



**V I L A F**

VIETNAM INTERNATIONAL LAW FIRM

# NEW REGULATION ON INTEREST RATE DERIVATIVES

The SBV has issued Circular 01/2015/TT-NHNN (Circular 01) on interest rate derivatives (IRD) products of commercial banks and branches of offshore banks (Banks) to replace Decision 62/2006/QĐ-NHNN (Decision 62). Circular 01 will take effect on 2 March 2015. Read more on the significant changes under Circular 01.

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## Changing requirements on parties to an IRD

One of the parties to an IRD, the “vendor,” must be a Bank having the appropriate banking license permitting IRDs. The counterparty, the “customer,” can be any legal entity formed in Vietnam including a Bank.

A non-bank customer must have an effective underlying transaction in compliance with its licensed business.

A customer being a Bank may enter into an IRD to hedge interest rate risk not only for an effective underlying transaction compliant with its licensed business as under old Decision 62 but also to hedge interest rate risk arising out of its balance sheet.

## Expanding permitted IRDs

Circular 01 expands the list of permitted IRDs. It still permits forward interest rate, interest rate swap, accrual interest rate swap and cross-currency swap. It however adds interest rate option, which is defined as a right, but not an obligation, to pay or receive the agreed interest rate on a notional principal at a certain time prior to or on the maturity date and consists of interest rate cap, floor and collar.

## Vendor’s capital requirement removed

Circular 01 removes the requirement that a vendor must have equity of at least VND1,000 billion as a condition to provide IRD products.

## Underlying transactions are more broadly defined

Circular 01 allows all types of lawful underlying transactions with interest rate risk to be hedged with an IRD, provided that the underlying transaction cannot be an IRD. Circular 01 as issued removes the requirement that the underlying transaction must have “floating interest rate” as provided in an earlier draft of this Circular.

## Offsetting IRDs and trading in international markets

Circular 01 adds provisions permitting offsetting IRDs. A vendor is permitted to manage its risk in relation to its IRDs with its customers by entering into offsetting IRDs with:

- (i) other Banks; or
- (ii) offshore financial institutions.

If an offsetting IRD is conducted for at least two IRDs, the tenor of the offsetting IRD may not be longer than the longest tenor among those of the IRDs and the value of the offsetting IRD may not be larger than the aggregate notional value of those IRDs.

A Bank may not participate in international markets except for offsetting purposes, for hedging interest rate risks under an underlying transaction, or for hedging interest rate risks arising out of its balance sheet.

If a Bank transacts with an offshore financial institution, it must choose those which are ranked at least Baa/P-3 by Moody’s Investor Service or BBB-/A-3 by Standard & Poor’s or BBB-/F3 by Fitch Ratings at the time of execution of the IRDs. This requirement does not apply in case a Vietnam branch of a foreign bank enters into an offsetting IRD with its parent bank or another foreign branch of its parent bank.

## Risk mitigation requirements

A Bank must limit its net loss from IRDs to 5% of its charter capital. Net loss is the sum of (i) the aggregate of net gains and net losses of all effective IRDs and (ii) the aggregate of net gains and net losses of all IRDs expired during the financial year.

Circular 01 removes the requirement under Decision 62 that the aggregate principals covered under all the IRDs with one customer may not exceed 30% of the equity of the vendor.

## Reporting duties

Circular 01 does not change the requirement for Banks to file IRD reports to the State Bank of Vietnam by 12th of each month. However, it provides two revised forms of report which cover more detailed items. Particularly, there is a section on providing IRD products in the domestic markets (as vendor), a section on IRDs in the international markets, a section on using IRD products (as a customer) in the domestic market, and a separate report on offsetting IRDs.



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