Myanmar’s historic transition

Implications for foreign investors

In an era of historic political transformation-and considerable uncertainty—Myanmar’s investment environment continues to evolve. This bulletin sets out what investors need to know about the status of the transition to democracy, the legislative achievements of the previous government and the challenges facing the new administration.
1 An NLD Landslide

Aung San Suu Kyi’s National League for Democracy (NLD) achieved a landslide victory in Myanmar’s general election on November 8th 2015, the country’s first free and fair national vote since civilian government was introduced in 2011. The NLD, which won approximately 80% of all contested seats, now controls parliament and on March 15th used its majority to elect a close ally of Ms Suu Kyi, Htin Kyaw, as president-the country’s first civilian leader in decades.1

The dramatic events of recent weeks underline the historic nature of political reform in Myanmar, bringing democracy to its 53m people. They also mark the next phase in an already remarkable period of opening of the country to foreign investment since 2012, when a new foreign investment law was passed.

Though there is uncertainty about the transition of power, Myanmar remains one of the world’s most interesting commercial opportunities. Foreign direct investment (FDI) rose to USD8.1bn in the fiscal year ending March 2015, double the 2013/2014 figure and USD3bn more than the government had initially targeted.2 Considering that the country’s most comparable Asian competitor for new investment-Vietnam-reported record FDI of USD22.8bn in calendar 2015,3 there is plenty of scope for inward inflows of capital to keep growing.

The issues facing prospective investors—political, legal and practical—are complex, but navigable. Entry as a foreign investor has the support of a developing legal framework, and this is strengthening over time. The previous government, under President Thein Sein and the military-backed Union Solidarity and Development Party, created and passed a raft of laws crucial to improving the investment environment and attracting foreign capital into the country (examined in Part 2).

That said, the legal framework for foreign investment, while no longer nascent, is still in its infancy. Some of the previous government’s laws are under revision; others have only just been introduced and their effectiveness is so far untested. Moreover, how the new government and the bureaucracies will interpret these laws is still open to question.

A delicate transition

The political transition is delicate since the NLD, seeking to deploy the levers of power effectively following nearly 50 years of military rule, must deal with practical challenges, such as ministerial appointments, before tackling the legislative agenda—which includes the passage of a revised investment law and a new companies laws (discussed in Part 3). Moreover, the NLD government faces massive expectations from the electorate regarding the delivery of reform. Political tensions could rise if it finds the realities of government hindering its ambitious reform plans. The NLD could also face rising opposition if it is unable to communicate its policies, priorities and targets clearly to the public.

It is also important to remember that the military is still a factor in government, despite the NLD’s absolute majority. Under the military-drafted constitution, unelected military representatives take up 25% of the seats in parliament and have an effective veto over constitutional change (which requires a greater than 75% majority). The army retains control of the ministries of defence, home affairs and border affairs, which in effect keeps it in charge of the nation’s international security and local administration. In addition, Myint Swe, a presidential candidate nominated by the military who came second to Htin Kyaw, will serve as one of the country’s two vice presidents. (Another NLD candidate, Henry Van Thio, will be the other vice president.)

That said, the transition period has so far gone smoothly, a national palliative for Myanmar citizens who recall the failed transition of 1990, when the NLD won a similar mandate in a general election but was prevented by the military from taking power. Along with enjoying tremendous popular support, politicians in the NLD are used to working together, having endured years on the periphery under military rule. They are conscious of their mandate and likely to tackle legislative problems constructively.

1. Though Ms Suu Kyi was barred from standing for president due to a clause in the constitution that prohibits anyone with foreign relatives from doing so (her children are British), she has said she will be “above the president” in the NLD hierarchy, retaining ultimate control over policy and decision making.
2_The Legislative Legacy

The parliamentary session that ended in January 2016 passed a raft of new legislation that underscores the nation's commitment to attracting responsible foreign investment and assisting such investment in key sectors. This was an extraordinary achievement of legal reform over a relatively short period. Still, in many cases the legislation leaves important details to be drafted by the ministries responsible. Some laws have vague language or overlapping definitions and are likely to face revision.

The following are some of the most notable achievements of the last parliament with relevance for foreign investors.

2.1_Arbitration Law

For foreign investors one of the most eagerly awaited new statutes was the Arbitration Law, enacted on January 5th 2016. This stipulates that a foreign arbitral decision must be recognised and enforced in Myanmar, unless limited grounds for refusal apply. The new legislation repeals a previous law enacted in 1944 and puts the Recognition and Enforcement of Foreign Arbitral Awards, known as the New York Convention, into force in domestic law. Many provisions of the new legislation are based on the United Nations Commission on International Trade Law's model law for international commercial arbitration, in which parties in an international arbitration are able to select the substantive law of the arbitration-for example, that of the UK, Singapore or Myanmar. The law encompasses both international and domestic arbitrations, although domestic cases are required to apply Myanmar law. There is also a clear distinction between domestic arbitration, to which the whole of the law applies, and foreign arbitration (i.e. where the place of arbitration is outside Myanmar), to which only select provisions apply. The Myanmar courts' interpretation of the provisions of the new legislation will emerge as test cases come before the Supreme Court.

The enactment of this law was the driver for Global Arbitration Review, in its annual GAR Awards on March 2nd 2016, naming Myanmar as the jurisdiction that has made the greatest progress in the past year.

2.2_Amended Mining Law

The parliament passed an amended version of Myanmar's Mining Law of 1994 on December 24th 2015. The most important amendments change the old law's production sharing stipulations, which had required mining companies to transfer up to 30% of output to the government. Now the law provides a mechanism for the state to opt for an equity interest in projects. However, the details of the mechanism have yet to be clarified, as implementing rules are still being written. The government still retains the right to participate in any project, whether through an equity partnership, production sharing or some other structure.

The amendments also increase the maximum production permit period for large-scale extraction and production to 50 years, and offer specific criteria to determine the size of individual production areas. They allow joint ventures between foreign investors and local investors for large-scale projects (as a means to encourage the upgrade of local small or mid-size projects). They uphold the priority right of mining companies with an exploration permit on a given project to gain a production permit for that project.

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4. For instance, the new Public Debt Management Law contains different definitions of public debt and leaves unclear whether it applies only to straight-up borrowing or also bond issuance and guarantees of contractual obligations.

2.3_Condominium Law

The Condominium Law, enacted on January 29th 2016, is also a major step toward opening the door to foreign investment that still requires clarification in specific areas. The law, which allows foreign ownership of up to 40% of residential units, gives broader residential ownership rights than the old legislation had stipulated: under previous laws, owners had contractual rights against the owner of the land on which the residence was built, but no actual title to individual units.

One unspecified element to the new law, still needing clarification, is whether the definition of “foreigners” includes the right of foreign corporations to own, lease or mortgage a residential unit. It has other areas of ambiguity that reveal a gap between the legal ideal and the reality of current code and practice. For instance, the law gives collective ownership of the land on which a residence is built to the owners, but overlooks the simple fact that in Myanmar residents cannot own land, but only lease it—a legacy of the nation’s socialist past. The contradiction will be settled either by legislative revision or in the courts.  


2.4_Banks and Financial Institutions Law

The parliament passed the Banks and Financial Institutions Law on January 28th 2016, laying out a wide range of guidelines for commercial, state-owned, private and foreign banks, and providing rules for non-bank financial institutions. This replaces a law covering banks passed in 1990, which provided only general rules for local financial institutions. The new law applies international standards on compliance, such as the capital adequacy and anti-money laundering provisions of the Basel III Accords, to banks operating locally.

The law, one of the better-drafted pieces of recently passed legislation, provides a more robust framework for foreign financial institutions seeking entry in Myanmar. A first round of foreign-bank licensing took place in 2014, when nine banks from Australia, Japan, Malaysia, China, Singapore and Thailand were awarded licenses. The government announced a second round on March 4th this year, granting licenses to the Bank of Investment and Development of Vietnam, the State Bank of India, E.Sun Commercial Bank of Taiwan and Shinhan Bank of South Korea.

While these licenses retain highly restrictive provisions on what services their holders can offer in the country, the entry of foreign institutions is an important step toward liberalisation of the sector.

3.1_A Large To-do List

Several pieces of legislation crucial to improving the investment environment have yet to be enacted and must be tackled by the new government—alongside its plans to reform the bureaucracy.

3.1_Revised Foreign Investment Law

Myanmar’s Foreign Investment Law, passed in 2012, opened up many new sectors to investment, including human resource development, infrastructure (utilities, roads and highways), banking and finance, high technology, and communications. The new law allowed any investment to be up to 100% foreign-owned and for overseas companies to fully own joint ventures.

The previous government took the reform of investment law into a new phase, revising the 2012 statute and merging it with the Myanmar Citizens Investment Law, with the aim of providing a single code that does not distinguish between domestic and foreign investors. The new law will be presented to the new parliament this year, although its swift passage is far from guaranteed.

The revision of the 2012 law includes important features for foreign investors, treating them like domestic investors with respect to establishing companies, buying companies, expanding within Myanmar or across borders and in managing and hiring. With the exception of investments in sensitive sectors, any investor—foreign or domestic—will (in theory) be able to invest in any enterprise in any sector, although until such time as new regulations are passed, the old regulations (with some restrictions) with remain in force. The new Foreign Investment Law also changes the remit of the Myanmar Investment Commission (MIC), the gateway agency for foreign investment, granting it expanded oversight powers as an autonomous agency with perpetual succession.

Key to the revision of the 2012 law are measures concerning employment, allowing any investor to hire qualified workers of any nationality to fill senior management, technical and advisory positions. There will no longer be a quota for local skilled labour. The draft also introduced rules covering the transfer of funds out of Myanmar for investors and expatriate employees with work permits. The consolidated draft new law retains the provision allowing foreign investors to obtain 50-year land leases that can be extended for two ten-year periods.

3.2_Companies Act

The new Companies Act will also be put before the parliament this year. The Myanmar Directorate of Investment and Company Administration (DICA) circulated a briefing paper last year that said the new law would be based largely on corporate law regimes in other common law states, such as Singapore, the UK and Australia. Until now, few guidelines have existed for companies to follow on incorporation and administration, and procedures have been done on a case-by-case basis under the oversight of the applicable government agency. The proposed legislation introduces guidelines, including clarification of company registration requirements and improving registration procedures, modernising the management.

In pursuit of better corporate governance the law also includes rules that explicitly state directors’ duties, detail financial reporting and audit requirements, provide minority shareholder protection and establish boundaries for transactions between related parties. Under the proposed law, DICA becomes the regulator with role of auditing companies, although the effectiveness of its enforcement capabilities has yet to be tested.

3.3_Bureaucratic reform

The passages of these essential pieces of legislation are just two of the many challenges facing the new government. Handover issues are likely to command the NLD’s attention for at least several months into the new parliament.

In the meantime, the NLD is busy with ministerial succession, and has spoken of taking a broom to the existing bureaucracy, vowing to reduce the number of ministries from 36 to the low twenties and to require some civil servants to undergo additional job training. Following a meeting of the party’s central executive committee on the transition, the NLD announced on March 4th that half the new members of its new cabinet will be non-party intellectuals.

The ministerial shakeup suggests that the government is earnest about delivering on its reform mandate. How it will play out in reality is another matter. The NLD has said that it will not reduce the number of ministerial employees; rather it will assign employees from redundant ministries to those that need resources. The approach sounds unwieldy at best, and hardly suggests a decisive house-cleaning.

On the upside, though, the NLD has said it plans to retain senior members of the bureaucracy in their positions for the foreseeable future, a sign that it is serious about continuity in power and drawing on the knowledge of the previous administration-which shepherded through the first phase of the country’s remarkable legal and regulatory reform.

One caveat for the foreign investor, often forgotten in the excitement of Myanmar’s rapid political evolution, is that US sanctions are still in place and remain an impediment to foreign investment. A substantial number of the big businesses operating in Myanmar are still blacklisted. The current US administration has been encouraging the big Myanmar groups to change, with the goal of removing them from the list. In December 2015, for example, the US eased sanctions by issuing six-month licences that permit US companies to ship goods and nonfinancial services in and out of Myanmar. Notably, this allows US companies to ship goods in and out of Yangon’s port, which is owned by a blacklisted company.\(^{10}\)

Whether this calibrated easing will persist largely depends on the outcome of the November elections in the US. For the time being, investors should ensure that business activities, or those of their business partners, do not violate US sanctions, even as a host of new opportunities arises in Myanmar.

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embrace attracting FDI as an imperative because it will help grow the economy and deliver on its campaign promises. The sectors of immediate interest in which it would like to show results are in infrastructure development and telecommunications, particularly mobile banking, and in power generation. Myanmar’s Telecommunications Law was passed three years ago, and consequently this sector has had greatest legal activity supporting foreign investment, following several acquisitions and major lending from multilateral institutions and commercial banks.

Another unknown is the how the NLD’s relationship with existing big businesses in Myanmar—those that had links with the military government—will develop. The common assumption that the NLD would resent these businesses as cronies of the military no longer necessarily applies. In fact, the party has cultivated closer links with them in the past three or four years, as they have started to provide it with financial support. An accommodation between the two sides has been forming—although it is never likely to be as close a relationship as that between the businesses and the former government.

As for the businesses themselves, some will be open to the government’s agenda to attract investment, while others could equally respond by urging a slowdown, using the familiar argument that essential industries need protection against foreign competition until they are strong enough to survive it. It is impossible to tell now how the government might respond to this kind of pressure.

In the current environment, then, the reform agenda that prioritises the opening of the country to foreign investment has a firm foundation and considerable momentum, but in a practical sense much is up in the air. How should foreign investors with an interest in Myanmar approach a situation in flux?

One important step is to maintain engagement. The government is likely to retain technocrats that favoured an expansion of foreign investment: that suggests a window is open now to cultivate relationships with those ministers or senior bureaucrats in the ministries, as it is likely that businesses will continue to deal with the same individuals. Making contact now could give an advantage over competitors that come in later.

Senior bureaucrats have in fact been willing to meet foreign investors and approach the meetings in a professional way—an outgrowth of the proactive leadership of the MIC. It is easy enough to get access via embassies or professional contacts. The latter, however, comes with a caveat: it is important to understand who you go with. In the changing political atmosphere it is easy to become tainted by association (i.e. with people who may have been commercially affiliated with the previous administration). On-the-ground guidance from an experienced advisor is invaluable here.

Myanmar has managed its remarkable transition so far without substantial setbacks. Indeed, progress in legal reform has moved forward at impressive speed. It is to be expected now, as the new government takes power, that the pace will slow as new ministers find their feet and the government refines its approach to economic policy. But the environment is broadly conducive to foreign investment already, and there an urgent need for investment in crucial areas, such as infrastructure. Companies with a strategy to expand in emerging markets have a strong incentive to take advantage of this exciting period of transition by coming to Myanmar now and building their businesses.
Allen&Overy’s on-the-ground presence and track record in Myanmar

We were the first international firm to establish a Yangon office in 2013. The office is led by Simon Makinson and supported by our on-the-ground legal and Myanmar national support team. We have advised and are advising on a number of on-going high profile projects in the Myanmar market for clients that are looking to enter, or have entered, the market.

We are advising clients across all active sectors including telecoms, banking and finance, energy including oil and gas, infrastructure, manufacturing and consumer goods. In addition to our on-deal experience, our engagement in Myanmar includes spending significant time and resources assisting with efforts to build capacity and up skill key stakeholders within the private and public sector and to encourage responsible investment. We regularly engage with the Myanmar government and spend a lot of time in the capital, Nay Pyi Taw, meeting with, and delivering seminars to, government officials and ministries including the Attorney General’s office, the Myanmar Investment Commission and the Directorate of Investment and Company Administration.

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