

Creating Enabling Environment for Micro-finance Sector Development in Vietnam: A Legal Framework Perspective

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ABSTRACT There is a long standing consensus in most developing countries that micro-finance is an important tool to reduce poverty. With the majority of people in developing countries such as Vietnam living in rural areas, the conventional wisdom is that micro-finance institutions can be utilized to direct resources to poor rural communities. It is argued that the poor lack access to financial resources and therefore, one crucial strategy for achieving pro-poor growth and poverty reduction goals is to increase the role of Micro-Finance Institutions (MFIs). However, developmental economists have long noted the complexity of MFIs providing effective rural credit delivery system without a vibrant legal framework that creates an enabling environment. Given that MFIs seek to reduce poverty in rural areas through providing sustainable micro-finance facilities, it is unfortunate that the important role played by a legal framework has largely been neglected by researchers. Using Vietnam as a case study, this research seeks to examine the legal framework governing the activities of MFIs in Vietnam, present the shortcomings of the legal framework and then suggest some legal framework reforms needed. The understanding is that, a reformed legal framework will facilitate a rapid development of MFIs in Vietnam and consequently alleviate rural poverty.

INTRODUCTION

There is a long standing consensus in most developing countries that micro-finance is an important tool in combating poverty (Roy and Chowdhury 2009). With the majority of the population in developing countries living in rural areas (Tsai 2004; Sievers and Vandenberg 2007; Chinomona and Tam 2013), the conventional wisdom is that micro-finance programs are an important health intervention tool, and an efficient and equitable tool for directing resources to rural communities (Mwenda and Muuka 2004; Baumann 2001). The genesis of this argument is that the poor lack access to financial services, credit, and savings facilities (Schreiner 2001; Weiss et al. 2003). The little or non-existence of effective financial services in rural areas affects people in many ways and therefore, one crucial strategy for achieving pro-poor growth and poverty reduction goals is to increase and improve the role of Micro-Finance Institutions (Ahmed et al. 2001; Chinomona and Tam 2013). Yet as Onumah (2003) points out, promoting efficient, sustainable and widely accessible rural financial

systems remains a major development challenge in most developing countries. Developmental economists have long noted the complexity of MFIs providing effective rural credit delivery system without a vibrant government policy or legal framework that provide an enabling environment (Chaudhur 2001; Chinomona and Tam 2013).

Notwithstanding the importance of the role played by a legal framework with regard to supporting the rapid development and effective operation of the microfinance sector in developing countries such as Vietnam, little research has been done on this matter. Previous academic studies have largely focused on microfinance institutions (MFIs) and women empowerment (Baumann 2001), the role of MFIs in agrarian communities, the operations of MFIs agents in rural areas (Armendáriz de Aghion and Morduch 2005), the volume of MFIs in Asia (Weiss et al. 2003) and a global survey of MFIs (McKim and Hugart 2005), a survey of MFIs in Vietnam (McCarty 2001), among others. Given that the main goal of MFIs in rural areas, is to provide sustainable micro-finance facilities to the poor in order to facilitate income generation and reduce poverty (Baumann 2001; Chinomona and Tam 2013) it is unfortunate that the important role played by government policy on the legal framework governing the development of the microfinance sector – in particular, the establishment and opera-

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tions of MFIs, has largely been neglected by researchers. While quite a lot has been written about commercial credit institutions in Vietnam (Barslund and Tarp 2008) there is only a very limited academic literature available on the obstacles faced by MFIs in the rural Vietnam as a result of the legal framework inadequacies, and in particular, the government policies needed to make MFIs effective tools for combating rural poverty. To the best knowledge of the authors, not a single objective academic paper has been written specifically targeting the legal framework guiding the MFIs in Vietnam.

Objectives of the Study

Against this backdrop and in order to fill this void, the main purpose of this research is three-fold. Firstly, the current study will seek to provide a background view of Vietnamese government policies with special attention to the legal framework on the transformation of Vietnamese rural communities which are largely agrarian in nature since 1988 and its support for micro-finance sector development in the country. Secondly, in light of the obstacles hampering the establishment and effective operation of MFIs in rural Vietnam, the shortcomings of the existing legal framework will be examined. Finally, some recommendations targeted at reforming the legal framework currently governing the development and operations of MFIs in Vietnam are suggested. It is the contention of the researchers that such policy prescriptions will go a long way to remedy the obstacles faced by MFIs and hence alleviate rural poverty in Vietnam. To achieve these objectives this paper will therefore be divided into four parts. The first part will provide a historical background to Vietnam – particularly the transformation of the rural agrarian communities and government support to these poor communities. The second part will explore the current legal framework governing the microfinance sector in Vietnam, and then a section on the shortcomings of the existing legal framework will be provided thereafter. The fourth part will provide some policy suggestions aimed at reforming the current legal framework. Finally, this paper will crown up by giving a conclusion to this study.

METHODOLOGY

A case study approach was utilized in this research in order to achieve the empirical objec-

tives of the study. As cited by Chinomona and Sibanda (2013), a case study is an empirical enquiry that investigates a contemporary phenomenon within its real-life context, especially when the boundaries between phenomenon and context are not clearly evident and it relies on multiple sources of evidence. It investigates pre-defined phenomena and does not involve explicit control or manipulation of variables but rather the focus is on in-depth understanding of a phenomenon and its context.

In this study, the data collection technique encompassed combining interviews, observation, questionnaires, and document and text analysis. First, this study employed an interpretative, qualitative methodology to examine the micro-financing process and regulatory framework in Vietnam. In this case, multiple cases were utilized to achieve this purpose. Second, owing to the limitations of relying on one source of information when collecting data on case studies, the study adopted data triangulation approach whereby, field researches that involve investigating the views and opinions of organizations directly and indirectly involved in the decision-making process by means of interviews, observations or otherwise were used.

According to Palmer and Quinn (2003), data triangulation refers to the use of multiple sources of data. Chinomona and Tam (2013) notes that, multiple and independent sources of evidence, including observations, interviews and document exploitation such as use of government policy documents. In this study observations and document exploitation were used to corroborate the interview data and, by so doing, developed convergent lines of inquiry.

The researchers managed to conduct the interviews while at the same time taking short notes for future coding. The general observation was that each interview would trigger the necessity for another interview as the themes began to unfold. The convergent in-depth interviewing used in this study allowed the researcher to develop, clarify, verify and refine the core issues of the interview protocol. In this regard, both structured and unstructured questionnaires were used.

Unlike in quantitative research, qualitative research views literature review as an ongoing process and serve as a source of data (Goldkuhl and Cronholm 2003; Glaser and Strauss 1967). As put forward by Turner (1983), literature from documented material should be viewed equally

the same as field notes. The same point was buttressed by Glacer (1998, 1992) who referred to documented literature as “everything is data” and Strauss and Corbin (1990) who asserted that a “cache of archival material” is equivalent to a collection of interviews and field notes. In this article the researchers reviewed documents with literature on both formal and semi-formal micro-finance regulatory framework in Vietnam. These documents served two purposes. Firstly, they were treated as another source of data collection. Secondly, as noted by Goldkuhl and Cronholm (2003), prior reading provided models to help the researcher make sense of the data gathered on the legal framework aspects of micro-financing institutions in Vietnam.

In this study, data collection and analysis were done simultaneously. Data analysis involved categorizing and triangulating the evidence from the multiple perspectives. Based on the field findings, the depth of MFI legal framework in Vietnam was deduced. The remainder of the paper now reports the findings from the in-depth interviews, document exploitation and observations made. For confidentiality reasons, the identities of respondents will not be disclosed in subsequent sections. The next section will provide a discussion of the MFIs legal framework Vietnam and the identified shortcomings. A conclusion and suggested recommendations will crown up the current study.

OBSERVATIONS AND DISCUSSION

An Overview of Vietnam's Agrarian Rural Areas

With a population of around 86 million people, nearly 70% of the Vietnamese population lives in rural areas (Barslund and Tarp 2008). Of this 70% rural population, 13.7 million households are rural agricultural communities as of 2007 records (General Statistics Office 2008). Furthermore, about 1.6 million of these households were reported to be in business and therefore, accounting for nearly 50% of the total households doing business countrywide (Barslund and Tarp 2008). The average income per head for the rural households in Vietnam is VND 6.1 million per annum (General Statistics Office 2010). In comparison with the national average income per capita, these households' incomes are still below the poverty datum line

(Asia Development Bank 2010). According to the figures released by the General Statistics Office on December, 31st, 2007, Vietnam had about 3 millions of its people at the starvation risk level (General Statistics Office 2007). Moreover, also when compared to the households dwelling in urban areas, the rural households living standards are well below their urban counterparts (Nguyen 2004; McCarty 2001).

However, after 15 years of implementing the Poverty Alleviation program and 7 years of executing social-economic development in extremely disadvantaged communes and the ethnic minority households programme (Programme 135), poverty rate in the poor households fell from 58 percent in 1993 to 13.1 percent by 2008 (General Statistics Office 2010). The GDP per capita also increased rapidly, from below USD 200 in 1993 to up to USD 1024 by 2008 (Asia Development Bank 2010). The current endeavor by the Vietnamese Government is to reduce poverty rate in poor households to below 11 percent. In spite of these great achievements by the Vietnamese government to reduce the levels of poverty in the country in general, high levels of rural poverty have remained a challenge and of major concern.

The Legal Framework Guiding the Transformation of the Agrarian Rural Communities in Vietnam

The transformation and recognition of a household as a self-control economic unit in the agrarian rural Vietnam can be traced back to 1988 after the promulgation of Resolution No. 10 of April 5, 1988. The resolution recognized a household as a unit to target for development and combating rural poverty. This was followed by the Land Law of 1993 which was coupled with a wide range of credit policies on providing loans to rural households. In 1995 more government policies were implemented to promote the creation of public and private micro-credit. The Law of Cooperatives of 1996 as amended in 2003 (Decree No. 88/CP on Associations and Unions) provided the much needed legal framework that empowered cooperatives such as the People's Credit Fund to act as economic tools that provide microfinance in rural areas.

As from 2005 to 2009, the legal framework (for example, Decree No.28/2005/ND-CP and Decree No.165/2007/ND-CP) aimed at regulat-

ing the establishment and operations of microfinance institutions was formulated. These laws were epitomized in Decree No.41/2010/ND-CP of April 12th 2010 which proffered an opportunity for informal organizations to transform themselves into formal microfinance institutions that operate professionally and in order to offer microfinance services efficiently and effectively to the rural communities in Vietnam.

Government Support for MFIS Activities in Vietnam

When compared to other sectors, it is extremely difficult for the microfinance sector in Vietnam to develop professionally and efficiently without some supportive government policies. The government of Vietnam has encouraged credit provision to rural regions through regulating policies such as streamlining procedures related to mobilizing capital and lending to rural areas, erasing financial policies that discriminated between customers in state-owned and non-state-owned sectors, applying policies with flexible and suitable interest rate to attract deposits and loans and gradually reducing preferential loans in order to direct financial resources toward the poverty stricken rural communities.

By and large, in recognition of the important role played by microfinance institution on poverty alleviation in rural communities, the Government of Vietnam directly undertook to develop this sector by for instance, subsidizing rural credit and supporting financial intermediaries providing micro-credit to the rural poor communities. Key institutions used by the Government of Vietnam for this purpose were the Vietnam Bank for Agriculture and Rural Development (VBARD), Vietnam Bank for Social Policies (VBSP), and People's Credit Fund (PCF). To date, these credit institutions have come to cover more than 95% of credit market in agrarian rural communities of Vietnam. VBARD which is state-owned has the largest network nationwide and with 2,096 branches. Because of its large network base, it has managed to channel government subsidized loans to a large pool of poor rural households operating small businesses. VBSP which is ranked the second largest micro-credit institution in Asia, currently operates 63 provincial branches, 612 transaction offices in districts, 8,495 communal mobile transaction points, and manages 239,647 savings and

lending groups with more than 8,000 staffs that provide preferential credit to the poor rural households in Vietnam. PCF has 1037 local staff members operating at grassroots level among the rural agrarian communities in Vietnam.

Besides, the direct microfinance support rendered to the rural poor by the Vietnamese Government, it has also encouraged the active mass participation of Non-Governmental Organizations (NGOs) such as Labor Union, Farmers' Association, Veteran's Union, Vietnam Women's Union (VWU) etc., in microfinance activities. According to a survey report of 30 provinces, VWU manages 557 programs/projects with a capital base of Vietnamese currency (VND) 244.2 billion and 172,089 participating membership. In addition to local NGOs microfinance activities, international development agencies from countries such as Sweden (Swedish International Development Agency), and international development organizations such as United Nations Development Programme (UNDP), United Nations Population Fund (UNPF), United Nations International Children's Fund (UNICEF) and the international non-governmental organizations (INGOs) also now coordinate microfinance projects targeted at benefiting the poor and combating rural poverty. Among INGOs implementing microfinance projects with more than 10 000 members in rural communities are Save the Children Fund (SCF) and Action Aid Vietnam (AAV).

The Legal Framework Regulating Credit Institutions and MFIS in Vietnam

The network providing microfinance products in Vietnam can be divided into three sectors, that is, official sector, semi-official sector, and unofficial sector. As a result of this, each sector has a different legal framework and policies regulating its operations despite serving a common group of customers – the poor rural communities. The official sector includes credit institutions which provide microfinance services, and small-scale financial institutions which specialize on providing microfinance services. This sector comprise of financial institutions such as the State Bank of Vietnam (SBV), Vietnam Bank for Social Policy (VBSP), and People's Credit Fund. The State Bank of Vietnam is tasked with issuing licenses or permits and supervising institutions belonging to this sector in order to ensure that the credit institutions maintain the best in-

ternational practice standards. The supreme legal document governing credit institution in Vietnam is the Law on Credit Institutions dated 12/12/1997 and its amendment and adjustment dated 15/6/2004. Under the law is the system of Decrees and Circulars guiding the organization and operation of credit institutions such as commercial banks. There are no specific regulations for microfinance activities, and therefore, commercial banks conduct microfinance activities based on the framework of regulations applied to traditional banking activities.

Vietnam Banks for Social Policies (VBSP) which was established under the Premier's Decision No. 131/2002/QĐ-TTĐ of October, 4, 2002, is a non-profit bank implementing lending policies and microfinance intended to benefit the poor people and other beneficiaries. The Prime Minister makes specific decisions and guidance for the organization and operations of this bank. The Ministry of Finance promulgates financial management mechanism, including risk provisioning and the SBV only issues guidance on operations.

The People's Credit Funds (PCF) is regulated by the Cooperative Law of 2003 and the Law on Credit Institutions. The system of People's Credit Funds is managed and supervised by SBV and operate based on a relatively sufficient and unified system of guiding documents (that is, Decrees and Circulars) which are developed under the State Bank of Vietnam (SBV) coordination. Such legal documents facilitate more favorable, autonomous and safer operation for People's Credit Funds (PCF).

With regard to the legal framework regulating the microfinance programs in semi-formal sector, there are two basic legal documents on the supervision, organization and operations of MFIs in Vietnam, namely the Decree No. 28/2005/ND-CP dated 09/03/2005 and the Decree No. 165/2007/ND-CP dated 15/11/2007 amending and supplementing some articles of Decree No. 28/2005/ND-CP. The promulgation of this separate Decree for microfinance has marked a significant milestone in the evolution of microfinance activities in Vietnam, affirming the Vietnamese Government's recognition of the role and importance of microfinance activities in the national finance banking system.

Following the above Decree, on 2/4/2008, the State Bank Governor issued a Circular No. 02/2008/TT-NHNN guiding the implementation of

some contents of the Decree and primarily focusing on conditions, process, licensing procedures, ownership structure, management, surveillance and control over MFIs operation (hereinafter referred to as Circular). Under the provisions of the Circular, MFIs are established under two forms, that is, MFIs in the form of one-member limited company, that is organized and owned by a mass organization; and MFIs under the form of two or more members limited companies. In the later case, at least one investor member must be a mass organization, a social organization, a professional organization, a charity, social fund, or a non-governmental organization (NGO) in Vietnam conducting sustainable microfinance activities in Vietnam.

The Circular also specifies regulations for cases in which no dossiers of application are submitted or submitted but failed to be licensed, or organizations conducting microfinance activities but are asked to limit their operational scale. For instance, such microfinance organizations are not permitted to take voluntary deposits from organizations and individuals who are not their microfinance clients. Furthermore, the total savings mobilized from their microfinance clients is limited to less than 50% of equity, and that they are required to deposit all the money from voluntary microfinance savings to one bank and can withdraw it only to return such savings to their clients (that is, using savings to lend out is not allowed).

The semi-official sector consists of mass organizations, domestic and international NGOs, programs and projects that provide microfinance services. The licensing and management of microfinance activities of this semi-official sector is done by different agencies depending on the type of the organization participating in the provision of the microfinance services. For example, mass organizations conduct micro-credit and savings activities based on what is approved by the Prime Minister. The management and supervision of such mass organizations' microfinance operations are conducted at four levels of governance, that is, central, provincial, district and commune/ward levels. At local level, the local People's Committees partake in the management and supervision of mass organizations operating in their local jurisdiction under specific guidelines from SBV or as directed by the Prime Minister.

On one hand, the operations of foreign NGOs participating in microfinance in Vietnam are

regulated by the Prime Minister's Decision No.340-TTg dated May 24, 1996. According to this regulation, the Committee for Foreign NGO Affairs is the licensing authority. Ministries, Agencies and provincial People Committees take responsibilities for instructing, supporting and controlling the execution of the regulations. On the other hand, the operations of domestic NGOs are regulated by Governmental Decree No.88/2003/ND-CP dated July 30, of 2003. Under the Decree, the Ministry of Home Affairs has the overall authority over license issuance to all inter-provincial associations and unions operating within Vietnam. However, while the Ministry of Home Affairs on behalf of the Government of Vietnam reserves the right to manage domestic associations and unions nationwide, the provincial People Committees are mandated to issue licenses to associations and unions operating at provincial or local level.

Informal sectors include lending activities agreed among individuals. Prior to 2006, the operations of the informal sector were not legally permitted. However, in November 2006, the Vietnamese Government promulgated Decree No. 144/2006/ND-CP on rotating savings and credit associations (ROSCAs). Among others, this decree stipulated that *in case of dispute arising, it shall be addressed in compliance with the Law of Civil Procedure*. The interest rates that MFIs in Vietnam charge are regulated by law. The Civil law sets a ceiling lending rate for all transactions to clients at 15% of the basic rate released by the SBV for respective loan products. The current basic lending rate of SBV in Vietnam is 8% per annum as of December 2009.

The Shortcomings of MFIS Legal Framework in Vietnam

Notwithstanding the tremendous achievements realized on the improvement of the legal framework targeted at fostering the development of the microfinance sector and enhance the MFIs operations in Vietnam, it is not without shortcomings.

First, the maximum lending rate imposed by the Government of Vietnam through the law on basic lending rate, is not sustainable for most MFIs operating in rural Vietnam. At present, the basic lending rate of SBV is 8% per annum and therefore the maximum lending rate is 12% per annum for MFIs. This rate is very low even when

compared to the lending rates of the most successful MFIs in foreign countries. Given that the microfinance clients in rural Vietnam have low income and are without collateral security, regulating the ceiling lending rate at low levels has posed a serious long term viability and sustainability challenge to most MFIs in rural Vietnam. To remain viable and be sustainable in the long term, research findings in Vietnam indicate that the MFIs need to charge an actual lending rate of between 20-25% per annum.

Second, while the Vietnamese Government's preferential policy to charge very low lending rates to targeted policy-based beneficiaries being implemented by the Vietnam Bank for Social Policies is commendable as a strategy to reduce poverty in rural Vietnam, this policy has also negatively affected the development of the microfinance market. For instance, it has affected the competitiveness and growth of other MFIs, discouraged other new microfinance providers from participating in the market, and causing psychological dependence syndrome of rural clients to rely on government subsidiaries for poor households.

Third, the interest subsidy policy granted to VBSP (Vietnam bank of Social Policy) has made it expand its network nationwide despite its difficulties to mobilize deposits at the prevailing market rate on its own. VBSP is state financed. Other MFIs cannot emulate VBSP since they are likely to make losses and consequently become insolvent. Due to this unlevelled playing field, the privately owned MFIs have found it difficult to compete with government subsidized institutions in microfinance business.

Fourth, in order to mobilize capital from its customers so as to stay afloat, semi-formal MFIs require compulsory savings from their clients. However, the savings amount is subject to regulation by the government. The approved savings rate is between 1-5% of the loan or the contribution should be a monthly absolute value of Vietnamese currency (VND) 3-10 thousand. However, this only constitute about 21.4% of the total capital source and is very low when compares to other developing Asian countries such as Bangladesh, the Philippines and Nepal that have 40%, 14%, and 12% respectively as compulsory savings rates for their clients. Compulsory savings are very essential to the long term survival of Micro Finance Institutions (MFIs) since it promote a saving habit among clients and cushion

the MFIs against risks associated with lending to the poor clients without collateral security.

Fifth, the current law on MFIs in Vietnam only allows microfinance institutions to exist under the legal form of a limited company which has strict restrictions and requirements. For example, the number of participants in any MFI is limited by law. Furthermore, the MFIs cannot choose a legal form of their choice just like other businesses. Thus, it is difficult to expand the scale of operation when their ability of increasing capital is somehow limited by law. For instance, MFIs cannot be publicly listed companies and therefore, cannot raise capital from the stock market, but can only increase the initial capital by retained earnings or by additional contributions from members. Such a limitation is handicapping the potential of MFIs development in Vietnam.

Legal Framework Reform, Government Measures and Policy Prescriptions

The Government of Vietnam has acknowledged the development of microfinance institutions as a leading strategy for its poverty eradication programs. The goal is to utilize MFIs as tools to channel the much needed financial resources to rural and poor communities in order to combat rampant poverty in the country. In this regard, the government policies – particularly the legal framework that guide the development of MFIs sector is paramount and central to the Vietnamese government’s approach to achieve poverty reduction in rural communities. In full view of the shortcomings of the MFIs legal framework aforementioned, it is imperative that the Government of Vietnam considers reforms on policies governing this sector. In particular, the Government of Vietnam needs to consider diversifying some policies governing the legal form of MFIs, *simplifying the procedures for establishing and reorganizing MFIs and modifying provisions governing the internal operations of MFIs.*

Diversifying Legal Form of Microfinance Institutions

Creating a standardized legal framework that is more conducive for the development and effective operation of MFIs in Vietnam is essential and urgent. The research paper recommends the rationalization of the current existing laws on MFIs as follows:

First, Amending “hard” regulations on legal form of the current MFIs in order to allow them to select a form and model of operation of their own choice is necessary, for example, the freedom to choose whether to be a limited company or joint-stock company. This amendment is reasonable because it will allow MFIs to have a chance to select a model of doing business of their own that is in accordance to their needs and vision. This means that if the MFIs want to limit the participation of investors they can choose to be a limited company and if so they choose to increase their financial strength and soundness by inviting the participation of many investors, they should be allowed to freely choose the joint-stock model. Furthermore, the recognition of various legal forms of MFIs will be consistent with other laws regulating business enterprises in general and credit institutions in particular. The current laws governing business enterprises in Vietnam allows them to operate under different legal forms. For instance the law on banking allows credit institutions to trade as limited or joint-stock companies. The researchers find no convincing scientific basis for the Government of Vietnam to allow other business enterprises to choose a legal form of their choice while at the same time barring the MFIs to do the same. More so, with the mechanism of internal management in MFIs now regulated by Circular No.02 – which calls for the separation of executive functions and management functions of owners, this makes the MFIs have a governance mechanism similar to that of a Joint Stock Company (Business Law 2005) rather than a limited company. Therefore, the Government of Vietnam seem to be inconsistent by restricting the legal form of MFIs to that of a limited company and yet requiring them to have a governance mechanism that is similar to that of a joint stock company.

Second, besides amending the regulation on legal form of MFIs, the Government of Vietnam should consider amending the current regulation that limit the number of MFIs members to five (5). The researchers believe that this amendment is necessary and reasonable because it also generate the consistency required among limited companies operating in different sectors of the economy. For instance, the Business Law of 2005 allows a limited company to have up to 50 members, and therefore, it appears not logically consistent to have only the MFIs of all companies registered as limited companies to be restricted

to 5 members. In addition, it is the contention of the researchers that the removal of this restriction will facilitate more business entities to participate in the microfinance sector. Perhaps the government's goal of reducing poverty in rural and poor community will be more likely achieved sustainably when large numbers of the members participate or invest in the microfinance sector.

Third, a change of a regulation on compulsory participation of mass organizations as prescribed in Point 3, Section I, Circular No.02 is recommended. Entities established as mass organizations are for charity and their sole existence is to help. The researchers think that it is not really necessary to have all MFIs registered under mass organization as a compulsory requirement. While MFIs can be utilized by the Government of Vietnam to implement its social policy and improve the lives of many poor communities, such a strategy should be sustainable in order to change the standard of living for the better for many Vietnamese in the long term. It is the contention of the researchers that in order for the MFIs to sustain their existence they need to make normal profit that enable them to develop and increase their scale capacity. One of the ways to achieve this is for the Government of Vietnam to reform this law restricting MFIs as mass organization such that interested major investors can invest in this sector and guide the executive management of the MFIs. This will likely keep the MFIs viable and profitable business entities.

Simplifying Procedures for Establishment and Reorganization of MFIs

By nature, a microfinance institution is a type of credit institution. The current regulation (Business Law of 2005) governing the registration process of other credit institutions such as joint stock commercial banks, financial companies, financial leasing companies, and so on, has two phases. However, the MFIs are currently established under the provision of Circular 02 despite being a form of credit institution. Furthermore, the requirements stated in Point 10.8 of Circular 02 that allows the State Bank of Vietnam to request additional information when necessary as part of the conditions for issuing MFIs with a license is very ambiguous and inconsistent with the Business Law of 2005 that regulate the registration process of other credit institutions afore-

mentioned. To avoid misunderstandings that arise when the State Bank of Vietnam request other unspecified documents as part of the requirement to register a microfinance institution, the researchers recommend the reconciliation of the current law on MFI registration (Point 10.8 of Circular 02) with the Business Law of 2005 that regulates the registration process of credit institutions in Vietnam. The amendment of Point 10.8 of Circular 02 is likely to ensure transparency and speeding up the registration process of MFIs once the applicants submit all the specified documents as required by the law.

Perhaps most of the issues pertaining to the registration process and re-organization of MFIs as stipulated in Circular 02 need to be amended. For instance issues raised in Point 9.2; 9.7; 9.8; and 10.4 of Circular 02 that touches on the involvement of "People's Committees". The researchers believe that while the aforementioned Points of Circular 02 might be necessary guiding conditions for institutions seeking to convert from microfinance programs or projects to MFIs, it is unreasonable to apply the same conditions or requirements to investors interested in establishing new MFIs. All in all, the provisions in Circular 02 regulating the establishment and re-organization of MFIs need to be reformed and reconciled with the Business Law of 2005. By so doing, Circular 02 will become simpler, transparent and consistent with the Business Law of 2005, considered to be the foundation for the existence of all types of business enterprises in Vietnam today.

Amendment of Some Provisions on Governance of MFIs in Vietnam

The conventional wisdom is that, the issue of good governance in any institution especially business entities, is paramount to its survival. Microfinance institutions are no exception to this. In this paper, the researchers argue that well crafted government policies and regulations promoting good governance mechanism are imperative to the survival, development and sustainability of MFIs in Vietnam.

In as far as the governance and administration of microfinance institutions are concerned, the MFIs in Vietnam have Board of Directors as intermediaries between Member Assembly (a body that represent the owners) and Directors/General Directors (a body representing the man-

agement of MFIs). However, this kind of arrangement does not apply to other limited business enterprises other than MFIs. This arrangement also applies to legal enterprises such as joint stock companies. The researchers are of the opinion that it is reasonable for the MFIs to be allowed to become joint stock companies given that they have similar governance model. In such an eventuality, the Member Assembly would become a General Shareholders Assembly. Such a legal framework reform is likely to reconcile and synchronize the existing different treatment given to limited companies operating in different sectors of the economy in Vietnam.

Perhaps too some sections of provisions on governance of MFIs need to be clearer and precise in order to reduce possibilities of confusion amounting from discretionary interpretation of the law. For instance, section 22 of Circular 02, stipulate that members of the Board of Directors (BODs), Board of Supervisors (BOS), General Director, Deputy General Directors, Head of Internal Audit and Chief Accountant of the MFIs are required to have “necessary skills, competence and capacity, experiences to conduct their rights and complete their tasks effectively”. It appears that this regulation might be open to a lot of discretionary interpretation since it lacks quantitative requirements. Terms used such as ‘necessary skills, competence, capacity, experiences to conduct rights and complete tasks’, are not defined or quantified and therefore are likely to be interpreted differently and cause confusion. Perhaps provisions such as these require to be more precise in as so far as to provide the level of education that is required or to set the criteria that should be used to measure skills or experience.

It might also be necessary for the Government of Vietnam to seriously consider a legal framework that improves the management, surveillance and policy making capacity of State authorities tasked with the granting of licenses, monitoring and supervision of MFIs. For instance, the State Bank of Vietnam can open specialized units or departments within its system, that are specifically responsible for offering professional advice or support and monitoring and supervision of MFIs under their jurisdiction. Perhaps this might be extended further to include the establishment of a microfinance council that is responsible for planning, developing strategies and policies and attending to problems related to micro-financ-

ing in the financial sector as a whole. Such a development can potential reduce the possibilities of MFIs becoming insolvent, besides aiding the MFIs to become more effective.

CONCLUSION

The received wisdom in most developing countries of Asia such as Vietnam is that, the majority of the poor households live in the rural and agricultural communities and therefore any consented effort to reduce poverty requires crafting strategies targeted at making these communities self sufficient by means of self-help projects or small businesses. A cross examination of the existing empirical studies and the current research findings indicate that lack of financial resources among others, is one of the obstacles incapacitating the poor rural and agricultural communities in Vietnam. One suggested strategy that has the greatest potential of uplifting the living standards of rural communities in Vietnam has been to increase the poor communities’ access to microfinance. Indeed, while microfinance business has improved the lives many in poor communities of Vietnam, the development of the microfinance sector has been quite a challenge. Among the various challenges incapacitating the rapid development of the microfinance institutions (MFIs) in Vietnam has been the issue of legal framework. In view of this identified obstacle, the purpose of this paper was to investigate the nature of the legal framework regulating the establishment, development, management and supervision of MFIs - with the intention of making policy prescriptions that might address the challenges faced by the microfinance sector in Vietnam.

RECOMMENDATIONS

In short, this study identified five main shortcomings related to the legal framework regulating MFIs in Vietnam. These are government imposition of interest rates through SBV, government policy on preferential treatment of credit institutions, subsidy policy, restrictions on compulsory savings and the legal form policy. In view of these identified legal framework deficiencies, the current study recommended three main reforms of the current legal framework. These are diversification of some policies governing the legal form of MFIs, *simplification of the proce-*

dures followed to establish or reorganize MFIs and the modification of provisions regulating the internal operations of MFIs. It is the view of the authors that if implemented, the legal framework reforms suggested by this study will go a long way in facilitating the rapid development of the microfinance sector in Vietnam and hence consequently reduce poverty through affording the poor rural communities access to the much needed financial resources that they require to support their self-help projects or small businesses.

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