



PERFORMANCE AND NON-PERFORMANCE OF CONTRACTS – REPORT FROM VIETNAM IN COMPARISON WITH THE PRINCIPLES OF ASIAN COMMERCIAL LAW

Dr Le Net, Partner, LNT & Partners, Arbitrator, Vietnam International Arbitration Centre

ABSTRACT

From the comparison between regulations of the Civil Code of Vietnam on contract law, and the provisions on performance and non-performance of the Principles of Asian Commercial Law (PACL), the article highlighted that the concept of breach under Vietnam law does not necessarily mean the same as non-performance elsewhere. Further, while a damage must be foreseeable, what constitutes foreseeability differ greatly from country to country. To its core, there is still no unified definition of causal link among countries. That makes the expectations of business people in Vietnam and those of other countries different and the extent of damages award to be different.

Key words: non-performance, breach, causal link, foreseeability, exclusion clause, notice of defect, penalty, price reduction, cost.

The performance and non-performance of contracts at the Principle of Asian Commercial Law have gone through a session in Korea in 2010 and later in Japan in March 2012 with major achievements. The viewpoints of Asian scholars are also not significantly different from European or American scholars, in the sense that the defaulting party shall have to be responsible for damages, and the damages must be reasonable. However, there are still discussions as to the definition of non-performance and the remedies thereof. Below, we will discuss, from the viewpoint of Vietnam law, the definition of non-performance, the remedy for non-performance, as well as the change of circumstances or hardship. We will provide comments to the Minutes of the Draft Non-performance PACL Seoul Forum with reference to

Ho Chi Minh City Head Office

Unit 3, Level 21, Bitexco Financial Tower
No.02 Hai Trieu Street, District 1
Ho Chi Minh City, VIETNAM
Tel: +84 8 3821 2357
Fax: +84 8 3910 3733

Hanoi Office

Unit 08A, Level 2, International Centre
17 Ngo Quyen Street, Hoan Kiem District
Hanoi, VIETNAM
Tel: +84 4 3824 8522
Fax: +84 4 3824 8580

San Francisco Office

101 California Street
Suite 2710
San Francisco, CA 94111 USA
Tel: +1 415 633 8831
Fax: +1 415 689 6821

Hong Kong Office (affiliate)

Two International Finance Centre
Level 19, 8 Finance Street
Central, Hong Kong CHINA
Tel: +852 3125 7639
Fax: +852 3125 7629

the PACL current draft, with experiences from Vietnam viewpoints.

1. The concept of non-performance

Article 1 PACL defines non-performance as a situation where a party fails to perform an obligation under the contract. However, this concept may be too broad. In Vietnam, a narrower concept, the concept of breach (i.e., non-excusable non-performance), is referred to. When Article 1 was drafted as non-performance, and set out the principle that “*the party is aggrieved by such non-performance may resort to any of the remedies*”, it would need to add a qualification of “*non-excusable*” non-performance, such as exclusion clauses or *volenti non fit injuria*.

Additionally, Vietnam law would agree to the concept that “*there is also failure of performance if, before performance is due, one party expressly or impliedly indicates his or her intention not to perform an obligation under the contract.*” However, until the time that performance is due, it is difficult to initiate a legal action. Rather, this could be an excuse to withhold performance of the counter-party.

The concept of “*volenti non fit injuria*” (self-infliction of damage) is a difficult concept. It is simple to say that “*a party may not rely on a failure of the other party to perform when such failure was caused by the first party*”, but there is a difference between “totally caused” or “partly caused” damages. Further, there is a difference between “directly caused” or “*indirectly caused*” damages.¹

For example, the parties in a contract may stipulate that a condition precedent for A to buy shares from B is that B must prove that there is no share pledged to a third party. The parties also agreed that 120 days after A becomes the owner of the shares, A must pay B the share prices. B has never proven that there is no share pledged to a third party, but A has nevertheless agrees to obtain the share ownership. A cannot subsequently use an excuse that B has never proven that there is no share pledged to a third party, in order for not paying B. This is because the condition precedent only applies for A to own shares from B, not for A to pay for

¹ Case 300241-2012 (Swiss Arbitration) *TL v SG*, non-recognition decision by Dong Nai People’s Court No 17/2014/QDST-KDTM dated 11 August 2014 (the *TL* case).

such shares.² Once A already agrees to own shares from B, it is already deemed to accept waiving the condition precedent that B must prove that there is no share pledged to a third party.

Article 1-1 PACL understands that when a party expresses that he will not perform an obligation under the contract, or indicates so by his conduct, the other party may resort to the remedies even before the due date of the performance. This provision is well understood, but it is difficult to judge what it meant by “*express*”, and whether a performance after the other party resorted to remedy is still possible if the due date has not come yet. The concept “*intention to breach*” is recognized in Vietnam under the concept of “*potential event of default*”. However, it is necessary to agree in advance in the agreement between the parties. If it is made to be part of PACL, then there is a concern that the parties may not opt for PACL to us due to its uncertainty as to the “intention to breach”.

The concept of Article 2 (fundamental non-performance) is similar to that of “material breach” under the Commercial Law of Vietnam.³ Under this provision, the material breach is a breach that was either stated in the contract or in the law and that when it occurs, the innocent party may terminate the contract. The wording of PACL, that a non-performance is “*fundamental if it results in such detriment to the other party to deprive him of substantially what he is entitled to expect under the contract, unless the non-performing party did not foresee and a reasonable person of the same kind in the same circumstances would not have foreseen such a result at the time of the conclusion of the contract*” would make this concept clearer. However, it is unclear as to how “foreseeability” could be an issue for fundamental breach. It is possible that in order to make the breach foreseeable, the innocent party must make a notice of breach to the default party, and only when such breach was not remedied within the period of notice for remedy, then a termination takes place.⁴ However, certain events could be dangerous, and the loss of the innocent party would be enormous, regardless of whether the defaulting party foresees the damages or not. For example, a taxi driver arriving five minutes late to the airport may cost the passenger a flight and later, an important meeting. Would such a delay be considered a fundamental delay, provided that the taxi driver could not have been aware that the

² Case 10/12, Vietnam International Arbitration Centre. VIAC Publishing.

³ Commercial Law 2005, Art. 295.

⁴ See *TL* case, *ibid*.

call for the taxi was for a trip to the airport? Regardless of the knowledge of the driver, the passenger should have the right to terminate if the taxi was late.

Regarding Article 2-1 (extension of time), it states that the aggrieved party, during the additional period so fixed, withhold his performance and claim damages for delay, but that may counter the traditional thinking about extension of time under construction law (such as the FIDIC form). It is therefore made clear that the extension of time should be reasonable. If the extension of time is not reasonable, then it bears no meaning and may mean a notice of termination. It is noted that the extension of time should be encouraged, but only when it is possible to do so from the viewpoint of the aggrieved party.⁵

2. Remedy for non-performance

2.1 Notice of non-performance

With respect to Article 3, it is agreed that the acceptance and lack of notice of non-conformity equates to the acceptance. This is so because otherwise, it would create an excuse for non performance on their turn. For example, a buyer of a scrap oil tanker may not rely on the excuse about the lack of information from the seller, if it has accepted the vessel and controlled it for one month but does not inspect or verify the information given by the seller, and later found that the oil tanker contained hazardous waste.⁶ At such, Vietnamese law supports the provision that non-conformity is not an excuse if the aggrieved party does not give a notice *“specifying the nature of the lack of conformity within a reasonable time after he has discovered or ought to have discovered the lack of conformity”*.⁷

With respect to para. 2 of the same provision, it would be a step back if the aggrieved party failed to give notice, but nevertheless can claim because a lack of conformity is something he knew or could not have been unaware. First of all, this may cause confusion as to whether, for example, the seller knowing about defect of the goods necessarily means that both parties accept that such defect exists and does not affect the sale price. Secondly, even if the seller

⁵ Case 06/14 of Vietnam International Arbitration Centre, VIAC publishing.

⁶ VIAC Arbitration Case 12/12.

⁷ *Ibid.*

knows of the defect, he may later refuse to recognize a defect that it does not know and nevertheless, the buyer has discovered the defect and does not object, so the buyer is deemed to accept such a defect. To make it clear-cut, we propose that para. 2 could be a basis for damages if it was a material/fundamental non-performance, regardless of whether the buyer discovered the defect or not. The notice must serve some purpose and must serve an interest. If it does not protect any interest or is used just to notify something that the parties already know, then such notice serves no purpose.

Vietnam law's viewpoint is silent about cumulative remedies, but it does not exclude it. That being said, one could not make double counting on damages, but may claim both damages and termination of the contract or specific performance. One exception is that if one has an option to choose between damage under tort and damage under contract for the same loss, he has to choose one of them.⁸

2.2 Suspension of performance

Vietnam law does not support the idea of an automatic right to suspend performance as proposed by Article 5.1 PACL (*"Where the parties are to perform simultaneously, either party may withhold performance until the other party tenders its performance substantially in conformity with the contract"*). This may lead to a circular request or mistrust between the parties, or a loophole to abuse. Vietnam law only allows a party to suspend if the condition precedent for performance is not yet fulfilled, or if the capacity to perform of the other party has been decreased to a substantial level that raises a doubt as to whether a performance from the other party was possible.⁹

2.3 Monetary obligation

With respect to monetary obligation (Article 6 PACL), it is an opinion from Vietnamese scholars that there should be stated the obligation to pay default interests as an automatic consequence of delay payment. As to the delayed payment, it should be clarified (perhaps in a

⁸ Case 28/13, Vietnam International Arbitration Centre.

⁹ Civil Code 2005, Articles 413 and 415.

comment) that it includes all kinds of payment, including deposits, advance payments, interim payments and final payments.

2.4 Non-monetary obligation

With respect to non-monetary obligation (Article 7 PACL), Vietnamese scholars recognize the similarity between Article 7 PACL and provisions of the Principles of International Commercial Contracts (PICC). As such, a request for specific performance is not possible if “(a) performance is impossible in law or in fact, (b) performance is of a personal character, (c) performance or, where relevant, enforcement is unreasonably burdensome or expensive, (d) the aggrieved party may reasonably obtain a substitute transaction from another source, or (e) the aggrieved party does not demand performance within a reasonable time”. Although there is no problem with (a), we believe there should be a link between (a) and (b); otherwise, it could be misunderstood to mean that a famous singer/actor could refuse to perform and pay damages in lieu of performance if he/she does not want to perform. That would impair the concept of *pacta sunt servanda*. The concept of (c), although plausible from the viewpoint of law and economics, should be cautious in its application. The words such as “*unreasonably burdensome* or *expensive*” should be supported with examples or clarifications or else, it could be a source of abuse. When PACL languages are uncertain, it loses attractiveness for business people to use them as a reference.¹⁰

As for (d), we support the concept that if substitution is easy and at a lower cost, it should be encouraged. As for (e), again, the word “*reasonable time*” should be clarified with examples and used with care, but we generally accept the concept.

2.5 Penalty

Stemming from the administrative concept of civil transactions applicable to a socialist country such as Vietnam, Vietnam law recognizes the concept of penalty as an “efficient breach” – a price to walk away from the contract that could make both parties happy. It is not required that a penalty must correspond to the loss. However, it is required that the penalty must be specific and clearly corresponds to the intention of the parties. In the case of conflict, the one

¹⁰ Case 18158/CYK ICC Arbitration (*Ob v. HCM PC*).

seeking to rely on a penalty clause will be at disadvantage during the interpretation of the intention of a penalty. In an arbitration case, the seller has provided deficient goods in two consignments. He referred to a fixed penalty clause in the first consignment and limited its liability for both consignments. It was held later that, since the email exchange on the penalty between the parties were agreed with respect to the first consignment, it did not cover the second consignment.¹¹ Therefore, we agree with the insertion of the penalty clause but requested that it should be interpreted *contra proferentem* as an exclusion clause, and perhaps could be used as a shield rather than a sword (a defence rather than a claim).

2.6 Price reduction

With respect to Article 11 PACL, Vietnam law also recognizes price reduction as a remedy. However, it is stated that a price reduction does not affect other remedies, and it should be so. The question is whether consequential loss such as loss of profit or loss of market value would be one of the damages to claim in addition to price reduction, or it should be an alternative claim.¹²

2.7 Cure

Article 12 PACL deals with cure rights. The cure right is possible under Vietnam, and even encouraged based on the principle of good faith performance. The cure is not a right, but a request. The tender of the cure as a right alleviates the performance in delay. We note, however, that such right should be exercised in a reasonable manner and provided that it is curable. The intention to cure is not as important as the consequence of the cure and whether such a cure could make good the irreparable harm that was caused by the breach. This, again, should be subject to a reasonableness test.

That is the reason why the proposal under Article 13 PACL is plausible, where para (c) impose a condition that “*the notice of cure is not expressly declined by the aggrieved party on the ground that the non-conformity amounts to fundamental non-performance or that cure harms his legitimate interest; harm to the aggrieved party’s legitimate interest includes causing*

¹¹ VIAC Arbitration, case 09/10-HCM.

¹² See Swiss Rule of Arbitration Case 300241-2012.

him unreasonable inconvenience, uncertainty or expense”. However, conditions (a) (“*The aggrieved party has not resorted to any remedy provided for in this Chapter that would be inconsistent with accepting cure*”) and (b) (“*The non-performing party gives notice without delay indicating the proposed manner and timing of the cure*”) may not be as important as condition (c).

With respect to Article 14(1) (“*The aggrieved party shall not unreasonably withhold cooperation to the non-performing party’s exercise of the right under Article 12 or Article 13*”), this provision is plausible, in the sense that the aggrieved party must mitigate the loss. Having said this, he must create favourable conditions for the defaulting party to perform (e.g., the employer shall provide the site access for the contractor to fix the defect), but other than this, he is not bound to incur further expenses. Also, the duty of cooperation must be seen from a cost and benefit perspective. If, for example, a hotel is in operation, giving site access to the contractor to fix certain rooms would do more harm than good to the normal business of the employer (the hotel owner).

2.8 Termination

The concept set forth in Article 15.1 PACL (“*Termination takes effect when such notice reaches the other party*”) may not be well perceived in Vietnam. Civil Code 1995 and Civil Code 2005 provided that a notice of termination must be well received by the other party and must give the other party a reasonable period to settle all outstanding issues after the notice is served. This is because a wrongful notice to terminate the contract would be a breach in itself.

The principle set forth under Article 16 (termination for fundamental breach) was well perceived by Vietnam law (both in Civil Code and Commercial Law). With respect to “*non-performance (that) is not fundamental, the aggrieved party may terminate the contract if he has given a prior notice of fixing a reasonable time and demanding performance within the period of time*”, this provision may be abused if the non-performance is impossible to perform, and such non-performance is not fundamental. For example, a condition precedent to receive ownership of shares in a share transfer agreement of a golf club is to give back membership cards that were pledged. Those cards have been cancelled and have no validity (as they were blank, not paid up and registered membership with the golf club), and impossible to retrieve as they were lost. It was held by the Vietnam International Arbitration Centre (VIAC) tribunal that

the lost report was already suffice to satisfy the condition, as the failure to give back the cards is non-fundamental and bears no adverse consequence to the share buyer, and the share buyer may not use it as an excuse.¹³

With respect to Article 17 (general effect of termination), Vietnam law also provides a similar solution, although not clearly stated in the Civil Code. That is, “*termination does not affect any provision in the contract for the settlement of disputes or any other term of the contract which is to operate even after termination*”. However, it is usual under Vietnam law that the parties will sign minutes of liquidation, in which performed or non-performed works are recorded as a basis for settlement or going to court/arbitration afterwards for a dispute. This is, however, unclear as to whether such minutes should be considered on a “*without prejudice*” basis if there was no such a notice.

Article 18 PACL (time limit of termination) is not provided for under Vietnam law but rather, is subject to general provisions in relation to the statute of limitation. However, under the Commercial Law, it is stipulated that any claim on defective goods must be brought within 90 days from the date of delivery. Therefore, it is plausible and a welcome provision that “*the right to termination shall be lost unless the notice of the non-conformity that will serve as the cause for termination is made to the other party within a reasonable time after the aggrieved party has become, or ought to have become, aware of the non-performance.*” Upon the time of delivery, if the obligee does not reject the performance, he should be deemed to have accepted it and therefore the right to request termination should be lost.¹⁴

Article 19 PACL (Restitution) sits oddly with the provision of termination. Normally, Vietnam law considers restitution as a solution for contract avoidance, when the contract is invalid *ex tunc* and the parties must restore the position for each other. Termination is a situation *ex nunc* and therefore, cannot restore the position. The position of PACL on the other hand, applies restoration for the situation whereby “*party who has supplied to the other party under the contract but has not received, or has properly rejected, the counter-performance which should correspond to his performance*” may claim restitution. Such a claim is equivalent as if there is no contract at all. This is also exposes potential abuse if the performance result has been

¹³ VIAC Case 09/12.

¹⁴ Id.

enjoyed by the other party and is impossible to restore. Moreover, it is unclear whether the restitution may overlap with other claims such as damages or request of payment for the price. It is enough to say that restitution should be adopted as a remedy of last resort and only applies when other solutions are not plausible.

With respect to termination of installment of the Contract (Article 21), it is plausible that certain schedules under the contract may be terminated without effect to other parts of the contract.

2.9 Damages

Under Article 23 (damages), it seems that PACL recognizes the concept of consequential loss by saying “*Damages include both any loss which the aggrieved party suffered and any gain of which he was deprived, taking into account any gain to the aggrieved party as a result of his avoidance of cost or harm.*” This loss, however, could be difficult to recover under Anglo-Saxon law. Under civil law countries, however, there is no such limitation. That principle is stated in the provision that “*Damages may not exceed the extent to which the non-performing party foresaw or could have reasonably foreseen at the time of the conclusion of the contract, in the light of the facts and matters of which he then knew or ought to have known, as a likely consequence of the non-performance.*” The question then becomes whether the damages should be rendered if that is the real loss of the aggrieved party. For example, a loss to a trader is obviously the opportunity to make profit on the purchased goods which are not damaged. The question then becomes what is the price of resale that could establish the degree of loss. If such a price could not be established with certainty, could we use a market value to be a benchmark of reasonable loss, or should we reject the claim for consequential loss in full?¹⁵ We are of opinion that such a claim should be plausible for both market price and the resale price. However, the problem is that both of those prices may have been unforeseen by the seller before it breaches the contract. If the court rejects the claim, the loss (real loss) may not be recovered. Therefore, we propose that such a loss could be estimated up to the judgment of the court, to a reasonable extent, and could use fair market value as a benchmark of loss of profits.

¹⁵ See Swiss Rule of Arbitration Case 300241-2012.

Conclusion

PACL has made a major achievement in drafting the two most difficult parts – performance and non-performance. PACL has captured the most recent development of contract law, such as hardship (change in circumstances), anticipatory breach and foreseeability of damages, but it has not left its footprint of something unique for PACL. At this point, PACL may need to discuss about the red line – the core value that PACL stands to protect – to protect the obligor or the obligee (the rightful party), and if so, to what extent. PACL cannot simply be a comparison of the civil laws among different jurisdictions. Rather, this should be the implementation of a core value, the so-called Asian value, and if so, what it is. Otherwise, PACL may fail to achieve its attractiveness.

Bibliography:

Le Net, Nguyen Xuan Quang, Nguyen Ho Bich Hang – Luật Dân sự Việt Nam (*Vietnam Contract Law*), Ho Chi Minh City National University 2008.

Le Net - *Contract Law of Vietnam*, in International Encyclopedia of Laws, Roger Blanpain (General Editor), Jacques Herbots (Editor), Kluwer Law International, First ed. 1999, Second ed. 2010.

Nguyen Ngoc Dien, Le Net – *Contract Law of Vietnam – Formation of Contracts*, report to the PACL 1st Congress 2008, Keio University, Japan.

Le Net – *Performance and Non-performance of Contract Law of Vietnam*, report to the PACL 3rd Congress, Seoul University, Korea.

UNIDROIT 1994 – Principles of International Commercial Contracts, translated by Le Net in 1999 - *Nguyên tắc Hợp đồng Thương mại Quốc tế UNIDROIT*.

Le Net – *UNIDROIT Principles and Vietnamese Contract Law*, in A. Bonelli (editor) – A Restatement of Lex Mercatoria – the UNIDROIT Principles of International Commercial Contract, Sweet & Maxwell.

Le Net – Kinh tế Luật (*Law and Economics*), Intellectual Press, 2007.

Le Net – Đầu trí và Luật (*Game Theory and Law*), Ho Chi Minh City University Press, 2005.

Index:

Anticipatory Breach

Breach

Causal Link

Contract

Cure

Damages

Exclusion Clause

Foreseeability

Material Breach

Notice of Breach

Non Performance

Penalty

Suspension

Termination