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### Compensation for Damages Resulting from Breach of Contract Under Vietnamese Law

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#### Abstract

Compensation for damages resulting from breach of contract is a common legal remedy applied when one or more parties fail to fulfill their contractual obligations. In Vietnam, this remedy is governed primarily by two legal instruments: The 2015 Civil Code and the 2005 Commercial Law. However, the relevant provisions in these two instruments remain

inconsistent in several respects. This article focuses on analyzing the provisions of the 2015 Civil Code and the 2005 Commercial Law regarding compensation for contractual breaches, identifying certain limitations, and proposing recommendations aimed at improving the legal framework in this area.

**Keywords:** Compensation for Damages, Contract Breach, Civil Law, Commercial Law

#### 1. Introduction

Contracts are formed on the basis of mutual agreement between parties with the purpose of establishing, altering, or terminating civil rights and obligations. Influenced by the principle of *Pacta sunt servanda* (agreements must be kept), the legal systems of countries around the world consistently affirm that once a contract is lawfully concluded, it has binding effect on the parties involved, as if it were law, and must be duly performed. Any act of suspension, cancellation, amendment, or supplementation of the contract must result from mutual agreement between the parties or be grounded on legal provisions.

The failure to perform, or improper performance of, contractual obligations without legal justification constitutes a breach of contract and is subject to legal sanctions. One of the most common sanctions applied in the event of a contractual breach is the remedy of compensation for damages.

Currently, in Vietnam, compensation for damages resulting from contractual breaches is governed by two key legal instruments: The 2015 Civil Code and the 2005 Commercial Law. Among these, the 2015 Civil Code is regarded as the foundational legislation that generally regulates liability for contractual damages, while the 2005 Commercial Law provides specific provisions applicable to contractual breaches in the commercial sector. Within the Civil Code, the relevant provisions are scattered across various articles, primarily from Article 360 to Article 364, as well as Articles 418 and 419. In the Commercial Law, the rules governing liability for damages arising from contractual breaches are set out in Articles 302 to 307. Although both the 2015 Civil Code and the 2005 Commercial Law uniformly recognize compensation for damages due to contractual breach as a form of civil liability arising when one party violates the contract and causes damage to the other party, there remain notable inconsistencies between the two laws in terms of: The types of damages eligible for compensation, the amount of compensation, and the cases of exemption from liability. These inconsistencies have posed significant difficulties in practical application and require further academic and legislative scrutiny for improvement.

#### 2. Research Purpose

This study is conducted with the objective of examining the differences between the Civil Code of 2015 and the Commercial Law of 2005 with respect to compensation for damages arising from contractual breaches. The research aims to analyze the shortcomings and inconsistencies in the current Vietnamese legal framework on this matter, thereby offering recommendations to improve the relevant provisions by drawing on comparative legislative experiences from other jurisdictions.

### 3. Research Methodology

This research adopts comparative and analytical legal methods to assess the Vietnamese legal provisions on compensation for contractual breaches in relation to the laws of selected foreign jurisdictions. On that basis, the study identifies existing inadequacies and derives lessons that may contribute to the improvement and harmonization of Vietnamese contract law.

### 4. Vietnamese Legal Framework on Compensation for Damages for Breach of Contract

#### 4.1 Conditions for Imposing Liability for Damages

Both the 2015 Civil Code and the 2005 Commercial Law consistently stipulate that liability for compensation due to contractual breach arises upon the fulfillment of the following conditions:

##### *First, actual damage must have occurred*

Damage is a prerequisite for imposing liability for compensation in contractual relations. The purpose of compensation is to require the breaching party to remedy the consequences by compensating for material and moral losses suffered by the aggrieved party. Accordingly, if no damage has occurred, no obligation to compensate shall arise.

##### *Second, there must be a breach of contract*

A breach of contract is defined as the failure to perform, or the improper performance of, obligations arising from the contract. These obligations may be expressly stipulated in the contractual terms or may arise under applicable legal provisions governing the contract. A breach of contract only occurs where a legally valid contract has been entered into and is in force. A contract is deemed valid if it satisfies fundamental legal requirements, including: Genuine consent of the parties (i.e., free from fraud, duress, or coercion); legal capacity of the contracting parties; lawful purpose and content not contrary to statutory prohibitions or public morality; and conformity with the prescribed form, where required by law.

An act shall not be considered a breach if the party performing it is under no legal obligation to do so. For example, in a contract for the sale of goods, if the seller delivers the goods before the agreed delivery date, the buyer is entitled to refuse acceptance, and such refusal cannot be deemed a breach of contract since the buyer is not legally required to accept early delivery.

##### *Third, there must be a causal link between the breach and the damage*

Liability for compensation shall arise only when there is a causal relationship between the contractual breach and the damage incurred. This means that the breach must be the direct cause of the damage, and conversely, the damage must be the inevitable and objective consequence of the breach. Only where it can be proven that the damage is a necessary and inherent result of the breach shall the breaching party be held liable.

In a causal relationship, the cause must precede the consequence; the cause gives rise to the effect. Therefore, temporally, the breach must occur before the damage. If, for any reason, the damage occurs prior to the breach, the two shall not be considered causally connected, and the party in breach shall not be held liable for compensation.

#### 4.2 On Compensable Damages

The Civil Code of 2015 and the Commercial Law of 2005

provide differing regulations on the types of damages subject to compensation in cases of contractual breach.

Under the Civil Code of 2015, compensable damages arising from a breach of contract include both material (pecuniary) and moral (non-pecuniary) damages (Article 361 of the Civil Code 2015). Specifically:

**First, material damages** refer to identifiable and actual pecuniary losses, including property damage, reasonable costs incurred to prevent, limit, or remedy such damage, and actual lost or diminished income (Clause 2, Article 361, Civil Code 2015). These are damages that can be quantified in monetary terms.

"Property damage" in this context refers to the loss, destruction, or deterioration of property caused by a contractual breach. Lost property denotes property that has permanently exited the ownership of its holder against their will and cannot be recovered, thus constituting an irreparable and total loss. Where property still exists but has been impaired, it may be categorized as either destroyed or damaged. "Destroyed property" refers to severely deteriorated property that can no longer be used for its intended function, whereas "damaged property" refers to items with impaired usability due to the malfunction of one or more components but which remain repairable.

"Reasonable expenses for preventing, limiting, or remedying damage" refer to the actual costs incurred by the aggrieved party to prevent further harm or to address the adverse consequences of the infringement of property, health, life, or non-material interests. These include, but are not limited to: Repair costs, replacement costs for materials, costs of mitigation, and expenses to rectify the damage already incurred.

"Actual lost or diminished income" refers to the lawful monthly income that the entitled party (the aggrieved party) was receiving or would have reasonably received had the breach not occurred. Such damages must be clearly and reliably established. The loss refers to income that the injured party was legitimately expected to earn but did not due to the breach. Diminished income refers to the measurable difference between pre-breach and post-breach earnings resulting directly from the contractual violation.

To qualify for compensation, these losses—property damage, reasonable mitigation costs, and lost or diminished income—must be "actual and ascertainable" as stipulated in Clause 2, Article 351 of the Civil Code 2015. This means that the damages must be objective and certain, not speculative or hypothetical. Actuality and certainty imply that the losses are not merely potential or inferred, but have either already occurred (e.g., destroyed or damaged property) or will inevitably occur in the future (e.g., income or profit that would have been earned from the now-lost or damaged property).

##### **Second, moral (non-pecuniary) damages**

Clause 3, Article 419 of the Civil Code 2015 provides that: *"At the request of the entitled party, the court may require the obligated party to compensate for mental suffering."* Therefore, in addition to material damages, the liable party may also be ordered to compensate for non-material harm. "Moral damages" are defined in Clause 3, Article 361 of the Civil Code 2015 as spiritual or psychological loss resulting from infringement of life, health, honor, dignity, reputation, and other personal rights of a legal subject.

In contrast, the Commercial Law of 2005 does not recognize compensation for moral damages. Clause 2, Article 302 of

the Commercial Law 2005 states: *"The value of compensation shall include the actual and direct loss that the aggrieved party has suffered due to the breach and the direct benefits that the aggrieved party would have enjoyed if such breach had not occurred."* Under this provision, damages for breach of contract are strictly limited to material loss and do not extend to moral injury. Material compensable damages under the Commercial Law are classified into two categories:

1. Actual and direct loss suffered by the aggrieved party due to the breach; and
2. Direct benefits that the aggrieved party would have received had the breach not occurred.

#### 4.3 On the Extent of Compensation for Damages

The Civil Code of 2015 and the Commercial Law of 2005 provide differing rules on the extent of compensable damages arising from a breach of contract.

Article 360 of the Civil Code 2015 stipulates: *"Where damage results from a breach of obligation, the breaching party shall be liable to compensate for the entire damage, unless otherwise agreed by the parties or otherwise provided by law."*

Accordingly, as a general principle, when liability for damages arises from a breach of contract, the breaching party must compensate for the entire loss. However, if the parties have entered into a prior agreement on the amount of compensation, then such agreement shall prevail. Under such an arrangement, the agreed compensation amount may be either greater or less than the actual damages suffered by the aggrieved party. Thus, the Civil Code of 2015 accepts the concept of liquidated damages or estimated compensation by agreement.

Conversely, the Commercial Law of 2005 does **not** recognize the parties' right to predetermine compensation through a liquidated damages clause. Clause 2 of Article 302 of the Commercial Law stipulates: *"The value of compensation shall include the actual and direct losses suffered by the aggrieved party due to the breach and the direct profits that the aggrieved party would have earned had the breach not occurred."*

According to this provision, compensable damages are limited to (i) actual and direct loss and (ii) direct profits lost, and the burden lies with the aggrieved party to prove the loss, its extent, and the direct profit forgone. The Commercial Law does not accept estimated or pre-agreed compensation determined at the time of contract formation.

#### 4.4 On the Exemption from Liability for Damages Due to Breach of Contract

The Civil Code of 2015 and the Commercial Law of 2005 also diverge in their provisions regarding circumstances under which a party may be exempted from liability for damages resulting from breach of contract.

Article 360 of the Civil Code 2015 reiterates the general principle that *"the breaching party shall compensate for the entire damage, unless otherwise agreed or provided by law"*. In addition, Clause 2 of Article 351 of the Civil Code 2015 provides that: *"Where a party fails to properly perform an obligation due to a force majeure event, that party shall not be held liable, unless otherwise agreed or provided by law."*

Pursuant to these provisions, the Civil Code recognizes three legal bases for exemption from liability for damages arising from breach of contract:

1. Exemption by agreement between the parties;
2. Exemption due to force majeure;
3. Exemption where otherwise provided by law.

In contrast, Article 294 of the Commercial Law of 2005 explicitly provides four circumstances under which the breaching party shall be exempt from liability:

1. Where a circumstance of exemption has been agreed upon by the parties;
2. Where a force majeure event occurs;
3. Where the breach is entirely caused by the fault of the aggrieved party;
4. Where the breach results from compliance with a decision of a competent state authority that could not have been foreseen at the time of contract formation.

#### 5. Recommendations for Improving Vietnamese Law on Compensation for Damages Arising from Contractual Breach

From the above analysis, it is evident that the provisions on compensation for contractual breach in the 2015 Civil Code and the 2005 Commercial Law remain inconsistent and partially conflicting. To improve the legal framework governing this matter, we propose the following recommendations:

##### *First, amend the provisions on compensable damages under the 2005 Commercial Law*

Currently, the definitions of compensable damages under the 2005 Commercial Law and the 2015 Civil Code are not aligned. While Clause 1, Article 361 of the Civil Code recognizes both material and moral damages as compensable, Clause 2, Article 302 of the Commercial Law only acknowledges material damages.

International legal instruments on contracts, such as the UNIDROIT Principles of International Commercial Contracts (PICC) and the Principles of European Contract Law (PECL), both recognize that compensable damages include not only material but also non-material harm.

For example, Article 7.4.2 of the PICC states<sup>1</sup>:

- (1) *The aggrieved party is entitled to full compensation for harm sustained as a result of the non-performance. Such harm includes both any loss which it suffered and any gain of which it was deprived, taking into account any gain to the aggrieved party resulting from its avoidance of cost or harm.*
- (2) *Such harm may be non-pecuniary and includes, for instance, physical suffering or emotional distress.*

Therefore, to better protect the lawful rights and interests of parties in commercial relations, ensure consistency between civil and commercial legislation, and bring Vietnamese law into greater harmony with international standards, it is recommended that Clause 2, Article 302 of the 2005 Commercial Law be amended to include compensation for moral (non-material) damages.

##### *Second, revise the regulation on the amount of compensation under the 2005 Commercial Law*

<sup>1</sup> <https://www.unidroit.org/wp-content/uploads/2021/06/Unidroit-Principles-2016-English-bl.pdf>

As previously analyzed, Article 360 of the 2015 Civil Code allows parties to agree on a predetermined amount of damages (liquidated damages), which may be either higher or lower than the actual loss incurred. However, the 2005 Commercial Law does not recognize such agreements.

In contrast, liquidated damages clauses are widely accepted in both civil and common law jurisdictions, including in the EU, the UK, France, Germany, the US, China, and in international instruments such as the PICC. Thus, Clause 2, Article 302 of the Commercial Law should be amended to permit parties to agree in advance on liquidated damages.

***Third, refine the regulation on liquidated damages under the 2015 Civil Code***

Article 360 of the 2015 Civil Code recognizes the validity of liquidated damages agreements. Under this provision, if, at the time of contract formation, the parties agree on a specific amount of compensation that the aggrieved party shall receive in the event of a breach, then upon the occurrence of such breach and resulting damage, the aggrieved party will be entitled to the agreed amount (even if the actual damage may be greater or lesser than the stipulated sum).

However, the 2015 Civil Code does not contain any provision allowing the court to adjust the agreed amount when it is excessively high or disproportionately low compared to the actual damage suffered. As a result, this may unintentionally lead to unfairness, whereby one party—by virtue of a stronger bargaining position—can impose a compensation clause that creates a substantial imbalance in contractual rights and obligations.

International instruments such as the 1980 United Nations Convention on Contracts for the International Sale of Goods (CISG) and the PICC contain mechanisms to limit excessive damages. Article 74 of the CISG provides<sup>2</sup>:

*“Damages for breach of contract by one party consist of a sum equal to the loss, including loss of profit, suffered by the other party as a consequence of the breach. Such damages may not exceed the loss which the party in breach foresaw or ought to have 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 possible consequence of the breach of contract”*

Similarly, Article 7.4.13 of the PICC states<sup>3</sup>:

- (1) *Where the contract provides that a party who does not perform is to pay a specified sum to the aggrieved party for such non-performance, the aggrieved party is entitled to that sum irrespective of its actual harm.*
- (2) *However, notwithstanding any agreement to the contrary the specified sum may be reduced to a reasonable amount where it is grossly excessive in relation to the harm resulting from the non-performance and to the other circumstances.*

The PECL, in Article 9:509, follows the same logic, granting courts the authority to reduce a stipulated amount of compensation if it is unreasonably high.

- (1) *Where the contract provides that a party who fails to perform is to pay a specified sum to the aggrieved party*

*for such non-performance, the aggrieved party shall be awarded that sum irrespective of its actual loss.*

- (2) *However, despite any agreement to the contrary the specified sum may be reduced to a reasonable amount where it is grossly excessive in relation to the loss resulting from the non-performance and the other circumstances.*

To better ensure fairness and balance in civil and commercial relationships, we recommend supplementing the Civil Code with provisions that empower courts to adjust liquidated damages where the agreed amount is disproportionately high or low in comparison to actual harm.

***Fourth, add a provision on exemption from liability for breaches resulting from government decisions***

Exemption from liability due to compliance with binding decisions of competent state authorities is recognized as a ground for excluding contractual liability. Such decisions are typically issued to serve public administrative functions and are binding upon affected parties.

In practice, contractual breaches due to government decisions frequently arise. For example, a provincial People's Committee may issue a directive suspending livestock trade in a region affected by disease. A seller operating within the affected area would then be unable to deliver goods as agreed, and should be exempt from liability for such non-performance.

However, exemption should only apply where such government decision was unforeseeable at the time the contract was concluded. If the parties were aware of the potential impact of a government decision and still entered into the contract, exemption should not be granted.

Currently, this basis for exemption is recognized under Point d, Clause 1, Article 294 of the 2005 Commercial Law but is not addressed in the 2015 Civil Code. Therefore, we recommend that Article 360 of the Civil Code be amended to include compliance with unforeseeable government decisions as an independent ground for exemption from liability.

## 6. Conclusion

Compensation for damages resulting from contractual breaches plays a crucial role in protecting the legitimate rights and interests of parties in contractual relations. It also contributes to maintaining legal order and promoting stability and security in civil and commercial transactions. However, as analyzed, the Civil Code of 2015 and the Commercial Law of 2005 contain numerous inconsistencies—particularly concerning the types of compensable damages (material and moral), the scope of compensation, the validity of liquidated damages clauses, and grounds for exemption from liability.

These discrepancies not only hinder the practical application of the law but also risk undermining the effectiveness of the legal mechanisms designed to protect injured parties. In the context of Vietnam's deepening integration into the global economy, building a unified, transparent, and internationally aligned legal framework is imperative.

Only when the rules governing compensation for contractual breach are consistent, coherent, and aligned with international standards can the law truly serve as an effective instrument for protecting lawful interests, preventing disputes, and fostering a stable and secure legal environment for commercial and civil activity in Vietnam.

<sup>2</sup> [https://uncitral.un.org/sites/uncitral.un.org/files/media-documents/uncitral/en/19-09951\\_e\\_ebook.pdf](https://uncitral.un.org/sites/uncitral.un.org/files/media-documents/uncitral/en/19-09951_e_ebook.pdf)

<sup>3</sup> <https://www.unidroit.org/wp-content/uploads/2021/06/Unidroit-Principles-2016-English-bl.pdf>

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