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BRIEFING

Vietnam – amended Civil Code

Summary

Broader, shorter, freer, clearer and without too many amendments: this is our summary of the amended Vietnamese Civil Code, which took effect on 1 January 2006. This briefing provides an overview of the changes introduced by the amended Civil Code.

Scope of application

The amended Civil Code abolishes the ‘economic contracts’ regulations. It governs not only ‘civil relations’ but also commercial, business and labour relations. This results in an upgraded legal framework for business as of 1 January 2006.

The original 1995 Civil Code only applied to ‘civil relations’ which, though not clearly defined, were generally understood to mean relations arising in the daily life and personal activities of individuals or organisations. Although the original Civil Code could apply to commercial and business transactions, its application was limited by the 1989 Ordinance on Economic Contracts, the 1990 Decree on Economic Contracts and the Commercial Law. The Economic Contracts regulations were a problem for lawyers for many years. They constituted an outdated, third body of contract law in Vietnam, which often conflicted with the Civil Code and the Commercial Law. They contained numerous problems, including:

- i compulsory contents for ‘economic contracts’, the absence of which rendered contracts invalid;
- ii strange termination rights; and
- iii a six-month limitation period for legal actions concerning disputes involving economic contracts. No-one (including the authorities) could clearly separate ‘economic contracts’ from ‘civil contracts’ and ‘commercial contracts’.

Although upgraded, the law is still not perfect. By expanding the scope of application of both the Civil Code and the Commercial Law and by failing to provide

a clear dividing line between the amended Commercial Law and Civil Code, the drafter has left various potential conflicts between the two laws.

Security interests

The provisions relating to security interests, particularly pledges, mortgages and guarantees have been amended. Some amendments have been taken from Decree 165 of the Government dated 19 November 1999 on secured transactions. Others are novel. Although further implementing regulations are required in order to understand all the ramifications, the amendments should provide greater flexibility for lenders.

Pledges and mortgages

Under the original Civil Code:

- a pledge was an arrangement under which the ‘obligor’ delivered movable property owned by it to the ‘obligee’ as security for the performance of its obligations. A pledge under the original Civil Code could either be a ‘possessory pledge’ (ie the pledged asset was held by the pledgee) or a non-possessory pledge; and
- a mortgage was an arrangement under which the obligor used immovable property owned by it as security for the performance of its obligations.

Under the amended Civil Code:

- a pledge is an arrangement where the pledgor hands over the possession of an asset to the pledgee as security for the performance of an obligation; and

- a mortgage is an arrangement where the mortgagor uses its assets (without handing over the possession of such assets) as security for the performance of an obligation.

This appears to change certain features of security interests law:

- a pledge or mortgage may be granted over both movable and immovable assets;
- the pledgor or the mortgagor is no longer required to be the obligor. As such, it may be possible for the pledgor or mortgagor to grant a pledge or mortgage to secure a third party's obligation; and
- a pledgee must possess the pledged assets, while a mortgagee must not have possession of the mortgaged assets.

Guarantee

The amended Civil Code does not expressly require that a guarantor uses its own assets as security for the secured obligation. This indicates that it may now be possible for a guarantor to provide a guarantee without being backed by specific assets as currently required by Decree 165.

Registration

Decree 165 provides that a secured transaction that is subject to registration only takes effect upon registration. By contrast, the amended Civil Code provides that:

- the registration of a secured transaction is a condition of the validity of such a transaction only if the law so provides;
- if a secured transaction has to be registered, then the transaction becomes legally binding against a third party from the time of registration; and
- if an asset is subject to multiple security interests, both unregistered and registered, then the registered interest will have priority in receiving payment from the realisation of the secured asset.

The above provisions suggest that even if a security interest is not registered, it does not affect the validity of the interest between the parties unless the law provides otherwise (as it might do, for example, in the context of a mortgage of real property). However, the secured party may lose its priority in receiving payment from the realisation of the secured asset if there is another registered security interest over the same asset. This is a significant change in the law, which could affect, for

example, banks that used to hold unregistered pledges over accounts and cash.

Set-off rights

Although not a security interest, a significant change in the law of set-off should be noted. Under the new Civil Code, a party to a bilateral contract who is in possession of property of the counterparty now has a broad statutory right to retain that property if the other party fails to perform its obligations under the bilateral contract.

It is not clear to what extent the terms of a contract will be able to restrict this statutory right. Article 416.3 of the Civil Code states that 'The right to retain property shall terminate ... pursuant to the agreement of the parties'. Unfortunately, it is not clear if this applies only after the set-off has occurred.

Contracts

The amended Civil Code has made certain changes to contract law.

Offer and acceptance

- The amended Civil Code does not require an offer to enter into a contract to include the major terms of the contract, as was required by the original Civil Code.
- If the offeror loses its civil legal capacity or dies after the offeree has accepted the offer or vice versa, then the contract is still binding on the party that loses its civil legal capacity or dies.
- The amended Civil Code allows the offeree to withdraw or cancel the offer before the offeror receives an acceptance notice from the offeree.

Formalities

The amended Civil Code provides that the failure to comply with formalities does not invalidate a contract unless the law specifically says so. To strengthen the new position, the amended Civil Code provides that a written contract is valid when the last party signs the contract, regardless of whether this contract has to be notarised, certified or registered. The original Civil Code said a contract that was subject to notarisation, certification or registration was only valid upon notarisation, certification or registration.

The amended Civil Code also repeals the requirement for ‘major contents’ in a civil contract. Under the original Civil Code, a civil contract needed to contain certain major contents prescribed by law. The failure to include any major content could render a contract invalid.

Payment

The requirement that a payment obligation must be denominated in Vietnamese dong has also been removed. This does not mean that payments in Vietnam can necessarily be made in foreign currency. The foreign exchange regulations still contain extensive restrictions in this area.

Non-performance and breach

In a bilateral contract, if one party fails to perform its obligations when due, then the other party is now entitled to delay its own performance, to the extent that it was due after that date.

The requirement that a party alleged to have breached an obligation has the burden of proving the contrary has been repealed.

Assignment

The assignment of an obligation can now be made in verbal as well as written form.

Form contracts

The amended Civil Code provides more protection to consumers presented with ‘form’ contracts. Under the amended Civil Code, in a form contract, provisions that limit the liability of the party offering the contract, increase the liability of the other party or disregard other legitimate rights of the other party will be invalid unless otherwise agreed. The exact meaning of this will need to be determined over time.

Validity

If, at the time of signing a civil contract, it is impossible to perform the contract, then such contract is invalid.

Period of limitations

The period of limitation for making a claim concerning a civil contract is two years from the date of breach. For contracts with a foreign element that are governed by foreign laws, the period of limitation for making a claim will be according to the applicable law of such contract.

Property and ownership

The amended Civil Code requires immovable property to be registered. The transfer of ownership of immovable property only takes effect upon the registration of such transfer. Unfortunately, most real estate in Vietnam is still unregistered.

Intellectual property

Due to the recent 2005 Law on Intellectual Property, most of the provisions concerning intellectual property in the original Civil Code have been removed from the amended Civil Code. However, the amended Civil Code retains a limited number of provisions. It is not clear how these provisions will be reconciled with the Law on Intellectual Property.

Civil transactions

The amended Civil Code provides more certainty about the validity of a civil transaction, a term which includes contracts and unilateral legal actions. It reduces the pre-conditions to the validity of a civil transaction. Now, in order to be valid, a civil transaction need only satisfy the following conditions.

- The parties must have legal capacity and must voluntarily enter into the transaction.
- The purpose and contents of the transaction must not violate ‘prohibitions’ in the law and must not be contrary to social morals. The ‘prohibitions’ are defined to mean those legal provisions which prohibit an individual or organisation from taking a specific action. ‘Social morals’ means the standards of human behaviour that are recognised and respected in society. By contrast, the original Civil Code required a civil transaction ‘not to be contrary with law and social morals’, without further explanation, which could leave even greater uncertainty about whether or not certain transactions were valid.
- The transaction must comply with the form set out in the law only if the law states that such form is mandatory. This is a relaxation of the original Civil Code requirement that a civil transaction must be made in the form mentioned in the law in order to be valid. In the past, based on this provision, the courts often held a transaction to be invalid for failure to comply with formalities.

The amended Civil Code also provides some rules of interpretation for a civil transaction. If there is any ambiguity, the civil transaction (except for a contract or a will) will be interpreted according to the following principles:

- according to the true intention of the parties;
- according to the meaning that gives effect to the purpose of the transaction; and
- according to the customs where the transaction takes place.

able to take better security packages. As always, the most important question is how the new provisions in the amended Civil Code will be implemented.

For further information please contact

Tony Foster
T + 84 4 8247 422
F + 84 4 8268 300
E tony.foster@freshfields.com

Representatives

Entities doing business in Vietnam have to be careful that their contracts are signed by the legal or authorised representative of the counterparty. Under the original Civil Code and the Ordinance on Economic Contracts, the person that signed a contract on behalf of a legal person had to be the representative of that legal person either by law or by a written letter of authorisation. A contract signed by an unauthorised person would usually be held invalid as Vietnamese law does not have any clear concept of ostensible authority or implied powers. Although no such concept is introduced in the amended Civil Code, it contains some improvements:

- a letter (or contract) of authorisation does not need to be made in writing unless the law so requires;
- a transaction entered into by a representative who has exceeded his/her power will become binding on the party represented by such representative if that party (i) agrees or (ii) is aware of and does not object to such transaction. This should reduce the number of cases in which transactions are avoided based on the technicality that they were improperly signed.

Conclusion

The amended Civil Code appears to be a positive but limited development. It provides more freedom to the parties to a civil transaction and removes certain uncertainties in the original Civil Code. The amendments to contract law may provide foreign investors slightly greater comfort in selecting Vietnamese law as the governing law of a contract. The new provisions on security interests should make lending to Vietnam slightly more attractive as the lenders may eventually be