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Taking Security in Vietnam

VILAF
VIETNAM INTERNATIONAL LAW FIRM

Overview

Effective security is available although there are significant issues with respect to enforcement.

Vietnamese law recognises mortgages, pledges, liens and security deposits. However, although it is debatable, an assignment is commonly considered not to be a valid form of security under the laws of Vietnam and the assignee would not be considered a secured creditor.

The laws of Vietnam make a distinction between two forms of assets, moveable and immovable. Immoveable assets include land use rights, buildings and other properties attached to land and all other assets are deemed to be moveable.

Assets subject to security must be owned by the grantor (except for property under the management of State Owned Enterprises ("SOEs") and land use rights), transferable and not subject to dispute (confirmed by way of an undertaking from the grantor).

Key Issues

- An entity can grant security in favour of a foreign bank or company except in respect of land use rights and assets attached to land.
- Private ownership of land is not permitted, however people and entities in Vietnam are able to enjoy land use rights. The laws of Vietnam recognise mortgages created over land use rights, buildings and construction facilities, where security can be granted in favour of credit institutions in Vietnam, including foreign bank branches and finance companies licensed in Vietnam. However, security over land use rights granted in favour of offshore entities is not referred to under the law and, as such, this is usually interpreted to mean that land use rights cannot be mortgaged in favour of offshore entities.
- The laws of Vietnam permit the creation of security over both existing and future property.
- The rights of a registered mortgagee are subject to the rights of a party having a lien over the mortgaged property, the mortgagee would have to settle the obligations pursuant to the lien prior to realising its interests under the mortgage.

| Issue | Vietnam |
|---|---|
| Guarantee Available | Yes |
| Effective Security Available | Yes |
| Security Interest over Whole Business | Yes (however taking security over individual assets is recommended) |
| Security over Shares | Yes (subject to qualifications) |
| Security over Receivables | Yes |
| Security over Bank Accounts | Yes |
| Security over Land and Buildings | Yes (subject to significant restrictions) |
| Security over Intellectual Property | Yes |
| Security over Moveable Assets | Yes |
| Security over Contractual Rights (other than receivables) | Yes |
| Security over Debt Securities | Yes |
| Security over Ships and Aircraft | Yes |
| Loans and Security Transferable | Yes |

Summary

| Security | Characteristics | Perfection |
|----------|---|--|
| Pledge | <ul style="list-style-type: none"> ■ In writing and registered in certain cases as required by law. ■ Effective on delivery of the asset to the pledgee. ■ The pledgee may hold the pledged asset or may authorise a third person to take possession. ■ The pledgor must own the pledged assets. ■ The pledgee is obliged not to sell, exchange, give, lease or lend the pledged assets nor use it as security for the performance of another obligation. ■ Rights of the pledgee: <ul style="list-style-type: none"> -The pledgee is entitled to be reimbursed for reasonable expenses incurred in taking care of the pledged asset. -The pledgee will have the right to the goods recorded in the pledged bill of lading (order or bearer bill of lading). | <ul style="list-style-type: none"> ■ By way of registration. ■ Pledge of securities, in respect of shares of public companies only, must be deposited with the Vietnamese Securities Depository (VSD) and will only take effect after the VSD has completed the book entries for the transfer of securities from the securities trading account of the pledgor to the pledged securities account of the pledgee. Offshore pledgee should consider requesting VSD to block foreign ownership availability, which is subject to a quota for the purpose of enforcement. |
| Mortgage | <ul style="list-style-type: none"> ■ In writing and notarised, certified and, in certain cases, registered, as required by law. ■ The mortgagor must own the mortgaged asset. ■ Leased assets may also be mortgaged by the lessor. Any benefit and income derived from the lease will form part of the mortgaged assets. ■ Insurance proceeds will be deemed part of the mortgaged asset. ■ The mortgagor or a third party may add improvements to or invest in the mortgaged asset without specifying whether such improvements form part of the collateral and may use such improvements to secure other obligations. ■ Proceeds from the sale of secured stock in trade form part of the mortgaged asset. | <ul style="list-style-type: none"> ■ Registration is required. ■ There are different registration agencies for different types of secured properties. ■ Mortgages over land use rights take effect from the time of registration. ■ The priority of secured parties is determined in accordance with the chronological order of registration and a mortgage is only effective “against third parties” at the time of registration. ■ A mortgage or pledge over assets of a SOE must be approved. ■ Notice of mortgage to insurer in mortgage over insurance is required. Acknowledgement from insurer is recommended. Notice of mortgage to and acknowledgement from relevant buyer/obligor in mortgage over receivable/contractual rights is recommended. |

| Security | Characteristics | Perfection |
|-----------|--|------------|
| | <ul style="list-style-type: none"> ■ Third parties are permitted to own assets being “stock in trade” of the mortgagor which are sold, exchanged or donated without permission of the mortgagee if: <ul style="list-style-type: none"> -such a sale or exchange of assets takes place before the registration of the mortgage and the buyer purchases in good faith; -the registration is invalid, or incorrect pursuant to the law relating to the registration of security interests. | |
| Guarantee | <ul style="list-style-type: none"> ■ In writing; and if so required by law, notarised or certified. ■ A beneficiary has the right to demand the guarantor to perform its obligation first, unless otherwise agreed. ■ A guaranteed obligation includes interest on the principal, penalties and compensation for any damage, unless otherwise agreed. ■ When more than one person guarantees an obligation, those persons must perform the guarantee jointly, except where it is agreed or provided by law that the guarantee comprises of separate obligations. The beneficiary may demand any of the joint guarantors to perform the obligation in its entirety. ■ Notice must be given to the guarantor upon the guaranteed obligation arising. ■ The guarantor and the beneficiary may agree on additional asset-backed security interests (i.e. mortgage or pledge over assets) where the guarantor may use its assets to secure its respective obligations to the beneficiary under the guarantee. | N/A |

Enforcement

Pledge and Mortgage

Notice of enforcement

Upon occurrence of an enforcement event the secured party or another person authorised by the secured party must issue a notice of enforcement to the other registered mortgagees (if the assets have been mortgaged in favour of more than one mortgagee) or register the notice of enforcement with the relevant security registrar before enforcing the security.

The notice of enforcement must contain the following information:

- reasons for enforcement
- secured obligations
- description of assets
- method, time and location of the enforcement

The advance enforcement notice requirement does not apply if the secured assets are susceptible to devaluation, are receivables or bills of lading. In such cases, the secured party could issue notice after enforcing the security.

Waiting period

The secured party can only enforce the security after the expiry of the waiting period, which may be agreed between the parties. In the absence of a specified period, the term shall be 7 days for moveable assets and 15 days for immovable assets from the date of the notice of enforcement or the date of registration of the notice of enforcement.

Handover of mortgaged assets

The secured party or its authorised person must give notice to the mortgagor or a third party who has possession of the mortgaged assets for the purpose of enforcement (the "Handover Notice"). The notice must stipulate the period for the handover of the mortgaged assets, which is not specified by law.

Upon the expiry of the handover period, the mortgagee can seize the mortgaged property itself or take legal action before a Vietnamese court. In the event the mortgagee chooses to seize the mortgaged property, it must give reasonable prior notice to the party which has possession of the mortgage property and the notice should specify a reasonable period (the "Seizure Notice").

The Seizure Notice needs to contain the following information:

- reason for the handover of the mortgaged assets
- time and date for the handover
- rights and obligations of the parties

The mortgagee may seek the assistance of the People's Committee at the ward level or the local police for assistance to enforce a seizure notice. However, in practice, it is difficult to obtain such assistance. The mortgagee may sue the borrower before a Vietnamese court for the failure to pay under a loan

agreement and to obtain the enforcement of the security for discharging the borrower's debt. This process may take from three to six months.

Enforcement methods

The parties may agree on the following enforcement methods:

- sale of the mortgaged property (by way of auction or private sale)
- take-over of the mortgaged property in satisfaction of the secured obligations
- receipt of direct payments from third parties
- other enforcement methods.

As such, the security agreement should provide for specific enforcement methods.

Priority

Priority is based on the chronological order of registration. If a secured transaction is not registered, priority is determined based on the date of the security agreement. Registered security has priority over un-registered security.

Proceeds received from the enforcement of security are distributed in the following order:

- costs and expenses for preserving and selling the mortgaged properties
- other necessary and reasonable expenses relating to the enforcement of the security
- payments to the mortgagee in the order of: principal, interest, default interest and damages.

While pending enforcement, the mortgagee may use or operate the mortgaged property.

Transfer of ownership

Ownership is transferred at the moment of possession or upon the completion of registration, if required. Transfer of ownership does not require the consent of the mortgagor and the security agreement is considered as the mortgagor's consent.

Sale

The sale, transfer or disposal of assets located in Vietnam must be denominated in, and conducted in, Vietnamese Dong except as otherwise approved by the State Bank of Vietnam. Proceeds from enforcement of the security may be remitted overseas to offshore lenders subject to submission of sufficient evidence to the remittance bank in accordance with foreign exchange regulations.

Guarantee

Beneficiary must serve notice to the Guarantor specifying the breach of underlying obligation and demanding that the Guarantor performs its obligations.

Issues relating to Specific Assets and Financing Structures

Assets

General business

- Restrictions exist with respect to taking security over immoveable assets (as discussed above).
- Transfer of the ownership interest in a foreign-invested company, upon the enforcement of the security, requires notice to be given to the licensing authority for the purpose of amending the Investment Certificate of such company. Some documents may need to be signed by the securing party or its project company, and there is a risk that it may refuse to sign. In this case, the security agreement should have a provision to allow the secured party to sign the necessary documents for the purpose of enforcement of the security.

Shares

- Listed shares: selling of listed securities on enforcement will be subject to regulations of the relevant exchange centre, such as a trading band and the 49 per cent cap on foreign ownership in the issuer's shares (the 49 per cent cap is also applicable to shares of public companies which are not listed).
- Shares: the transfer of shares may be subject to a lock-up period of three years for founding shareholders. An approval of a general meeting of shareholders of the company should be obtained for the transfer of shares upon enforcement in such cases.

Immoveable property

Borrowers are restricted from granting security over land use rights and land unless it is leasing land from the State and the Borrower has paid all land rental in advance, in which circumstances it is entitled to mortgage land use rights and assets attached to land to credit institutions licensed to operate in Vietnam only.

Contractual Rights

The laws of Vietnam expressly recognise the creation of security over property rights originating from copyright and intellectual property rights, the right to claim payments, the right to receive insurance proceeds and other property rights, whether these originated from a contract or some other legal basis. While it is possible to create security over contractual rights, this is limited to rights to receivables and it is questionable as to whether security could be created over non-receivables such as the lessee's right to lease under a lease agreement.

The right to insurance proceeds is also considered to be a property right and may be used as security and the right to receive insurance proceeds in respect of a mortgaged property is deemed part of the mortgaged property. The holder of security in relation to insurance proceeds is required to provide notice to the insurer. In respect of taking security over contractual rights, only when requested by the obligor in the

underlying contract is a notice of security required to be given by the holder of the security to the obligor under the underlying contract.

Future assets

Future assets are defined as assets in respect of which ownership shall be acquired by the securing party after the establishment of the secured obligations or after the execution of the security document. It is generally accepted that only a mortgage may be created over future assets. Updating the list of assets with the relevant security registrar is required when the future assets are formed.

Finance leasing

A banking license permitting finance leasing is required.

- A finance leasing transaction must satisfy one of the following characteristics:
 - Upon expiry of the lease, the ownership of the leased assets is transferred to the lessee or the lessee continues to lease the assets, as agreed by the parties;
 - Upon expiry of the lease, the lessee has the preferential right to purchase the leased assets at a par price less than the actual value at the time of acquisition thereof;
 - The lease duration of each leased asset must be at least sixty (60%) per cent of the period required for amortisation of such asset;
 - The total lease payments for each leased asset in the contract must be at least equivalent to the value of such asset at the date of contract.
- Leasing assets must be registered with the relevant registrar of security transactions.

This section discusses onshore finance leasing only and is not applicable to cross-border finance leases from offshore finance leasing companies to onshore companies in Vietnam.

Sale and lease back

A banking license permitting finance leasing is required.

- It is deemed a finance lease. Please refer to "Finance Leasing".
- The sale agreement is only effective from the effective time of finance lease agreement.
- Must be registered with the relevant registrars of the security transactions.

Hire purchase

It is deemed to be a finance leasing transaction under which the lessee will purchase the leased asset at the end of the lease. Please refer to "Finance Leasing".

Conditional sale / Lease of assets

A sale contract in which the seller retains ownership in the property until the sale price is paid in full which must also be in writing.

- Apart from this documentation requirement, the law does not specify any other requirements as to form and content of conditional sale agreements.
- Registration may be necessary in order for a seller of a conditional sale to protect itself against a third party which takes security over the same goods in relation to the buyer's obligations.
- Where the conditional sale of moveable property is not subject to registration, the seller shall enjoy first priority over the property. Conditional sale and lease arrangements do not need to be registered, even if the property has been used as a secured asset to secure the buyer's or lessee's obligations if the term of such lease agreement is less than one year.
- If the conditional sale or long term lease has not been duly registered within 15 days, or if registration of the sale or lease is after registration of the security interest, the secured party (mortgagee or pledgee) will have first priority over such moveables. The competent registrar for conditional sale transactions of moveables is the National Registration Agency of Secured Transactions ("NRAST").
- A bank licensed in Vietnam must operate within the scope of its banking license. As the business line permitting conditional sale of a business or assets would not usually be included in the banking license of a Vietnam licensed bank, such banks would generally not be able to enter into conditional sale agreements.

Factoring (aka invoice discounting) e.g. sale of lease receivables

- A banking license permitting factoring activities is required.
- Although it is not a type of security, an assignment of the right to claim repayment of debts could be registered with NRAST in order to enjoy priority over other assignees or mortgagees.

Issues for International Lenders and Foreign Entities

Foreign governing law

When a secured transaction involves a "foreign element" (i.e. where at least one party is a foreign entity or where assets are located outside of Vietnam), the security agreement may be governed by a foreign law, subject to:

- i) The application of foreign law not being against the "fundamental principles of the laws of Vietnam." It is noted that there is no further guidance as to what is meant by the term "fundamental principles of the laws of Vietnam."
- ii) The security agreement in respect of immovable properties in Vietnam must be governed by the laws of Vietnam.
- iii) If the security agreement is entered into in Vietnam and entirely performed in Vietnam, the security agreement must be governed by the laws of Vietnam.

iv) Enforcement considerations may mean that Vietnamese law governed security is required in most cases.

In accordance with the above a security agreement between parties located in Vietnam should normally be governed by the laws of Vietnam.

Language

There is no legal requirement on the language of the security document except for:

- the application in relation to the registration of security transactions must be made in the form as required by law, which is in Vietnamese.
- Security documents to be notarised must be made in Vietnamese.

Security documents over immovable assets to be perfected by way of registration are, in practice, required by the security registrar to be submitted in Vietnamese.

Security Agents

The laws of Vietnam are silent as to holding security on trust. A company is entitled to authorise another company to execute and perform a contract on its behalf. A bank is entitled to provide the services of an agent and a bank can hold security as agent in favour of a syndicate of lenders as an authorised representative of the lenders. It is unclear under the regulation on syndicated loans whether the security agent must be one of the syndicated lenders.

The agent shall have the liability imposed on it as an authorised representative, including:

- An authorised representative may only perform works within the authorised scope of works. Where a person and the authorised representative enter into and perform a civil transaction deliberately beyond the authorised scope of works and thereby cause damage to the principal, they shall be jointly liable to compensate for the damage.
- An authorised representative must inform third parties in civil transactions of the authorised scope of works.
- An authorised agent must be an independent third party.

It should be noted that:

- As the laws of Vietnam do not explicitly recognise the concept of security agency, it is still uncertain whether the appointment of a local bank to take security for and on behalf of offshore lenders for the purpose of taking security over immovable assets is valid. Article 72 of Law on Credit Institution has given credit institutions operating in Vietnam the right to offer "entrustment" services or to act as agent for "other organisations" in various areas relating to banking operations, however, local credit institutions are hesitant to provide trust or security agent services due to a lack of detailed guidance.

- The main risk associated with this option is the legal uncertainty of the authorisation of an offshore bank as the principal, to any local bank, as the security agent, to take a mortgage over immovable assets. As discussed above, as offshore lenders are not able to take security over immovable assets, the courts of Vietnam may take the view that a local security agent is only allowed to take a security interest over assets that the offshore lenders, being the authorising entity, are legally permitted to, which does not include immovable assets.
- In practice, the Prime Minister granted a special approval for the use of an onshore security agent to take security over “assets attached to land” in the case of BOT power projects and important infrastructure projects. This is, however, a special preferential treatment for those sectors currently being promoted.

Transfer

In the event of the transfer of a secured loan, the transfer shall include the relevant security by operation of law and pursuant to the subsequent amendment of the applicable registration.

Insolvency

Claims with priority over a secured party include:

- Liens which will prevail over registered security as a right to retain the relevant assets subject to the corresponding debt being settled or discharged.
- Bona fide buyers are permitted to own assets other than “goods in circulation” sold, exchanged or donated without permission of the mortgagee in the following cases:
 - purchase takes place prior to registration
 - registration is invalid or incorrect
- Buyers are permitted to own assets being “goods in circulation” of the mortgagor in all cases.

Claw Back and Nullifying Security

- The courts of Vietnam have discretion to avoid security transactions entered into by the secured party within a three month period preceding the filing of an application for the bankruptcy of the securing party.
- Requests of secured creditors for enforcement may be automatically suspended from the date of a bankruptcy application being registered, until the court issues a liquidation decision to commence the liquidation process, at all times during and after which, the secured creditors will remain secured and rank in priority to any unsecured creditors.
- However, enforcement may only be permitted by the court if the following conditions are satisfied:
 - the mortgaged loan has become due;
 - the enforcement does not have a significant effect on operation of the mortgagor; and
 - the application for enforcement of the mortgage justifies enforcement.

Tax

There is no stamp tax in relation to the creation, perfection or enforcement of the security (however, registration fees are applicable).

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