

**DRAFT AGENDA ITEMS
THE BANKING WORKING GROUP MEETING WITH
THE STATE BANK OF VIETNAM**

1. Circular 40/2011/TT-NHNN dated 15/12/2011 on the issuance of license and organization, operation of commercial banks and foreign bank branches (“Circular 40”)

The Banking Working Group (“the BWG”) acknowledges the new requirements in the Law on Credit Institutions and Circular 40. However, the BWG faces difficulties in the licensing procedure due to unclear guidance on licensing steps and some administrative delays in license applications. Therefore the BWG requests the State Bank of Vietnam (“SBV”) to consider the extension of effective date of Cir 40 so as to allow credit institutions (“CIs”), and foreign bank branches (“FBBs”) to continue providing operations and services, which have not been stated in the Operating License and granted Sub-licenses but which were regulated by legal documents as stipulated in Article 37 of Circular 03/2007/TT-NHNN (replaced by Circular 40) to ensure the continuity of business. Moreover, we recommend SBV to only set licensing requirement for new ‘business activity’ but not for every single new products under same activity. And CIs should only need to register with SBV for such new products. For example, if the CI has FX and derivative activities in their license, they should be allowed to conduct all FX and derivatives products that the SBV has stipulated in relevant regulations instead of applying for every single product under these activities such as Cross Currency Swap (“CCS”).

BWG has also sent a separate letter to SBV on this subject and would appreciate SBV’s positive feedback.

2. Foreign shareholdings in local banks

Decision 254/QĐ-TTg of the Government on approving the Scheme of “Restructuring the Credit Institution System in the 2011-2015 Period” (“Decision 254”) encourages foreign banks to participate in M&A and integration with local banks. The decision also mentioned the consideration of allowing increased shareholdings of foreign banks in local banks which are under the restructuring plan. We understand that draft decree replacing decree 69/2007/ND-CP dated 20/4/2007 submitted to Government for approval keeps 30% cap unchanged with the limited exception for the case of M&E in weak banks. We request that any increase in foreign ownership of local banks should apply across all institutions. We believe that an increase in foreign shareholdings will help foreign bank shareholders to implement the risk management and governance reforms set out in Decision 254, which will otherwise take longer to achieve.

3. Circular 09/2012/TT-NHNN dated 10/4/2012 on using payment means for loan disbursement

The BWG supports the SBV’s intentions in promoting the use of non cash payments and ensuring loans are used for their stated purpose. However, the BWG suggests the SBV

should consider allowing Financial Institutions to use their own controlling mechanisms where these also satisfy the SBV's requirements. There are two main reasons:

- (i) If the disbursement does not go through the customer's own account, they will not be able to claim input VAT in accordance with circular 06/2012/TT-BTC dated 11/1/2012 of MOF; and
- (ii) Further, a major issue with Circular 09 is linked to the Core Banking/Accounting systems of foreign banks, which automatically cause disbursement through debiting internal loan accounts and crediting the customer's current account, before the loan is subsequently transferred to the beneficiaries. Changing core banking systems is a very costly and difficult exercise.

We believe that if foreign banks are required to change their core banking systems to comply strictly with Circular 09, there will be no greater compliance with the purpose of Circular 09, which we believe is well served by the proposal made by the BWG. In fact, it will increase lending costs. Therefore, we fully agree that overdraft facilities should strictly comply with the drafting of Circular 09, but respectfully request that in regard to loan disbursement, the SBV to give positive feedback on our proposal.

4. Draft circular replacing Circular 13/2010/TT-NHNN ("Circular 13") on Prudential ratios

We would like to thank SBV for the recent meeting with Safety Policy Department on BWG's comments on this draft and recommend SBV the followings:

- **On the CAR calculation:**
 - Capital includes the Net of placements by foreign bank's head office and branches in Vietnamese branch and its placements in head office and those branches. This confuses capital and loans.
 - Grandfathering of credit agreements signed before the effective date (to exclude those contracts in CAR calculation).
- **Single Borrower Limit (SBL)**
 - Credit extension towards cash collateralized facilities, guaranteed facilities, and other -approved facilities should not be subject to the Single Borrower Limit. We recommend SBV to keep the excluded cases as Circular 13 as the credit risk of this credit is either eliminated or mitigated, depending on whether they are cash-collateralized or payment is guaranteed by a third party bank.
 - Further, we continue to recommend that offshore guarantees or Standby Letters of Credit ("SBLC") from the head office or other offshore financial institutions be allowed to offset the credit exposure to a single borrower should a single borrower (or related group company borrowers) reach and need to exceed the single lending limits in Vietnam. A parent guarantee and/or SBLC has been extensively used to transfer risk between banks in many countries, allowing prudent lending above the single lending limit set by central banks. The guarantee and/or SBLC would be issued in respect of an exposure of the group entity to a third party, e.g. the off-shore parent bank guarantees its Vietnam branch or subsidiary against a specific exposure of the Vietnam branch or subsidiary to a third party borrower for amounts exceeding the single lending limit. This solution should enable corporate customers and large infrastructure projects in Vietnam to access their required large funding for business expansion. This solution will greatly help the efficient financing of large businesses and projects whilst simultaneously ensuring prudential credit exposure by banks.

Governor Binh, when he was still Deputy Governor, gave an indication that the SBV would adopt this recommendation, and we await a final response.

- **Liquidity requirement**

- 'Immediately Disposable Assets' should include balance of Nostro accounts at other banks, and lending or placements to other banks at maturity.

- **Solvency ratio**

- We recommend that SBV should not require this ratio for other convertible CCYs because these CCYs only account for small portion of the BS. Moreover, there is no FCY liquid asset (bonds and other valuable papers) in Vietnam. We have previously raised this but SBV has not taken into account in the latest draft.
- Banks can't comply with 100% for each CCY due to liquidity gap. Within 30 days, cash outflow always bigger than cash inflow because deposit tenor is always shorter than loan tenor given market situation.
- Cash inflow should consider the inflow from committed facilities provided by parent bank and cash outflow should remove the unconditional cancellable committed facilities to customers.

- **Loan to Deposit Ratio ("LDR") 80% for Banks and 85% for Finance companies**

- Recommend SBV to include capital in the source of fund. This ratio should be at 100% first with gradual reduction in line with overall market liquidity situation.

- **For Consumer Finance Companies**

We suggest more relevant safety ratios should be applied to Consumer Finance companies due to the different nature of the consumer finance industry. Consumer finance does not mobilize individual deposits from the general public, and has limited funding mobilization options so there will be a minimal positive impact on the whole banking system if all the safety ratios are applied in the same manner as required to banking system.

5. Draft circular replacing Decision 62/2006/QD-NHNN dated 29/12/2006

According to Decision 62 of the SBV and the draft replacing this decision, there is a cap set at 30% of a bank's capital on the total outstanding notional swap amount with clients. This limitation is unduly restrictive and has essentially shut down the derivative market in Vietnam.

Also there is no netting guideline in this draft. If trading partners within Vietnam were able to offset their positions or obligations with each other, it would help to improve market efficiency dramatically. Transaction costs would be reduced, as would credit and liquidity risks, and ultimately systemic risk. Additionally, given that netting results in more favorable capital treatment for credit risks, netting arrangements are crucial for Vietnamese-domiciled banks as it may help to improve their credit ratings when they participate in the international markets in order to hedge their positions.

Recommendation: We recommend the SBV to review the cap setting for the notional swap amount and allow netting in the new circular replacing circular 62. In the VBF and its position paper, we also recommend the government to work with industry and external experts to develop regulation on close out netting and set-off in line with international best practice. The BWG is pleased to cooperate with SBV in a more detailed working session on these subjects.

6. Circular 07 on NOP

Circular 07 on NOP does not take into account the NOP which is created from derivatives transactions, particularly CCS transaction which is a commonly used hedging instrument by clients. The inclusion of NOP created from derivatives transaction into the NOP calculation is of international practices as it correctly reflects the actual NOP of the bank for risk management. This will also help SBV to have a correct NOP number for effective management actions. We understand that there is currently lack of accounting guideline for derivative transactions which drive the reporting of NOP. We would like SBV to coordinate with the MOF to issue necessary accounting guideline and amend the Cir 07 to officially capture NOP created from derivatives.

7. Circular 03 on FCY lending and Decision 857/QD-NHNN on FCY short term loans

Circular 03 only allows CIs and FBBs to lend FCY to importers who have sufficient FCY income. Decision 857/QD-NHNN, which is effective until 31/12/2012, allows CIs and FBBs to lend FCY to exporters for domestic uses, but they are required to sell that FCY amount to the lenders. We recommend SBV to allow enterprises that generate FCY revenue to borrow short term and long term FCY loans for other legitimate purposes. For companies that do not have FCY revenue, the current law is not having the intended effect of encouraging a switch to VND borrowings, but rather is pushing the financing off shore, away from SBV supervision and to the detriment of the local banking sector.

8. Circular No. 21/2012/TT-NHNN regulation on operation of lending, borrowing; term purchase and sale of valuable papers with term among foreign CIs and FBBs

According to this Circular 21, from 01/09/2012, the consumer finance companies shall not conduct deposit activities (excluding payment account) at other CIs, FBBs. We are only allowed to borrow from other CIs with the term of less than 1 year. This change incurs some concerns (i) Deposit activities: Finance companies often deposit unused funds in banks, which is a safe, efficient, flexible profitability solution for us. However Circular 21 contradicts with other prevailing SBV circular requesting finance companies to keep 15% of its total liabilities in liquid form (cash). Hence we believe that SBV will continue encourage this investment (ii) Loan term: In addition to capital, loans from other CIs are necessary for the business of consumer finance companies since we are not allowed to mobilize capital from individuals. The consumer loans are normally granted to customers during the term 6-36 months or longer for Mortgages. The restriction of Circular 21 on the loan term as between CIs and FBBs for less than 1 year will generate maturity risk and will create a long term systematic risk. We expect SBV continues to allow the consumer finance companies to carry out the term deposit activities in other CIs as well as to remove the regulation on restriction of loan term from other CIs.

9. Foreign Account Tax Compliance Act (FATCA)

FATCA was introduced by US government in an effort to improve compliance of US tax payers on worldwide income and to combat tax evasion by US persons holding investment in offshore accounts. It has worldwide application to all institutions with a US banking license.

FATCA will take effect on 1 July 2013 and requires FIs globally to: register with the US Inland Revenue Service (IRS); update their client on-boarding and account opening process to ensure all US persons are identified and verified; report annually to the IRS the personal and account information of confirmed US customers; and apply a withholding tax on certain US customer types. Failure by a foreign FI to comply with FATCA will result in a 30% withholding tax penalty being levied by US IRS on their US earnings annually.

The BWG is seeking legal advice on the conflict within the laws and regulations in Vietnam. Article 14.3 of the recently promulgated Law on Credit Institutions requires only the consent of the customer for disclosing information to other organizations and individuals while Decision 45/2007/QĐ-NHNN states that information disclosures on customers' deposits and assets are secret information of the State and requires the approval from the SBV. We request SBV to provide the guidance whether the CIs are permitted to provide their customers' information to the US Tax authority with customers' consent.

10. Follow up of issues in previous meeting minutes that have no progress

- **Network and distribution:** The BWG requests clarification on when the new regulations on network of commercial banks will be passed. The SBV has stopped licensing for new branch network pending the new circular.
- **Interest rate subsidy reimbursement**
For over two years, banks have been due a reimbursement of an interest subsidy as part of the subsidy program that ended in 2009. We have complied with all data requests in relation to the reimbursements and the amounts due are clear. We understand that the State Audit has performed an audit review on compliance to this program and confirmed the figures already. It has been two years now and the unpaid accruals begin to pose a problem for banks' internal accounting policy and audited financial statements. We understand that 14 banks have been settled the payment. We request the SBV to continue to make the necessary payments as soon as possible for the remaining banks.
- **Wealth Management Products**
The BWG requests a more active process to develop guidelines of wealth management products. While the SBV granted licenses to a number of banks to offer structured deposits as investment products, these products have not been able to be developed because they are being treated as needing to comply with the deposit cap requirements, rather than as investment products.