

COMMENTS ON DRAFT LEGAL PAPERS ON FOREX CONTROL

*Presented by
Treasury Sub-Group/Banking Working Group*

The VBF Banking Working Group would like to send the warmest greetings to the State Bank of Vietnam. We appreciate the opportunity to review and comment on the following draft legal papers on forex control:

- Draft Circular on Foreign Exchange Transactions in Vietnam Foreign Exchange Market (No.40661/NNNN-QLNH)
- Draft Circular on the Foreign Exchange Control of Foreign Investment into Vietnam
- Draft circular on Foreign Exchange Control of Domestic and Overseas Securities Issuances
- Draft Circular on Instructing Lending Overseas and Collect Debts from Overseas for Residents being Organizations

Below are our detailed comments. We would like to submit these to the State Bank of Vietnam (SBV) for its consideration in the process of drafting the legal papers.

I. Comments on Draft of Circular on Foreign Exchange Transactions in Vietnam Foreign Exchange Market

In general, the “New draft Circular” has relaxed some of practices as well as the range of foreign exchange activities. However, according to the liberalization spirit of FX ordinance 28/2005 PL – UBTVQH 11 dated 13/12/2005 and Decree 160/2006/ND-CP dated 28/12/2006, this circular is not as clear and does not present the whole new idea of foreign exchange transactions in Vietnam foreign exchange market as Decision No 1452/2004 / QD –NHNN dated 10/11/2004 in particular transaction related to VND.

Article 1:

1. We would like to have a definition of Vietnam foreign exchange market in order to know more clearly about the range of foreign exchange activities. Moreover, we would like to know whether there is any differentiation between FCY/FCY and FCY/VND.

Article 2 point d:

2. We would like to make some changes as follows: “Swaps are two simultaneous of sell and buy transactions of the same amount of **one currency (there are 2 currencies involved in the transactions)**”. This is to omit ‘foreign’.

Article 5 point b:

3. We would like to have a clearer definition of “Economic organizations” and “Other organizations and individuals (including unauthorized credit institutions)”? Do they include offshore organizations? We would like to add the classification of “Residents” and “Non-residents”. We need clear guideline regarding non - resident. It is very important to do so to avoid confusion later on.

Article 6 point b:

4. We also would like to know whether regarding options against VND, authorized institutions are allowed to buy options in VND.
5. Financial institutions can not buy option from corporates and individuals. With international practice, we normally sell structured options which include of both

selling and buying options simultaneously which will result in a zero cost structure for the clients.

In a structured option, where there is a simultaneous buy and sell of an option by the bank with the client, and which results in the client not receiving any premium from the bank, we request that this should be allowed because there is no unlimited risk on the part of the client.

6. Also, exemptions should be made for certain options that have economic organizations and other organizations and individuals which will be able to contribute to the development of the Vietnam financial markets. Included in this category are supra-nationals such as the IFC, ADB, World Bank, etc. Potential bond issuances by these supra-nationals in the domestic markets will require cross currency swap transactions that will provide the benefit of creating swap benchmarks and bring the Vietnam financial markets to par with international standards.
7. Whether we can use USD/VND FX spot and forward to hedge the exposure for all FX option position and this one will not be counted in daily FX position limit.

Article 6 point c:

8. We would like to know “Why Authorized Financial Institutions are not allowed to execute swap transactions with customers who are other organizations and individuals?” According to Article 6 point a, authorized financial institutions are allowed to execute spot and forward transactions with other organizations and individuals, therefore we would like to know the reasons of not allowing to execute swaps relating VND with other organizations and individuals

Article 7:

9. Determining the daily exchange rates should not be included as a responsibility of the General Director. First, it is driven by market forces. Second, the foreign exchange unit of every credit institution should be the one tasked to provide these daily exchange rates to all parties concerned.

Article 9 point a:

10. We would like to amend as follows: “Parties to FX transactions can conclude deals via telephone, telex, or through other means as agreed by credit institutions as per international practices (Reuters and Bloomberg) and, in the future, through SBV-accredited brokers and relevant prevailing laws and regulations. Transactions are legally binding right after the parties conclude them via telephone, telex or through any other means as mentioned above.

Can we also conclude the deal via internet as well since some Bank have offered to all their interbank customers. (FX online trading).

Article 9 point b:

11. We would like to amend as follow: “Deal Confirmation: Upon concluding a FX transaction, a formal deal confirmation document must be signed by both counterparties. The content of and timing to send a confirmation is decided by credit institutions as per international practices and current regulations. Each credit institution shall be required to issue a confirmation to their counterparty. Failure to issue a FX confirmation will not make a deal invalid, provided that the party that

claim compensation would be able to provide supporting documents, including, but not limited to, the deal tickets from an acceptable trading platform such as Reuters, Bloomberg or recorded phone call.

12. Similarity, if on value date the counterparties fulfill their respective payment obligations under the FX transaction despite a party failing to receive the counterparty confirmation from the other credit institution then the transaction will be considered as settled and it is not required to obtain the missing confirmation.
13. Moreover, SWIFT confirmations should be allowed in the interbank markets and with customers who are capable and able to confirm through this method; the SBV regulation should be open to other forms of confirmation that may develop and will be acceptable in the international markets.

Article 10 point a:

14. We would like to supplement as follows: “When a client being an economic organization, other organization and individual buys foreign currency against VND from an authorized credit institution, they have to submit necessary documents supporting the purpose, amount, payment currency, and **estimated** payment date as required by current regulations on FX control”.
15. In order to avoid disputes which may arise we would like to request the State Bank of Vietnam to release a Circular promulgating detailed instructions on required documents for FX sale and FX purchase and cross border payments; or Commercial banks to prepare their own check list of supporting documents for the State Bank of Vietnam to approve Commercial banks will execute the checking against such approved list.
16. In reality, for forwards deals, many customers may not have enough documentation when the deal is booked, can they submit documentation when the deal is settled? Please provide guidance on what minimum documentation is required on trade date and how long thereafter to complete such documentation requirements.
17. Is it required to check supporting document for SWAP transaction? (eg. in transaction USD_VND_USD. Does the Bank need to check docs for the second leg)
18. We would like to know if corporate client buy foreign currency for the payment of current transactions, what is the **maximum holding period** that client can keep their foreign currency in their current account ?

II. Draft Circular on the Foreign Exchange Control of Foreign Investment into Vietnam

In general, this new circular has significantly simplified and clarified the FX control framework of foreign investment in Vietnam. We highly appreciate the fact that the draft circular contains broader but concise guidelines. Moreover, it also provides flexible and suitable amendments for meeting practical demands for foreign investments into Vietnam and conforms with international practices.

In Chapter I: Indirect Investment**Article 1:**

1. Pursuant to paragraph a, scope of non-resident entities is very limited. Actually, many foreign entities (i.e. charity, endowment foundations...) are interested in investing in Vietnam market.

Article 3:

2. This Article provides that foreign investor shall open 1 (one) capital account in VND for indirect investment at 1 (one) authorized credit institution. As we are aware that under current forex control regulations as provided by Circular No. 03/2004 dated 25/05/2004 and Decision 1550/2004 dated 06/12/2004, it stipulates that there must be two (02) VND accounts to be opened for indirect investment purposes. In order to comply with the new regulations, these queries can be identified as follows:
 3. Whether the foreign investor will be required to close one of their existing VND accounts to be in compliance with the new regulations? Will foreign portfolio investors have to close these two VND accounts and open one to comply with this new Circular?
 4. Does this mean that one VND cash account is sufficient for both listed and unlisted securities? Can the investor open more than one cash account at a credit institution for different purposes and control by different holders?
 5. We suggest to change to Incoming/ Outgoing fund.

Article 4:

6. As provided in paragraph 4.1, will income from interest earned on surplus balances and funds transferred from one offshore investor to another (under the same relationship) be acceptable?
7. We know that currently the SSC is drafting regulations on guiding for investment into Vietnam securities market of foreign investors. In the draft, foreign investors are required to open both USD and VND cash accounts at a custodian bank for their investment in securities while the SBV allows transferring and receiving VND funds from their account at the securities company. It will confuse the market. Further, there's no stipulation for term deposits. Investors bring their money into the country and they are unable to disburse all funds in one or two days, so they will place this fund in term deposits. The term deposit can be placed at a commercial bank where they are maintaining their cash accounts or at another bank. It is also understood that this is considered as their receivable and payable account.

Article 5:

8. The term "within 30 days from the purchase date" may be confusing. We are of the opinion that it should be changed to "30 days after the FCY is received in the account".

In Chapter II: Direct Investment**Article 7:**

1. In accordance with provision in paragraph 6.1, the joint venture enterprises shall execute direct investments into Vietnam. May foreign partners in joint venture entities use their onshore income or funds in VND to make a direct investment? Will

they have to open a VND capital account for direct investments? Or will they have to buy USD from VND and open USD capital account for their investment?

Article 11:

2. Do customers have to use the foreign currency straight away after the value date? It is suggested to have a max. holding period in the account of up to 30 days since some customers have many small payments and can not settle all at once.

Article 12:

3. We are of the opinion that foreign investors will supply necessary documents and are responsible for the legality and accuracy of the documents. The verification of local authorized offices would not be required

Article 12, 13:

4. The SBV puts the responsibility on authorized banks to guide investors in terms of account opening and closing procedures including verification of supporting documents. To ensure a level playing field, could we suggest that the SBV provide the market with minimum standards in this area? Indeed, some banks may be tempted to have less stringent sets of requirements and thus benefit from unjustified advantages.

III. Draft circular on Foreign Exchange Control of Domestic and Overseas securities issuances

Article 2.1 b

1. We would appreciate if the SBV could clarify whether it intends to allow the securities investment accounts in foreign currencies to receive funds from other foreign currency accounts maintained at authorized credit Institutions without any restrictions, i.e. not subject to only security issuance activities.

Article 9:

2. We would like to understand whether the SBV, through this provision, intends to liberalize *the* Capital account transactions and lift the control on capital outflows. If the issuers want to transfer abroad of the FCY converted from VND collected locally, will there be any conditions imposed by the SBV?

Article 10.1 b):

3. similar to article 2.1 b)

IV. Draft Circular on Instructing lending overseas and Collect Debts from Overseas for Residents being Organizations

Part I

Article 2:

1. We are of opinion that there should exist a definition on foreign borrower (i.e. non-residents individuals who are not living, working and operating in Vietnam and non-residents organizations not being established and operated in Vietnam).

Part II

Foreign Lending and Debt Collection of Credit Institutions (CIs)

2. We understand that CIs are allowed to operate the lending business and they are strictly compliant with lending regulations including (i) monitoring borrowing purposes and lending approval process; (ii) lending limits; (iii) loan classification and provisions and (iv) other lending regulations including reporting requirement.

Such specific requirements are very unique and only applicable in banking industry but not in other businesses.

3. Given the above, in order to provide favorable conditions for credit institutions and to simplify the administration process, we are of opinion that credit institutions should not be required to register their loans overseas to the SBV and then receives SBV's confirmations. Instead, the credit institutions should be required to report their overseas loans to SBV on a monthly basis subject to reporting templates setting out by the SBV.

Annexes

4. SBV should consider making the forms in Spreadsheet (with fixed fields) so in future SBV can then use the file as the database and easily for any consolidated reports etc.

V. Other General Comments

ABN

1. We would like further clarification of the definition in Article 37 of the Degree 160.

Foreign exchange market is a market under which foreign currencies are traded. Participants to this market consist of the State Bank of Vietnam authorized credit institutions, foreign exchange desks and organizations, individual residents and non residents in Vietnam.

Interbank foreign exchange market is a market where transactions between the State Bank of Vietnam and authorized credit institutions and between authorized credit institutions together are conducted. Members to the interbank foreign exchange market conduct FX transactions with trading modes and processes based on agreement and commitments between parties following international practices and prevailing rules and regulations.

The SBV would need to clearly state under what conditions Decision 101 applies and when does 1452 or 160 apply. There should only be one set of regulations, so actually 101 should be superseded by 160, as will be 1452.

2. The State Bank of Vietnam is kindly requested to confirm if it is necessary for credit institutions, which already have FX license and separate licenses for each type of FX transactions to obtain again approval from the State Bank of Vietnam indicating allowed FX transactions when this Circular (to replace the Decision 1452) comes into effect.
3. State Bank of Vietnam would need to clearly state that the SBV regulations, including those on FX Transactions, are the regulations governing Banks, which are licensed by the SBV.

In our prior audit, relating to the ICB case, we were told that any higher law or ordinance will override a SBV regulation, even if that regulation specifically covers actions to be taken in the guidelines (ie. FX Contracts/Confirmations - Ordinance of Economic Contract was considered to override the guidelines set out for issuing FX Confirmations under Decisions 17, 1452, & 101) . In other words, even if a financial institution adheres to all rules and regulation issued by the SBV, it may unknowingly be in violation of non-SBV articles.

4. SBV would need to clarify what are regulations covering " FX Netting " and what sort of agreement needs to be in place for banks to do netting, if it is permitted. Presently, there is no regulation covering " FX Netting ", which leaves any transactions open to challenge.

Citibank

1. Confidentiality: Any credit organization that engages in trading in the interbank market must have appropriate measures to protect the confidentiality and integrity of all information entrusted to them. Chinese Wall measures should be implemented as applicable.
2. Dealing rooms of credit institutions should be secured and access is restricted to authorized persons. A statement should be included that shows that every credit institution that engages in interbank trading will ensure that all deals transacted through the acceptable conveyance instruments (telephone and dealing screens) are committed trades (thus, it is to their best interest to secure their dealing rooms from unauthorized persons).
3. Know Your Client/Anti-Money Laundering
 - a. Management of credit institutions must be aware of the risks involved in money laundering.
 - b. Reference should be made to strictly following the money-laundering laws of the country and appropriate internal controls such as account openings, documentation procedures and management information and monitoring systems should be in place.
4. Ethics

Management must establish an internal code of conduct that conforms to the relevant Vietnam laws, industry conventions and bank policies that may include:

 - i. Questionable trading practices
 - ii. Trading for personal account
 - iii. Entertainment and Gifts
5. Legal and Compliance
 - a. Legal, regulatory and reputation-risks have grown significantly in the financial markets, including the foreign exchange markets and infractions are quite difficult to detect. A Compliance Unit should be set up to provide employees awareness, training and enhanced due diligence.
 - b. Industry standard documents should also be encouraged to provide for sound mutual agreements among counterparties for conducting foreign exchange and other financial markets transactions such as Authority Documents, Confirmations and Master Agreements.
6. Risk Management

Effective risk management is necessary to prevent excessive losses for credit institutions in the areas of trading, positioning, sales, credit extension and operational activities. Thus, a comprehensive risk management strategy for the whole credit institution, detailed internal policies on risk-taking, strong information systems for managing and reporting risks and a clear indication of individuals and groups tasked to assess and manage risks must be evident.

7. Operations

- a. Operational risk happens in force majeure instances, or from day-to-day activities including differing methods and conventions used by two counterparties to transactions and from disruptions in the electronic processes of a credit institution. Inability to prepare for such results in huge losses, inaccurate reporting of trading positions and uncontrolled credit risks for all parties concerned.
- b. A provision must be placed into the regulations that specifically separate the trading and operations (backroom) aspects of the business. This is very critical to ensure that there is no collusion to defraud the credit institution and its clients of money that rightfully belongs to them, or to hide trading losses that result from adverse market movements.
- c. The confirmation process should be articulated properly in the regulations in that promptness and efficiency must be emphasized to ensure that no unauthorized dealing results and once identified, the problem can be rectified with minimal negative financial impact.
- d. Netting as a practice should also be articulated, particularly emphasizing that only legally enforceable documents should be used to protect the interest of all parties concerned. Presently, there is no regulation covering "FX Netting", which leaves any transactions open to challenge. It would be great if SBV can clarify what are regulations covering "FX Netting" and what sort of agreement needs to be in place for banks to do netting, if it is permitted.

8. Human Resource

- a. Credit institutions should have the necessary internal infrastructure to ensure that concrete hiring, training and appropriate trading guidelines is instituted. In this way, traders/dealers have the necessary integrity and tools to deal in the foreign exchange markets, protecting the interests of all parties concerned - their credit institution and that of their counterparties, including corporate clients.
- b. Most of the focus by management is on the trading personnel and the policies that govern them. The circular should also provide provisions on putting the responsibility to the management of credit institutions to put importance on developing the support staff or the back office in terms of training and control procedures that they must establish for the successful foreign exchange activities of the banks.
- c. There must also be a provision that emphasizes that the back office is sufficiently independent from the trading side in terms of organizational reporting lines to ensure that there is no pressure placed on them by the front office or trading and sales desks to collude to defraud, hide losses and alter reports to favor the front office.

9. International Practice

SBV would need to clearly state what "international standards" SBV regulations are referring to, as this again becomes a grey area, open to challenge. Why does SBV not join the standards group that most FX Trading countries subscribe to, as per the regulations we have on file. Same applies to accepting ISDA's and other internationally recognized standard documents.

We would like the State Bank of Vietnam to refer to The Model Code, The International Code of Conduct and Practice for the financial Markets, issued by the ACI- The Financial markets Association, as the international practices in this Circular instead of simply using "international practices."