

17 November 2021

THAILAND

Newsletter

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Practical Insights: Thailand's New Default Interest Landscape

Introduction

The Notification of the Bank of Thailand No. SorGorSor. 2.9/2563 Re: Calculation of Default Interest and Application of Proceeds ("**BOT Notification**") and the Royal Decree Amending the Civil and Commercial Code ("**CCC**") 2021 ("**Royal Decree**") were enacted in the second and third quarters of 2021 with an aim to reshape the lending framework in Thailand. This article provides details of the amendments and discusses practical issues and remaining uncertainties in interpreting the law in relation to default interest. The authors also discuss how the amendments may lead to different practices and positions in drafting loan agreements.

Background

The amendments in the BOT Notification and Royal Decree are summarized as follows:

	CCC (Section 224/1)	BOT Notification
Default interest rate	As specified; or If not specified, interest rate ¹ plus 2% per annum	Actual maximum interest rate plus maximum 3% per annum
Basis of default interest calculation	Principal of the installment(s) in default.	a. Installment loan: principal of each installment in default up until the court's acceptance of a complaint; and b. Revolving facility: the outstanding amount
Scope of application (in respect of the default interest rate and basis of default interest calculation)	a. Default interest rate: of general application; and b. Basis of default interest calculation: installment repayments of monetary obligations between any party.	Installment loans and revolving facilities between: a. Lenders: (i) financial institutions; (ii) companies within financial business groups which operate supervised personal loans, supervised nano finance, leasing, hire-purchase or asset management businesses; (iii) specialized financial institutions; (iv) non-bank supervised personal

		loans operators; (v) non-bank nano finance operators; or (vi) asset management companies ¹ b. Borrowers: (i) retail borrowers; or (ii) SME borrowers
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Key issues

1. Default payment of interest

CCC

The CCC does not provide a definition of 'installment repayment' under Section 224/1 and there is currently no definite interpretation by the officials as to which payment (e.g., the principal, or interest) is deemed as an installment repayment.

Certain loans feature a periodic payment of interest which is not scheduled to be jointly paid with principal, e.g., a bullet repayment, payment on demand and certain amortizing loans (where periodic repayment of the principal and periodic payment of interest are not set to be due in the same interval).

There remains uncertainty, in the aforementioned cases, whether a periodic payment of interest is considered as an installment repayment under Section 224/1. This leads to different positions in cases where only the interest payment is in default. Prior to the introduction of the Royal Decree, there were provisions in various loan agreements which stated that if a borrower does not pay the interest when due, the borrower must pay interest accruing on the principal amount outstanding at the default rate. Given that interest accrues on the entire outstanding principal amount, this contractual provision contradicts Section 224/1.

BOT Notification

The Q&A attached to the BOT Notification state that 'installment loans' mean credit with provisions on installments, which extend to cover credit-like transactions and include credit and credit-like transactions with a definite repayment period, whether in a single or multiple installments. Therefore, a loan with bullet repayments for example, may be considered as an installment loan under the BOT Notification. However, if the borrower merely defaults on an interest payment, since there is no base principal amount in default on which the default interest can be calculated, the lender may not be able to demand the default interest on the principal amount.

2. Impact on loan agreement drafting

As mentioned above, the customary provision in loan agreements prior to the introduction of the Royal Decree may be contradictory to Section 224/1. The lenders should consider whether such provision should be deleted in its entirety or formulate alternative wording to protect themselves in a case where there is a default in an interest payment.

¹ Section 7 of the CCC stipulates that if interest is to be paid and the rate of interest is not specified in an agreement or by provisions of law, the rate of interest shall be 3 per cent per annum.

² Effective rates of certain credit, e.g., supervised personal loans and supervised nano finance, are also subject to specific laws.

3. Loans granted to corporate borrowers

The types of borrowers subject to the BOT Notification are retail borrowers, SME borrowers and corporate borrowers. Each of these are classified by definitions set forth by each lender. A corporate borrower is not subject to the default interest rate and the basis of default interest calculation criteria under the BOT Notification, therefore must comply with the CCC, which is of general application in these matters. Consequently, the default interest rate that a lender (under the BOT's supervision) can demand from a corporate borrower is as agreed between the parties on the basis of the CCC and such agreed rate is not subject to the ceiling of 3% per annum under the BOT Notification. It is important to note that in the case of a corporate borrower, a lender is subject to the BOT Notification in terms of the application of proceeds, i.e., the proceeds will be applied towards fees, interest and the principal respectively on a horizontal basis (or otherwise, if more favorable to the borrower) the details of which can be found here (for more details on horizontal application of proceeds, please see our Newsletter, "Change to Calculation Method for Default Interest" dated 25 November, 2020 at this [LINK](#)).

4. Acceleration of loans

CCC

According to the Office of the Council of State, typical acceleration clauses in loan agreements (i.e., the clause that entitles the lender to declare an occurrence of an event of default under a loan agreement and demand all outstanding amounts to be due and payable immediately, and where a failure to make a payment upon acceleration will result in default interest being charged on the whole outstanding amount) does not contradict Section 224/1 as it will be deemed that the loan is no longer due on an installment basis.

BOT Notification

Although we believe that there should not be any issue in adopting the acceleration clause in loan agreements from the BOT perspective, there is currently no clear interpretation as to whether an acceleration clause contradicts provisions regarding the basis of default interest calculation under the BOT Notification in the case of an installment loan.

Conclusion

The BOT Notification and Royal Decree have created some uncertainty as to how default interest rates are determined, and whether contractual clauses that have traditionally been used in loan agreements remain valid. As such, lenders and borrowers should not only become familiar with the amendments introduced by the BOT Notification and the Royal Decree, but also reexamine existing loan agreements to ensure due compliance with the law and their own protection as well as to avoid any negative consequences in the event of a default arising.

If you would like to discuss any of the legal implication of the matters discussed above, please contact the authors listed in left-hand column.

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