given restrictions on holding interests in land, restrictions on ownership of certain types of business and difficulties in acquiring or transferring key business operating licenses and other government approvals. Enforcement of security through the Myanmar court system, and enforcement of foreign judgements or arbitral awards, is difficult and potentially unpredictable.

Offshore loans require Central Bank approval, as do major changes in terms or their refinancing, which limits flexibility for creditors and distressed businesses alike, and often results in significant delays in implementing new financing arrangements.

The Need for a Robust and Practical Framework

On paper the legal framework for managing insolvencies in Myanmar is quite good – a familiar, coherent and reasonably well adapted set of rules which balance the interest of different stakeholders and give primacy to the efficient restructuring of distressed enterprises where it is possible to do so.

In practice, it is inoperative and therefore not protecting those who need it. This places more pressure on an economic system which is already in crisis. Interim regulatory measures to facilitate the most basic winding up and restructuring processes, and which provide some discipline on boards and some assurance to those with a credit exposure to distressed enterprises, are desperately needed. We are trying to support the development of these.

Until then, commercially negotiated outcomes, with case-by-case interventions by the corpo-

rate and investment regulatory agency, and to a lesser extent the courts, will continue to be the norm.

Likely Developments and Practical Strategies

The continued application of regulatory and de facto capital controls will cause more firms to both look for mechanisms to remit or keep funds offshore and to manage liquidity, particularly foreign currency liquidity, onshore. Care needs to be taken when evaluating and implementing such capital and currency management initiatives as this is an area subject to heightened regulatory scrutiny and intervention.

With the financial sector in such difficulty the availability of credit will continue to decline. Economic conditions are expected to remain depressed and new equity will be scarce. Deleveraging will occur, debt will be rescheduled and/or converted where possible and more firms unable to do this will default on their obligations and collapse. Implementing a capital restructure requires significant planning, careful negotiation, robust documentation and a lot of regulatory follow up.

The government is unlikely to be able to offer significant support to distressed enterprises, however regulators at different levels will need to be involved in managing the consequences of significant enterprises which fail. Advancing creditor claims in these circumstances will require patient and effective advocacy.

Directors and shareholders of failed enterprises are likely to come under more pressure from creditors and regulators, with unpredictable outcomes (and heightened exposure to criminal sanctions). An ability for those impacted to properly and compliantly engage the relevant regulators and protect their position (or limit the most adverse outcomes) will be key.

MYANMAR TRENDS AND DEVELOPMENTS

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Secured creditors, especially those which are foreign owned, will continue to face obstacles when enforcing security. Practical asset protection and realisation measures are likely to be as or more important than the legal enforcement of contractual rights, and a preparedness to engage closely with debtor entities and regulators, with the assistance of skilled advisers will be necessary.

More companies will look to voluntarily suspend trading and exit the market. With the legal framework for voluntary winding up still in flux, and a range of regulatory notifications and, in some cases, approvals, required to complete an exit, making a clean break, responsibly and compliantly, is not a simple exercise. Compliant structures and processes to facilitate a quicker exit can be implemented with the right on the ground advisory partners.

Since the coup almost every action involving regulatory approval is taking more time, with applications perceived to be complicated, sensitive and/or involving the transfer of significant funds offshore subject to lengthy delays. For investors from jurisdictions which have imposed sanctions on Myanmar (eg, the USA, UK and EU) engagement with government officials by is often considered to be problematic (if not technically in breach of the applicable sanctions frameworks).

Patience, persistence and effective and ethical local support is necessary.

Many Myanmar people are currently facing great hardship and political sensitivities are running high. The possibility of community backlash against investors or creditors perceived to be engaging inappropriately with the *Tatmadaw*, high ranking government officials, military linked enterprises or other organisations perceived as being close to the government is high so care needs to be taken if engagement with such parties is necessary.

Exiting responsibly and treating all Myanmar staff, partners, suppliers, customers, communities, and other stakeholders with sensitivity and with full recognition of their rights, interests and needs is also critical.

Conclusion

Restructuring or being involved in the insolvency of a business in Myanmar at the moment is about as difficult as it can be. Unfortunately, the need to do so is increasing rapidly. The consequences of a mismanaged process can be significant and it is imperative to ensure that effective local support is on hand at all times.

SCM Legal is a leading independent firm in Myanmar owned and operated by the team that prepared Myanmar's new Companies Law and Investment Rules. The firm provides practical, correct and creative advice and insights to help investors succeed in a challenging market. SCM Legal practises Myanmar, English and Australian laws, and is led by a diverse partner team with magic circle and global law firm backgrounds, and over 30 years' combined

experience in Myanmar. The firm covers all areas of Myanmar commercial law and has completed transactions in almost all sectors, with real depth in the telecommunications, financial services, consumer goods, government, real estate and manufacturing sectors. It also provides a range of other corporate services, including company formation and administration, accounts and payroll services, and translations.

AUTHORS



Christopher Hughes is a founding partner of the independent Myanmar firm SCM Legal, which he started in 2018 after a career with the international firms Baker &

McKenzie, Clifford Chance and Bryan Cave Leighton Paisner. He has been based in Myanmar since 2013 and drafted the Myanmar Companies Law 2017 and Myanmar Investment Rules 2017 for the government. Chris is experienced in major M&A and finance transactions, infrastructure projects and PPPs, privatisations and government reform programmes. Chris is chairman of the Australia–Myanmar Chamber of Commerce.



Stefan Chapman relocated to Myanmar in late 2011, making him one of the first internationally trained transaction lawyers to be based in the country. Stefan has

assisted many foreign investors in establishing and carrying on their operations in Myanmar, particularly in the infrastructure and telecommunications sectors, working on some of the largest M&A transactions in the country. Stefan was involved with the drafting of the Myanmar Investment Rules for the government and has considerable experience in working with investment-related authorities. Stefan is a director of the Myanmar Venture Capital and Private Equity Association.

*Contributed by: Christopher Hughes, Stefan Chapman and Min Min Ayer Naing, **SCM Legal***



Min Min Ayer Naing joined SCM Legal as a partner in August 2018 following extensive experience at international law firms, Baker & McKenzie and Kelvin Chia in Yangon. She

brings over 20 years of legal experience in acting on local Myanmar matters and international transactions. Min Min has special expertise in foreign investment in Myanmar, including a deep understanding of the role of regulators and permitting and approval requirements. In addition to foreign investment, Min Min regularly advises on a wide variety of corporate, banking, compliance, regulatory and employment matters for Myanmar and international clients.

SCM Legal

#16-05 Sule Square
221 Sule Pagoda Rd
Kyauktada Township
Yangon Yangon
Myanmar

Tel: +95 979 575 8272
Email: office@scm-legal.com
Web: www.scm-legal.com



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