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BANK FINANCING FOR REAL ESTATE BUSINESSES IN VIETNAM

Financing in the real estate sector ranges from borrowing money from a bank or shareholders of the real estate entity to issuing bonds to the public. In Vietnam, real estate developers may even mobilize funds from purchasers of an apartment that is under construction for an advanced payment to finance the project. This article discusses the financing provided by Vietnam-based banks to real estate sector businesses in Vietnam.

Legislation on Lending and Security of Vietnamese Banks

Vietnam does not have a single law dealing with real estate financing. Instead, real estate financing activities are regulated by several legal documents. Of these, the 2005 Civil Code of Vietnam acts as the basic law providing provisions on the loan relationship between a lender and a borrower. The code contains basic provisions governing the conclusion of loan agreements, rights and obligations of parties, security arrangements, and the enforcement of the collateral in the event of default.

Financing by a bank is further regulated by the 2010 Law on Credit Institutions, Decision No. 1627/2001/QĐ-NHNN dated December 31, 2001, by the Governor of the State Bank of Vietnam (SBV) issuing Regulations on Lending by Credit Institutions to Their Customers, as amended in 2005 (Decision 1627).

Aiming to elaborate on the general provisions on secured transactions under the Civil Code, the government independently issued Decree No.163/2006/ND-CP dated December 29, 2006, on Secured Transactions (Decree 163). This decree secures the performance of credit obligations (e.g., the repayment of the loan by a client to the bank) and stipulates the creation and enforcement of security agreements.

A common asset to secure a bank loan for real estate projects is the land and the after-acquired assets on the land on which the project is developed. The only form of security available in Vietnam is the mortgage over the land and the after-acquired assets. Basic legal documents governing such mortgage are the 2003 Land Law; Decree No. 181/2004/ND-CP dated October 29, 2004, on the Implementation of the Land Law; and Circular No. 05/2005/TTLT-BTP-BTNMT dated June 16, 2006, on Guiding the Registration of the Mortgage and Guarantee over Land Use Rights and Assets Attached to Land (as amended in 2006, 2007, and 2010).

Issues on Bank Financing

Eligibility. To be eligible for a loan, a real estate developer must meet the following statutory conditions:

1. Be duly set up under the enterprise law of Vietnam;
2. Have a lawful purpose for borrowing;
3. Have financial ability for the repayment of the loan; and

4. Have feasible and effective investment, production, or business projects.

To satisfy the requirements in items (1) and (2) above, a bank will require the borrower to submit the corporate documents, such as the business registration certificate/license, charter, and board resolution for the loan. The borrower has to fill out the application for the loan provided by the bank. For the requirements in items (3) and (4) above, the bank normally requires the borrower to submit its financial statements, business plans, and other relevant documents for the project such as the investment license, project license, construction permit, land title deed, and so forth.

To borrow in foreign currencies, a borrower must further meet statutory conditions such as the purpose of the loan (i.e., for payment of imported goods or prepayment of foreign loans or for offshore investment or production of export goods or services). It is worthwhile to note that other loan purposes that are not listed under the law are not eligible for loans in foreign currencies.

Term of the loan. The term of a loan is agreed by the parties. In a real estate project, it is usually a medium- or long-term loan (i.e., tenor of more than 12 months). When the borrower is a legal entity with a term of operation (as specified under its license or articles of association), the term of the loan cannot extend beyond the term of operation of the legal entity.

Forms of lending. The parties are allowed to agree on the form of lending. It may be a single loan, syndicated loan, credit line or swingline, etc. However, a bank is generally not allowed to grant a loan to refinance debts of the borrower.

Lending limits. Except for cases such as loans to related parties (for which the lending limit is more restricted), a bank may lend a single client a maximum of 15 percent of its equity capital. It is worth noting, however, that this threshold does not apply to the loans that are funded from sources entrusted to the bank by the government or by another eligible person. A bank may also provide loans in excess of 15 percent in cases which are approved by the Prime Minister. Otherwise, if the bank wishes to provide a loan to a single client beyond the statutory threshold, it must join with other banks to form a syndicate.

Interest rate, default interest, and fees. Interest rates of loans in any currency are made on the basis of agreement by the parties. For loans in local currency, the parties may make reference to the monthly basic interest rate notified by the SBV.

The maximum default interest rate is 150 percent of the applicable interest rate. Below this threshold, the parties may agree upon their own default interest rate.

The recent circular of the SBV imposes strict regulations on bank fees. Most bank fees that are common in other jurisdictions are not permitted in Vietnam. Generally, banks in Vietnam may only collect fees for prepayment of principals and standby lines of credit. For syndicated loans, a processing fee may be collected.

Form and contents of the facility agreement. The facility agreement must be made in writing or via electronic form. It must contain clauses on disbursement conditions, purpose of the loan, types of loan, loan amount, applicable interest rate, tenor, security, value of security assets, method of repayment, and other statutory clauses.

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Rights and obligations. Decision 1627 lists the statutory rights and obligations of the borrower and the bank, as set forth below. The parties may agree on other rights and obligations in the facility agreement.

Borrower's rights

- To refuse to satisfy any requirement of the bank which is inconsistent with the facility agreement; and
- To lodge complaints or to institute legal proceedings for any breach of the facility agreement by the bank.

Borrower's obligations

- To provide full and accurate information and documents relating to the loan;
- To utilize the loan monies for the correct purpose and to perform properly the facility agreement and any other undertakings;
- To repay the loan principal and interest as per the facility agreement; and
- To be responsible for failure to perform properly the terms for repayment agreed in the facility agreement and the terms relating to loan security in the facility agreement.

Bank's rights

- To require the borrower to prove the feasibility of the investment project or plan for production, business and services or investment project, as well as to prove the financial capacity of the borrower prior to lending;
- To refuse to lend if the lending conditions are unfulfilled or the lending project or plan is not effective or is illegal, or if the bank has insufficient capital sources;
- To inspect and supervise the loan utilization and repayment process;
- To cease lending and recover debts upon discovery of false information or breach of the facility agreement by the borrower;
- To institute legal proceedings for breach of the facility agreement;
- To enforce the security if the borrower fails to repay the debt on time in order to recover the debt; and
- To exempt or deduct loan interest, debt term extensions, and adjustments of repayment periods; to trade in debts as per regulations of SBV and to carry out debt restructuring, debt blockade, or debt write-off.

Bank's obligations

- To comply strictly with the provisions in the facility agreement; and
- To maintain credit records in accordance with the provisions of the law.

Issues on Security

Assets used as security. Decree 163 allows the parties to agree on asset/property used as security, provided that (i) the property belongs to the party that offers the security and (ii) it is commercially transactionable. The secured property can be an existing or future property (e.g., an after-acquired apartment).

In addition, an asset can be used as security for multiple loans or several assets can be used as a security for a single loan.

Validity and binding force of a secured transaction. Under Vietnamese laws, a secured transaction becomes valid (and has legal binding force accordingly) on the parties when the parties conclude the security agreement, except in the following cases:

- When the parties agree otherwise;
- If the security agreement is a pledge, its validity and binding force starts from the moment of handing over the security;
- If the security agreement involves the mortgage over land use rights, an aircraft, or a ship, its validity and binding force starts from the moment of registration of the mortgage agreement; and
- If the security agreement involves the mortgage over a house, its validity and binding force starts from the moment of notarization of the mortgage agreement.

Effectiveness against third parties. A security agreement is effective against any third party from the moment of registration of the agreement. The security of an immovable asset, such as land or the assets attached to land, must be registered with the local land use right registration office.

Enforcement. Decree 163 allows the parties to agree on the circumstances where the security can be enforced. In the absence of such term, the law allows the bank to enforce the security when (i) the borrower does not perform or improperly performs its payment obligation; (ii) the borrower provides false information or breaches the facility agreement; and (iii) the borrower becomes bankrupt.

Methods of enforcement. The parties may agree on the methods of enforcement of the security. In practice, various forms of enforcement are adopted, such as selling via auction, selling directly to a third party, or receiving the security as the payment for the outstanding debts. If the parties fail to agree on the methods of enforcement, the security will be sold via auction.

Enforcement process. In the event of default, the bank may require the borrower to hand over the security for enforcement by sending a notice.

If the borrower fails to hand over the security, the bank is entitled to take possession of the security or bring a legal action. When taking possession of the security, the bank has to notify the mortgagor in writing of the taking over of the security and give the borrower a "reasonable time" for arranging the surrender of the security. The notice must specify the reasons, the time of taking possession, and the rights and obligations of each party. Vietnamese law does not define "reasonable time."

The bank may also ask the local People's Committee and the police where the land/building (as the security) is situated to keep the peace and order to help the bank exercise its right to take over the security. Unfortunately, neither the local People's Committee nor the police have a statutory obligation to cooperate with the bank or guarantee the success of the taking over of the land/building. If the bank cannot take over the security due to the borrower's refusal to complete the handover, the only recourse for the bank is to initiate a lawsuit against the borrower.

Vietnamese courts normally find in favor of the lender. However, the courts always allow the security to be sold via auction to minimize hardship to the borrower. 🏠