LEGAL IMPEDIMENTS TO INVESTMENT IN LAOS

by Terry Reid

Asia's most significant political and economic power group ASEAN has a new member, Laos.[1] To date most of the western world has found little enthusiasm to become involved in this land locked country which is one of the ten poorest nations in the world.[2] Economic development in Laos is in the infancy stages of a more remarkable transition, moving from a centrally planned to a market oriented economy. With the gradual opening of its doors to western visitors and encouraged communication by its senior bureaucrats with western nations, Laos has been quick to see the benefits that may result from an improved market economy.[3]

This paper examines some of the potential legal impediments which may arise for both domestic and foreign investors in Laos. First, we will consider the government's direction for the economy and secondly the legal and regulatory framework required to support this direction. Some specific examples of laws and decrees will be considered which may be relevant to potential investors. It is prudent to consider some brief geographical and demographical points before embarking on the examination of the possible impediments the legal system may provide in Laos's transformation.

BACKGROUND

Laos is a land locked country which has a population of 4.3 million inhabitants.[4] Mountainous terrain promotes a sparsely populated land. Laos lies in the middle of countries with significantly larger populations, ie. Thailand, Vietnam and China; it is also bordered by Cambodia and Myanmar. The key concentration of population is along the Mekong River with the capital of Vientiane having a population of approximately 500,000.[5] The population are therefore predominantly rural with a definite mix of different ethnic groups.[6] Laos is rich in natural resources which include water, minerals and timber. It is strategically well positioned with a huge consumer population at its disposal and it has a large and very cheap labour force. It has also enjoyed over two decades of stable political leadership.

Since the revolution in 1975 the Laos Peoples Revolutionary Party has ruled. The one party state is closely intertwined with the central committee of the Laos Peoples Revolutionary Party.[7] During the past twenty two years the government has shifted direction markedly. It commenced with a five

1 Laos together with Myanmar was admitted to ASEAN in July 1997.
2 See M Graham "Big Brother Little Brother" (1997) *Asia Magazine* 8 September 19-21, 19.
3 Under various technical assistance programmes senior Lao officials have been encouraged to study and visit other countries. New Zealand and Thailand have a joint funded educational institute in Thailand (The Mekong Institute) which supports courses for various levels of officials from Mekong countries.
4 Lao. EC Co-operation Guidelines 1994-1997, Information for the ALA Committee p.2.
5 Ibid.
6 Approximately 68 Lao "nationalities" are recognised by the government, however the population is divided into three ethnic groups:(i) Lao Soung-Lao - mountain summit dwellers. (ii) Lao Theung-Lao - mountain slope dwellers. (iii) Lao Loum-Lao - plain dwellers.
7 see Asia 1996 Yearbook *Far Eastern Economic Review* 156.

year central planning phase from 1975 to 1979 with the purpose of replacing the various sectors and state enterprises within a central plan framework. Agriculture co-operatives were quickly established and it was clear almost from the commencement of the new government that reforms were not going to achieve the desired transformation. Following 1975 there was an evaporation of US aid and many of the country's trained and key professionals, bureaucrats and business persons left the country. In addition to this, relations with Thailand were strained and this worked against achieving favourable trade results.[8] Inflation was a serious problem and by 1976 had reached 400 percent.[9] Prolonged drought periods had a profound affect on the rural sector and damaged the agricultural co-operatives.

The second stage of reform which was implemented at the behest of the IMF and Soviet Union concentrated on central planning with reform socialism. Taxes were reduced for agriculture in the hope that an increase in production would occur. Also State Enterprises were given greater freedom to generate profit. The aim was to get State Enterprises to generate their own growth and operate at a profit. Production did increase and there were other improvements but many other aspects of the economy were ill prepared for growth ie. the banking system. Foreign aid was used to fund almost all capital development and the country's infrastructure showed little improvement. The objective of initiating a centrally planned economy was bold but the reality was that it foundered. It was easier to implement changes and monitor them in the urban areas but in the rural areas this was difficult.

New Economic Mechanism

The most significant historical event in the country's history has been the implementation of the new economic mechanism.[10] The government made a decision that the economic performance of the country had improved very little since 1975. The influence of a charismatic party general secretary maintained that the state enterprises needed to take a lead role in the reform process.[11] The underlying theme of this advocacy was the adoption of management restructuring within state enterprises. The process was approved by the party congress and an ambitious economic reform programme was launched. Various laws/decrees and measures were introduced to enhance the implementation process.

Although committed to this new strategy the government moved tentatively at the outset. From 1988/89 the pace of reform accelerated tremendously.[12] In 1990 a decree was issued that converted state enterprises into new forms of ownership.[13] Agriculture, once again, was a key target for reform with an emphasis on diversification and private sector leadership. The government encouraged a move away from collectivisation to family

8 Thailand imposed temporary economic blockades in late 1975 and in 1977. This disrupted border trade significantly.

9 see R Vokes and A Fabella "Background and Recent Economic Developments" in *From Centrally Planned to Market Economies, The Asian Approach*, eds P B Rana & N Hamid, ADB Publication, 1996. p.12.

10 Adopted by the Fourth Congress of the Lao Peoples' Ruling Party, in November 1986.

11 General Secretary Kaysone.

12 In March 1988 Eleven decrees were published covering financial and fiscal reform, state enterprise autonomy, etc.

13 Decree No. 17, March 1990.

farms. This was complemented by various guarantees given to farming families in the leasing of land. Land ownership has been a controversial and perplexing issue for the government to contend with. Complex historical ownership structures has prevented any rapid change in land distribution to date. From the early stages of development direct foreign investment was seen as pivotal in the success of Laos under the new economic mechanism.

LEGAL AND REGULATORY FRAMEWORK

A significant effort was needed to enhance the existing legal framework to ensure that private sector growth would occur. There has been considerable progress made and the most important development was the adoption of a new constitution in 1991.[14] The constitution was to provide the impetus for private sector investment and it provides both guidelines and a clear basis for the adoption of laws which will further enhance the reform process.

The constitution establishes the political system and law making structure. It also places emphasis on the direction the socio-economic system is to take. Article 13 states:

"The economic system in Lao PDR is based on the multi-sectoral economy which goal is to relentlessly develop the production and the circulation of commodities, convert the subsistence economy to the market economy, bringing further development of the national economic basis and upgrading the pluriethnical people's material and spiritual living conditions."

Complementing this overall objective are that interests of investors (foreign and domestic) be protected under the constitution.[15] Although these provisions may provide some comfort, as we will see later in our discussion, the practice does not ensure the protection of interests and the constitution does not override any inconsistencies that may exist in other laws and/or decrees.

The law making structure attempts to establish a hierarchical arrangement. The constitution provides the base and is the supreme law of Laos. The National Assembly has the power under the constitution to make laws.[16] The President of the State is able to issue a state law between sessions of the National Assembly.[17] Such a law would then require ratification at the next session. The most common form of rule takes the form of a decree. Decrees are issued by the Council of Ministers, individual ministries or other agencies.[18] They are issued and are considered a ***"test run"*** of a law. The decree has force, as if it were a law, and during the testing period inconsistencies and loopholes are determined and opinion is gauged in order to produce a modified law that is effective in its application. Often decrees will continue to be in force for long periods of time without becoming laws. The potential problem of conflict has not been addressed in the constitution and does not appear in practice to have manifested itself at this stage.

14 The Constitution of the Lao Peoples Democratic Republic was passed by the National Assembly on August 14, 1991.
15 See Articles 14-15.
16 Section IV, Articles 40-51.
17 Article 53.
18 Article 57.

Aside from the laws and decrees, agencies and ministries will draft and adopt their own regulations. These regulations allow for the practical implementation of the laws and decrees. They are intended to be operational in nature but this has generated some difficulties. Often regulations are drafted which conflict with the laws and there is no form of resolution of that conflict. Practices outlined in the regulations are often hampered by limitations and inconsistencies within the laws and decrees. Although regulations can be very helpful, they appear on occasions to be given cursory consideration by the ministry or agency responsible for their implementation.

Of the above, only the laws and decrees are published and many are not translated or distributed to the public. Therefore, those wishing to access the current laws and decrees will find it difficult unless they seek assistance from local law firms.[19] The introduction of an Official Gazette was commenced in 1993. The objective was to publish the laws and decrees as they were passed in the Lao, English and French languages. The introduction added to the national dissemination of laws and decrees. Also published in the Official Gazette were some of the decisions of the courts which may highlight a desire to develop a consistent approach to cases heard by the courts and some system of jurisprudence. The Official Gazette was supported by the Swedish International Development Authority (SIDA) under the ***"strengthening the rule of law project"***. Unfortunately a withdrawal of funding has brought about a halt to publication of the Gazette and after a few issues its future is in doubt.

A clear programme of laws and decrees to be implemented has been established. Since 1990 a number of laws and decrees have been enacted which are of particular significance to investors. These include the Contract law,[20] Property law,[21] Inheritance law,[22] Insurance law,[23] Labour law,[24] the Code of Civil Procedure,[25] Business law,[26] Secured Transactions law,[27] Bankruptcy law,[28] Decree on the Settlement of Economic Disputes[29] and Financial Investment law.[30] A number of these raise important issues relating to investment and we will consider them later in this paper.

The Rule of Law

An examination of business practices in Laos shows that there are major difficulties with the interpretation and enforcement of the newly drafted laws and decrees. This would appear to be an appropriate response given the relatively rapid drafting and implementation process that has occurred. The bureaucrats who have input into the drafting of new laws have an opportunity to discuss and evaluate alternatives. However those who are outside the drafting process have little opportunity to provide feedback or

19 A handful of local law firms operate out of Vientiane.
20 Adopted 27/6/90.
21 Adopted 26/6/90.
22 Adopted 27/6/90.
23 Adopted 29/11/90.
24 No. 24/PR adopted 21/4/94.
25 Adopted 29/11/90.
26 No. 3/94 adopted 18/7/94.
27 No. 07/94 adopted 14/10/9.
28 No. 06/94 adopted 14/10/94.
29 No. 106/PM dated 15/7/94.
30 Adopted 13/3/94.

discussion and yet are expected to comply with them. Automatic acceptance of new laws is an inappropriate and unrealistic expectation. The raft of legislation has heralded economic change to the Laos economy and it has had a profound impact on the social development of the country. In many parts of Laos there is an absence of awareness of the new laws or their impact on different socio-economic groups.[31] The courts themselves have been forced to accept the new structure under the Constitution and interpret a continuous wave of new laws and decrees.

For those investors seeking refuge amongst the laws and decrees, the inconsistencies aside, the refuge may not be as safe as it appears. Even a meticulous adherence to procedures and rules defined by the laws may result in an unexpected outcome in the event of litigation or even in 'street level' practice. It will clearly take time for Lao users to develop confidence in the law and for the courts to uphold them in the manner the government intends. There has been considerable argument for a promotion of a rule of law project to enhance the acceptance of the legal system and its laws amongst the general populace.

The current ongoing rule of law project has resulted in a number of positive initiatives.[32] These include:

- Reorganisation and training of the judiciary.
- Clear civil and criminal procedures being developed.
- Additional trained staff to be utilised by the law school.
- The re-establishment of the Laos bar.[33]

The traditional view of rule of law from a western perspective may be highly inappropriate for Lao society.[34] The lack of government intervention in the economy may be some time away and it may be that process and improved social conditions will be the only factors that enhance the general acceptance of the new laws and legal system.

FOREIGN INVESTMENT AND MANAGEMENT

To enhance and manage foreign investment in Laos a Foreign Investment law was passed in 1988 and together with two implementing decrees passed in 1989, formed the base for the regulation of foreign investment.[35] A clear institutional structure was established which would manage all foreign investment and the task of managing this process rested with a foreign investment management committee (FIMC). It had the responsibility of authorising licensing of foreign investors and monitoring performance and imposing any conditions that were considered necessary. The Foreign Investment law guaranteed protection of investors' interests and taxation rates etc. After four years of operation there had been a good deal of foreign investment inflow but there were some clear problems in the process.[36]

31 Outside of Vientiane, the majority of the population are unaware of new laws or the changes in direction which have occurred.

32 SIDA have been responsible for managing the rule at law project . This is a jointly funded project - Swedish and Lao governments.

33 S Beling *Report on Rule at Law Project* February 1994.

34 See M Smith "Private Law and Public Control of Commercial Activity in Japan - The Role of the Codes", in *Commercial Legal Development in Vietnam: Vietnamese and Foreign Commentaries*, ed. J Gillespie, Butterworths, Asia 1997 p. 261 at 262.

35 see R B Sunshine, *Managing Foreign Investment - Lessons From Laos*, East West Centre, Hawaii, 1995 p.11.

36 By the end of 1990, ninety one investments had been approved, totalling US$143 million in commitments or proposed capital value see Sunshine, supra, n 35, p.13.

Licence applications, in many cases, took a long period of time to approve and the terms and conditions attached to these varied significantly. There was still a marked absence of ***"name investors"*** and the government decided to set up an investment reform programme to assist in the attraction of investment and subsequent regulation of same.

After much research and consultation a new Foreign Investment law was passed. The law on the promotion and management of foreign investment in the Lao PDR was adopted by the National Assembly in March 1994.[37] The overall objective of the new law was to encourage foreign persons to invest in Laos, and to guarantee protection of property investment in Laos under the laws and regulations of Laos.[38] The law outlined the investment vehicles which may be utilised by foreign investors, these are:

(i) A joint venture with one or more Lao investor; or

(ii) A wholly foreign owned entity.[39]

There are a wide range of benefits, rights and obligations applicable to foreign investors under the new law, these including the following:

1. Protection of foreign investment and property by the government.
2. Priority of labour recruitment must be given to Lao citizens. Foreign personnel can be employed with approval by the relevant authority and there is an obligation on training Lao workers.
3. Bank accounts must be opened in Lao currency and foreign currency with a Lao bank or a foreign bank established in Laos.
4. Tax rates are set at a flat rate on net profit. (In certain cases exemptions may be granted.)
5. All disputes if not resolved by consultation or mediation must be referred to the economic disputes office or a foreign alternative if that can be agreed upon.[40]

The FIMC continues to exist under the 1994 law and has the overall brief of promotion and management of foreign investments within Laos.[41] The FIMC will licence and monitor all foreign investment.[42] In an attempt to streamline the previous system, time limits are placed on the processing of applications.[43]

A desired approach in the drafting of the new law was to emphasise harmonisation of all commercial laws. As there had been many laws introduced since the original 1988 Investment law the government desired a complete framework which fully applied to foreign investors in the same way it applied to domestic investors. The FIMC also advocated the adoption of standard form contracts in certain areas of investment eg. mineral investment contracts.[44] This would provide a degree of certainty for all parties involved and would provide some comfort to the Lao parties who

37 No. 01/94 adopted 14/3/94.
38 Articles 2, 3.
39 Articles 4-9.
40 Section 3, Articles 10-21.
41 Article 22.
42 Article 23.
43 Articles 26-27.
44 Sunshine, supra, n 35, p.134.

were unfamiliar with many of the intricacies of commercial contracts. Standard form contracts read together with the Contract law would uplift the level of confidence in the new commercial law framework.

The FIMC also wanted to be seen by all investors as applying the rules and imposing conditions in a consistent manner. Obviously large scale foreign investment requires much more regulation and tailoring but smaller investors must not be seen to be disadvantaged by their size. The FIMC has been a pivotal body in encouraging foreign investment in Laos but more work needs to be done. A further key agency was established in early 1996 to further enhance the approval and monitoring process, the committee for investment in foreign economic co-operation (CIFEC) which comes under the direct responsibility of the Prime Minister's office. This further indicates the commitment by the government to promote long-term foreign investment in Laos.[45]

LEGAL ENTITIES

For those wishing to engage in business in Laos there are a number of entities which have been established by the National Assembly under the Business Law 1994.[46] Many of the entities are based on the traditional western model. The Business Law has as its objective the promotion of all economic sectors and the transformation of the Laos economy according to market forces.[47] The caution in this objective is the government's decision to adjust the market forces as it deems appropriate.[48] All domestic and foreign investors will receive general protection in respect of their interests under the general law of Laos.[49] The Business Law establishes two forms of enterprise; sole trading enterprises and companies.[50] In Laos there are three forms of company:

- Partnership company.
- Limited liability company.
- Public company.[51]

The basis for each of the above companies is the contract that exists between the shareholders.[52] The contract which details the contribution of capital is enforceable under the Contract Law which was promulgated by the National Assembly in 1991.[53] All companies will have articles of association which will determine the internal management structure and also deal with dissolution, liquidation and methods of dispute resolution.[54] There are further general provisions which relate to companies and the one of note is the requirement to create a reserve fund which is created from the deduction of 5 percent to 10 percent of the company's net profits.[55]

45 Additional Technical Assistance Programmes are to be aimed at further enhancing the current Investment law framework and encouraging direct foreign investment.
46 No. 42/PDR adopted 13/8/94.
47 Article 1.
48 Article 13 lists a number of business sectors which are considered important to national security, the economy or society and must therefore be closely controlled by the State eg. electrical power, telecommunications, mines and minerals, liquor, smoking tobacco.
49 Article 2.
50 Article 4.
51 Article 21.
52 Article 22 - similar to Articles of Association.
53 Supra, n 20.
54 Article 27.
55 Article 24.

The reserve fund serves as a means to increase the company's capital. If there is an increase in the number of shares, existing shareholders have a pre-emptive right to take the new shares before any new shareholders.

Partnership Company[56] — this type of company is analogous to the traditional partnership in English law, the use of these partnership companies causes confusion amongst those that are familiar with the historical distinction between partnership and company. The basis of the relationship of shareholders is one of trust and it is made clear that all shareholders are jointly and severally liable for the company's obligations. To ensure there is no confusion for those entering transactions as such, mention of the words ***"partnership company"*** must be included in the company's name. It would appear the partnership company entity is not a popular form utilised by investors as such entities are difficult to find in Laos.

Limited Liability Company[57] — the most popular form of business entity is a limited liability company which requires two or more founding shareholders and shall not exceed twenty shareholders in number. There is a distinction drawn between shareholders and business persons with the former not having the legal status of a business person. The English law principles of limited liability attach to limited liability companies in Laos. There appears to be a little confusion in the law in that it provides for one person companies who are able to limit their liability in the usual manner, such companies have minimal capital requirements.[58]

Public Companies[59] **and State Enterprises**[60] — public companies are provided for under the Business Law where the initial capital is provided by seven or more founding shareholders.[61] As with the limited liability companies shareholders do not need to have business person status.[62] A board has the responsibility of management of the public company and there must be at least one workers' representative on the board.[63] All directors must be shareholders with the exception of the workers' representative.[64] There are extensive provisions which relate to public companies and the shareholders have the same rights and duties as the shareholders in a limited liability company.

Part IV of the Business Law makes provision for State Enterprises which are defined in a broad manner and these are divided into State Enterprises and State-mixed Enterprises. A ***State Enterprise*** is simply a business entity in which the state establishes and invests by itself or in a joint venture with another enterprise in which the state invests 51 percent or more.[65] The state enterprise will take on the form of a limited liability or public company but specific provisions will apply.[66] A state enterprise will be responsible for its debts and the Minister of Finance will represent the government in the position of capital owner of the state enterprise.[67] The responsibility

56 Section II, Articles 38-44.
57 Section III, Articles 45-59.
58 Article 57 - 5 million kip.
59 Section IV, Articles 60-76.
60 Section V, Articles 77-90.
61 Article 60.
62 Ibid.
63 Articles 64-71.
64 Article 65.
65 Article 78.
66 Article 79.
67 Articles 79-80.

for the management of the state enterprise will rest with a board of directors which may vary in number from three to eleven.[68]

A state mixed enterprise is a business entity established on the basis of a joint venture between another type of enterprise within the state and the state will invest 51 percent or more of the total of capital, but less than 100 percent.[69]

It should also be noted that the Business law makes provision for collective enterprises which are business entities established by a collection of two or more families to conduct profit making activity.[70] Such enterprises are defined as co-operative joint ventures which are established by local farmers or small traders and are conducted on a voluntary basis.[71] The individual members contribute to their capital, labour, equipment and services with the objective of making a profit. There would appear to be a lot more flexibility in the operation of collective enterprises, the law does state that the administration of such entities should comply with the provisions applicable to public companies.[72] In practical terms such co-operatives often operate according to long established rules and customs which are unique to the geographical area and the families involved.

Registration

A final point that should be raised is the requirement of registration of the entity. This is simply the adoption of a similar essential requirement under English law. If you wish to establish an enterprise of any type you need to submit an application for establishment of registration to the relevant ministry.[73] An entity must only register with the government ministry which has jurisdiction over the particular commercial activity the entity is involved in.[74] If it is difficult to determine which is the correct ministry then, the Ministry of Finance will provide the appropriate guidance.

To ensure some consistency of registration practice the business law establishes an ***"enterprise registry book".***[75] Final approval of the entity will be placed in the registry book which will contain all the relevant contracts and information relative to each company. Each entity receives a number and is registered in a sequential manner. At this point the entity is also registered for tax purposes and if it does not commence activities within one year its registration shall lapse.

It is unclear as to how much of a public document the registry book is. There is nothing in the Business Law which will allow a member of the public or for that matter an interested party from searching the registry book. Probably the best approach is to seek the approval from the appropriate ministry concerned in an endeavour to obtain the information needed. This would in all probability be a protracted and difficult task. Investors and lenders must pursue the need to ensure the public availability of the registry book in order to facilitate all business and finance transactions.

68 Article 82.
69 Article 88.
70 Article 91.
71 Article 91.
72 Article 93.
73 Article 16.
74 Article 17.
75 Ibid.

SECURITY AND ENFORCEMENT

As stated earlier, as local financial institutions have become involved in financing investment in Laos there has been considerable nervousness on their part when ascertaining the types of security which should be taken. Following the new economic mechanism in 1986 one of the more pressing areas of reform was security and its subsequent enforcement. The legal framework was not sufficiently advanced to enable financial institutions to enjoy the comfort of being able to perfect a security.

The passing of the Secured Transactions law in 1994 commenced the first phase of improving the legal environment for security enforcement which it was hoped would encourage investment in business throughout the country.[76] The major objective of the Secured Transactions law was to place a greater emphasis on contractual obligations and encourage the use of various forms of property as security.

Before considering the available types of security it is necessary to consider some of the difficulties that arise as far as different assets are concerned. For the majority of assets (ie. chattels and land) there are, as yet, no established and reliable systems of title identification.

Chattels — chattels do not necessarily require registration and even if registration is required, for example in the case of a motor vehicle, it is common for the owner not to satisfy this compulsory requirement, or often the registered owner may not be the true owner. Sometimes chattels are registered in the names of groups of individuals. Insurance is Laos is at an early stage of development and the majority of chattels of any value are uninsured. This clearly adds to the risk for the lender but at this stage it is an unrealistic expectation to insist assets be insured.

Land — as a security land provides a huge problem in that no guaranteed system of land titling exists.[77] Given the centuries of upheaval the Lao people have experienced it is difficult to establish correct title over land. Part of the New Economic Mechanism was to develop markets for land which would in turn create enforceable land use rights. This would facilitate the use of land as a collateral which would in turn enhance and encourage private investment. As a corollary to the objective, sustainable management of land has been advanced as a desirable outcome of the reform.

The government, through development of the legal framework, set about creating a stable legal environment for transfer and use of land. The Property Law granted the land to the national community, the State then is able to grant to individuals or other entities the right to control, use, transfer or assign the land.[78] A subsequent decree passed in 1992 modified land rights and ownership principles and enabled land owners and users to offer land as collateral to banks.[79] Non-residents or non-aliens who are approved investors in Laos are able to obtain usage rights through leases and concessions.[80]

76 No. 07/94 adopted 14/10/94.
77 The English equivalent to indefeasibility of title does not exist in Laos.
78 Adopted 27 June 1990, Article 3.
79 No. 99/PM, December 1992.
80 Implementing Decree for the Law on the Promotion and Management of Foreign Investment in the Lao PDR adopted June 1994, see Article 12.

Types of Security

The Secured Transactions law defines three broad categories of securities. In their order of priority they are:

- Security created by law.
- Security created by court decision.
- Security created by contract.[81]

Security Created by Law — this security receives priority over all other types of security and is defined under the law as *"the assurance of debt repayment as determined by law based on principles of humaneness and general national interest"*.[82] This appears a rather vague and difficult definition to contend with and it could mean that securities will not be enforced if such an action would prove harmful or not in the interest of the borrower.

An example given in the law itself is where debts arise from the labour of workers. This would seem to suggest that employees could possibly take priority over secured creditors in a competition for the employer's assets.[83] Any salary owed to workers would rank ahead of other creditors.

Other examples of such security can arise under the Bankruptcy law[84] where taxes, royalties and other payments and debts payable to the government rank ahead of all other creditors.[85] This would amount to a security created at law. In the event of the company owing large amounts for wages and/or taxes, the equity in a secured asset could be diluted significantly. The practical application of the security created by law is as yet to be considered by courts in Laos and so the uncertainty will continue.

Security Created by A Court Decision — this security which ranks in priority ahead of a contractual security is defined as "the guarantee of debt repayment as provided for in a court decision or a decision by the economic dispute resolution tribunal which has been certified by a court decision".[86] Once again, the practical application of this article causes significant anguish for lenders. After working through the dispute process the court may order the seizure or sequestration of an asset. At the hearing of the Economic Dispute Resolution Tribunal, a security holder may not always be represented and often the existence of a prior or subsequent charge will not be taken into account by the tribunal. This leaves the lender in the unenviable predicament of having legal perfection of a security and finding that the priority has been displaced by a subsequent order by the tribunal in respect of the asset.

Security Created by Contract — this category of security is the most common found in Laos. It covers all securities taken by agreement between the parties. By creating a security by contract the security holder will ensure

81 Secured Transactions Law, Article 3.
82 Article 5.
83 Ibid.
84 No. 06/94 adopted 14/10/94.
85 Article 44.
86 Secured Transactions law, Article 6.

she/he has priority over subsequent secured creditors and unsecured creditors. The three forms of contractual security are:

- Contracts secured by moveable assets.[87]
- Contracts secured by immoveable assets.[88]
- Contracts secured by an individual or a juristic entity.[89]

Moveable Assets — the security over moveable assets can be of three types:

1. A deposit of goods where the debtor transfers his or her goods into the possession of the creditor, who then has the responsibility of taking care of the goods unless the debt secured by the goods is satisfied.[90]
2. A documentary deposit. The distinguishing feature of a documentary deposit is that only the title documents to the assets are transferred to the lender.[91]
3. A deposit of inventory which is defined as ***"the use of a security instrument (for stored goods) to secure the repayment of debt to a creditor".***[92] It is unclear as to what would constitute a deposit of inventory.

Immoveable Assets — it is possible to grant a charge over immoveable assets such as land, factories, houses etc by executing a charge and providing evidence of legal title to the assets.[93] There are some specific requirements as to the execution of the security in the case of land where the documents must be signed in front of a notary or a village chief at the place where the asset is located.[94] The notary system in Laos is not very well developed so the majority of transactions are certified by the village chief. The major problem encountered by the lender is the falsification or inaccuracy of title deeds. As stated earlier, with no guaranteed system of registration it is very easy for creditors to advance money against land as security that is owned by another party. The ***"Lao PDR Land Titling Project"*** will assist in the elimination of much of the uncertainty but this will be some years away.[95]

Guarantees — it is possible under the Secured Transactions law to take a guarantee from an individual or business entity as security.[96] The guarantor is able to guarantee the entire debt or a portion of the debt. The obligation will be for the principal only unless the guarantee document makes provision for the charging of interest.[97] There is an obligation on the creditor to seek repayment from the debtor failing payment from the guarantor.[98] Debtors have an obligation to keep guarantors informed about the debt and its status.

It is possible to take a guarantee from joint guarantors and each will be jointly and severally liable for the debt.[99] A guarantor will be released

87 Section II, Articles 10-18.
88 Section III, Articles 19-24.
89 Section IV, Articles 25-29.
90 Article 12.
91 Article 15.
92 Article 17.
93 Article 19.
94 Article 20.
95 US$30 million is being provided to support a Land Titling Project in Laos. The implementing agency being the Ministry of Finance. It is the first stage of a programme designed at providing secure land ownership - compiling a cadastral mapping system and developing land administration and valuation systems.
96 Article 25.
97 Article 26.
98 Ibid.
99 Article 27.

from the guarantee and repayment of the debt if there has been some alteration to the contract between the debtor and creditor.[100] Also, if the guarantor looses their mental capabilities or dies his/her successors will be bound as per the Secured Transactions law.[101]

Secured Transactions and Issues Arising

The Secured Transactions law has made progress in defining different types of securities that may be given by investors as security. As can be seen, the law does provide a number of options for financial institutions but there are some problems with the law which make a number of the options unattractive. For example, the deposit of goods means that only goods which can easily be held in the possession of the bank can really be deposited. The most common types of goods subject to this type of charge are jewellery and small personal items of value. As the value of the goods has to be established when the goods are deposited this causes some problems as often the goods have a limited market and valuation is especially difficult.[102]

The other problem with such a security is that the responsibility to take care of the goods rests with the bank.[103] Any loss or damage is at the cost to the bank. It is suggested that some form of insurance, the premium payable by the debtor, may assist in alleviating this concern. However it should be noted that insurance may not be easily obtained and the premium may be excessive, given that the goods are not in the possession of the owner. In the event of default by the debtor the goods may be difficult to sell and this has been confirmed by financial institutions.

With the deposit of documents , a more attractive security option is presented. The deposit is similar to a mortgage over chattels that operates in other jurisdictions. The major flaw in taking such a security is the relatively ineffective system of registration. Although the law makes it clear that the debtor is unable to further charge the asset and a priority is created in favour of the creditor.[104] It is unclear as to when the priority is created, ie upon registration, and the biggest disadvantage is that the creditor is unable to check whether or not the asset has been previously charged. This once again emphasises the need to put in place a more reliable system of registration that will provide some comfort for those using this type of security.

There is very little detail in the law regarding the granting of a security over stored goods by depositing the security instrument for the stored goods. There are the standard problems with securing goods in Laos, as exists in other jurisdictions. If the legal interest in the goods is transferred to the lender, this has the effect of denying the debtor the right to dispose of the goods in the ordinary course of business. The lender may also be liable for storage costs, such costs may be quite high especially if the goods are of a perishable nature. There also exists the difficulty of a bona fide purchaser taking possession of the goods and being effected by the lender's priority. The Secured Transactions law does not provide detail as to how such

100 Article 29.
101 Article 28.
102 Article 13.
103 Article 14.
104 Article 16.

problems can be alleviated and what the rights of the different parties are should such problems arise.

The most attractive alternative is not to focus on the rather unworkable Deposit of Inventory and pursue an argument for the development of a charge similar to a floating charge used in many other economies. Such a security would make it easier to take a charge over assets such as stock, crops, etc.

It would appear to be difficult to use a ***"floating charge"*** under the current law. The deposit of documents may permit the depositing of documents that would give a charge over a mix of assets that would ordinarily be covered by the broader floating type of security. There is the restriction on the debtor of transferring such assets, although the restriction appears to apply to transferring to creditors only. This being the case it may be possible to draft a document that resembles a floating charge and would fall under the deposit of documents requirement. However, as a word of caution, such a security would certainly be unique in Laos and may infringe against the spirit of the Secured Transactions law and consequently a lender relying on such a document may have difficulty in enforcing same.[105] The problems of registration would continue to cloud the reliability of a 'floating charge' as it does all securities.

As foreign investors cannot directly own land they cannot give an effective security over the land. Joint venture companies will not own the land, the Lao partner will be the owner and therefore is the only party capable of giving the security.[106]

Priority and Void Securities

The priority set down in the Secured Transactions law indicates that a priority according to law is ranked first. It is concluded that such a description implies that a security created according to the law would rank first. Registration is required and priority may be displaced if the asset secured is not the property of the debtor or the debtor wishes to terminate the registration , with the effect of displacing the creditors priority, if the security was made incorrectly. This is a major problem for lenders, if the security is not taken in the correct manner, it may be made void at the whim of the debtor. If the debtor misrepresents the asset as being owned by him or her and it is not, then it will be void. The debtor may then be dealt with under the law but this will prove of little benefit to the creditor. As stated earlier, a reliable system of registration would alleviate this problem. The lender, if it fulfils all the requirements of the law, and verifies title in the asset by reference to the register, should get a good security. As it stands at present, the lender doing all it can to perfect its security may still find it has an imperfect or unenforceable security.

COMMERCIAL DISPUTES

The Decree on Settlement of Economic Disputes covers any dispute that occurs during the carrying out of commercial activities.[107] This is

105 There may be some difficulties in circumventing the requirement that all goods must be described in the security. see Property law Article 6.

106 State Enterprises under the Property law cannot give a charge over land or any other assets they may own. See Property law Article 6.

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especially in the area of agricultural and industrial production, trade, services and other economic activities.[108] The Decree has as its principal objective, the settlement of economic disputes. In order to achieve this objective the Office of Economic Disputes (OED) is established under the Decree.[109]

The office has an obligation at law to deal with all disputes promptly, in confidence and with absolute impartiality.[110] Before the OED is able to deal with a dispute it has to be sure that the parties have consented to the process.[111] There are a number of factors that can be taken into account when disputes are considered by the OED; these include the following:

- The Decree and the processes outlined in same.
- Any laws or decrees that relate to the transactions eg the Secured Transactions law.
- Transactions between the parties.
- Business Practices.
- Impartiality is essential.[112]

There is a time limit on appeals of decisions made under the decree of three years from receipt of the decision.[113]

Procedure

A request must be made and forwarded to the OED. The request will include a number of details, consent and the desired mode of settlement must be stipulated.[114] The alternative modes are Conciliation or Arbitration. The OED will consider the request and will advise within thirty days the claimant as to whether the OED will hear the matter.[115] The debtor is informed and this is done within time limitations set down in the decree. As stated there are two modes of settlement, Conciliation and Arbitration.

Conciliation — the objective of the conciliation process is to provide alternative solutions to the problem as presented by the conciliator.[116] There is a set procedure for appointment of conciliators and in certain cases a right to challenge an appointment will be available.[117] The parties can agree to have one conciliator or a panel of three. The procedure is aimed at a prompt settlement and must be concluded no later than fifteen days after the appointment of the conciliator.[118] The hearing is attended by both parties and can come to an end if:

(i) One or both parties fail to participate without valid reason.

(ii) The parties fail to reach agreement.

(iii) The parties reach an agreement.[119]

If an agreement is reached it is committed to writing and signed by the parties and the conciliator. The agreement is binding on the parties.

108 Article 11.
109 Ibid.
110 Article 7.
111 Article 20.
112 Article 6.
113 Article 10.
114 Article 19.
115 Article 20.
116 Section II, Articles 21-26.
117 Article 22.
118 Article 23.
119 Article 24.

Arbitration — Arbitration is seen as a more severe method of dealing with disputes. With this method an arbitrator acts in a judicial fashion and makes an award to resolve the dispute. The arbitral award will be binding on the parties with a limited right of appeal to the courts.[120]

The parties will either consent to an arbitration after the dispute arises or it may be stipulated in any earlier agreement they may have entered.[121] The procedure for appointment of arbitrators is the same as for conciliators.[122] There is also an obligation to deal with the dispute in a prompt fashion although more complex disputes have a time limit of 18 months imposed.[123] At the hearing all the parties will have an opportunity to present evidence, this may be in the form of documentary evidence or oral witnesses.[124] The arbitrator also has the jurisdiction to carry out his or her own investigation and call his or her own witnesses.[125]

Following the hearing the arbitrator will make an award within 30 days. If there is a panel of arbitrators then it must be a majority decision.[126] The award will take effect from the date of its receipt. The award will be binding on the parties but if a party is dissatisfied, it may lodge an appeal with the Court. It is possible for the parties to reach an agreement prior to an arbitral award being announced. If this occurs the arbitrator will draw up an agreement and it will be signed by the parties and it will be binding.

Costs

The costs of both conciliation and arbitration may be considerable. For example they may include:

- Fees of OED.
- Honorarium of experts.
- Expenses for witnesses.
- Scale fees depending on the amount of the dispute payable to the State.
- Lawyers expenses.[127]

Under a conciliation, expenses will be shared equally whereas under an arbitration the arbitrator will determine how expenses will be paid.

The overall objective of the Decree on Settlement of Economic Disputes, that of a rapid, fair and effective regime for the settlement of commercial disputes, is not carried over in the daily operation of business. Although strict time limits are set down these are often not adhered to and parties are seemingly delayed for inordinately long periods of time. The general feeling amongst financial institutions is that the economic disputes regime should be avoided as results are difficult to achieve and often decisions are not in their favour.

It may be that as those involved in hearing disputes become more conversant with the Decrees and the types of disputes that arise, the objective may be achieved. There is no evidence of a system of precedent being in place so inconsistencies are well documented. If a more uniform approach to settling disputes is not adopted, confidence may be undermined to the point that the Decree becomes redundant in a practical sense.

120 Article 38.
121 Article 27.
122 Article 28.
123 Article 29.
124 Article 30.
125 Ibid.
126 Article 31.
127 Article 42.

One point that should be noted is the issue of governing law and jurisdiction. It would clearly be in the interests of foreign investors to nominate an alternative governing jurisdiction although local Lao investors will be subject to the Decree.[128]

CONCLUSION

Our brief discussion of the legal and regulatory framework which covers aspects of investment in Laos, reveals a desire by Laos to create a stable legal environment for investment. This is evidenced by the wide range of Decrees and laws passed since the embracement of the New Economic Mechanism in 1986. Future plans to continue the development of the framework further endorses the objective of stability.[129] It would be incorrect to state that the laws and decrees provide parties with a clear protection of interests and generate a climate offering comfort. There are many loopholes, ambiguities and inconsistencies, however, what appears to be paramount is the government's aim to attract investment and provide a legal environment that encourages that aim.

As agencies and those responsible for implementation become conversant with new policies, procedures and practice, the many delays and frustration that currently pervade the business arena will abate. There is an emphasis on providing training in all sectors and this is crucial to achieving an acceptance of the new laws. Such an acceptance will only occur through improved processes and ultimately better living conditions for the majority of the population.

Those wishing to invest in Laos should always take the usual precaution of employing strict due diligence procedures. Much time should be taken in ascertaining what requirements should be satisfied, ie. Licenses and authorisations etc. When entering business arrangements the drafting of contracts should be carefully considered and provision for many of the difficulties should be provided for.

The legal framework has experienced rapid development since 1986 and an acceptance of the laws will clearly take time. Laos is a country rich in potential and it has travelled a long distance in a short time. All investors must ensure that the needs of the Lao people and the importance of their customs are taken into account when doing business in Laos. Such an approach must be paralleled by policy makers and draftspersons.

128 Under the Secured Transactions law a security over immoveable assets located in Laos must be made in Laos (Article 20). The current practice seems to be that such a security will be executed, certified and registered in Laos and will be governed by Lao law.

129 Future plans are to enact an Environmental law, Commercial law and Bills of Exchange law.