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VIETNAMESE BOND FINANCING **COLLATERAL UNDER THE LENS**

In this article, we provide an insightful look at the critical solutions for dealing with diverse collateral difficulties and the dynamic techniques required to react to shifting collateral tactics.

1. Current Framework

In the complex world of finance, companies often resort to bond issuance as a mechanism for raising capital. These bonds constitute a form of debt financing, where the investors extend funds to a company in exchange for future repayment with interest. While this mechanism typically functions seamlessly in stable market environments, it can present complex issues during periods of stock market volatility, particularly in respect to the collateral securing these bonds.

In this context, collateral is an asset pledged by bond issuers as security for bond repayment. It's akin to using your home as collateral for a mortgage loan. If the bond issuer fails to meet its repayment commitments, the investors have the right to seize the collateral. Initially, bond issuers use stocks as collateral, either their own, those of subsidiaries, or those held by their shareholders. But what if the value of these stocks falls significantly? In such circumstances, the bond issuer must find other assets, such as real estate, to maintain the collateral's value.

2. Selection of Bondholders' Representative

Prior to the issuance of bonds, the bond issuers will appoint a representative for the bondholders. The representative is either a depository member of the Vietnam Securities Depository and Clearing Corporation (VSD) or a securities investment fund

management company. It's important that this representative shall not be too closely connected to the bond issuers. Also, they shall not be a guarantee for the bond issuer's payments, own the collateral, or be a significant shareholder or related person of the bond issuer. In cases where the bonds are backed by collateral, the representative assumes the role of receiving and managing the collateral and safeguarding the bondholders' interests by enforcing the collateral.

The handling of real estate as mortgage collateral is strictly regulated under Vietnamese legislation. In Vietnam, only regulated credit institutions are permitted to accept real estate as mortgage collateral from corporations. Banks, which are classed as credit institutions under the credit institution law, are thus legally authorized to handle real estate mortgages. Securities companies in Vietnam, on the other hand, are barred from obtaining this authorization because they are not recognized as credit institutions.

3. Collateral Management Entities: Securities Companies vs. Banks

Depending on the nature of the collateral, collateral is often managed by either a securities company or a bank. They play an important role in ensuring that bond issuers follow all of the rules and agreements relating to bond issuance. Securities companies are often selected for maintaining stock-based collateral due to their particular experience and regulatory framework. However, it is critical to understand that they are not authorized to manage real estate assets as collateral. This constraint derives from unique regulatory regulations as well as the specialized knowledge necessary in real estate management. Banks, on the other hand, have the legal power and operational competence to manage a broader range of collateral, including both stocks and real estate. Their legal standing and the full regulatory structure within which they operate facilitate this larger spectrum of capacity.

4. Solutions for Managing Different Types of Collateral

However, securities law provides a solution in situations where the bonds are publicly offered and the appointed representative is prohibited from receiving certain types of collateral due to specialized regulation. In such cases, the representative is required to appoint a third party to manage the collateral. There are two possible outcomes:

A. Representative Replacement:

The representative may consult with the bondholders to consider replacing the representative. Such a change necessitates the approval of at least 65% of the total outstanding bonds of the same type. It also requires amendments to various documents, including the agreement with the representative, the bond terms and conditions, and any other related documents. This process ensures a smooth transition

to a new representative who is capable and legally authorized to manage the collateral.

B. Appointing a Third Party:

Alternatively, the representative can continue to act as an intermediary amongst the bond issuer, bondholders, and other related parties, fulfilling all of their other responsibilities as outlined in the original agreement except for receiving and managing collateral. A third party would be appointed specifically for this purpose, ensuring that the collateral is managed by an organization or institution legally authorized and equipped to handle such responsibilities.

5. Adapting to Changes in Collateral Strategy

In the actual world of bond issuance, situations can arise where a bond issuer must adapt its collateral strategy, such as switching from stocks to real estate or adding real estate to its existing collateral portfolio. This shift often necessitates a change in the entity responsible for managing the collateral. If the initial collateral was in the form of stocks managed by a securities company, and the new or additional collateral is real estate, the representative typically needs to transition the role of collateral management to a bank. This is because, as previously discussed, banks are legally authorized to manage real estate assets, whereas securities companies are not.

In these scenarios, retaining the current representative while appointing a bank to take over the management of the new real estate collateral can streamline the process. This approach minimizes the need for extensive modifications in the bond's terms and conditions, and reduces the administrative burden. The existing representative continues to fulfill their role, ensuring that the bond issuer remains compliant with the bond terms and conditions, and executed agreements. Meanwhile, the bank, as the new collateral manager, takes on the responsibilities associated with managing the real estate assets.

6. Public vs. Private Bond Offerings: Differences in Collateral Management

It's critical to understand that these above-mentioned practices are primarily pertinent to public bond offerings. Public offerings are those where bonds are made available to the public. In this context, the rules and procedures around collateral management, including the appointment of representatives and collateral managers, are often more standardized and regulated to protect a broader range of the investors.

Conversely, in private bond offerings, where bonds are sold to a select group of investors, the rules and practices can be different. Private offerings often involve more tailored arrangements that can be negotiated based on the specific needs and agreements between the bond issuer and the investors. This adaptability allows for different approaches to collateral management, representative roles, and other terms of the bond issuance. The nature of these private transactions often means they are subject to less stringent public disclosure and regulatory requirements than public offerings, allowing for more customized and negotiated terms.