



**PROCEEDINGS**

# **ICYREB 2023**

**THE 9TH INTERNATIONAL CONFERENCE FOR YOUNG  
RESEARCHERS IN ECONOMICS AND BUSINESS**

**Volume 3**



**NHÀ XUẤT BẢN KINH TẾ  
TP. HỒ CHÍ MINH**

**October 26 - 27, 2023  
Ho Chi Minh City**



# PROCEEDINGS **ICYREB 2023**

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RESEARCHERS IN ECONOMICS AND BUSINESS**

## **Volume 3**

## TABLE OF CONTENT

**HOW DO CELEBRITY CREDIBILITY AND OVER-ENDORSEMENT AFFECT ONLINE CELEBRITY BRAND EQUITY ON TIKTOK AND FOLLOWERS' BOOKING INTENTION?.....9**

*Tran Thi Kim Phuong, Ho Mai Thao Nhi,  
Nguyen Ky Vien, Do Thi Thu Uyen, Tran Trung Vinh*

**THE IMPACT OF CULTURAL IDENTITY AND ATTITUDE-TO-BRANDS ON CUSTOMER LOYALTY: A CASE STUDY FROM FOREIGN FRANCHISING BRAND IN VIETNAM CONTEXT .....10**

*Hoang Vu Phi Long, Bui Thi Thao Hien*

**THE IMPACT OF TRANSFORMATIONAL LEADERSHIP ON EMPLOYEE ENGAGEMENT OF GENERATION Z: THE MODERATING ROLE OF OPTIMISM AND RESILIENCE .....11**

*Nguyen Thi Anh Tho, Pham Thi Khanh Ly, Tran Minh Quang,  
Tran Thien Huong, Vuong Quoc Anh, Nguyen Tuan Long*

**THE PATHWAY FROM ADVERTISING APPEALS TO BEHAVIORAL INTENTION UNDER THE MEDIATING ROLE OF SELF-EXPRESSIVE AND THE MODERATING ROLE OF LGBTQ+ ADS.....31**

*Loan Pham Thi Be, Dinh Tran Dinh, Ha Le Thi Khanh,  
Thao Dinh Thi Phuong, Thao Le Nguyen Phuong*

**DETERMINANTS OF CUSTOMER SATISFACTION: THE MEDIATING ROLE OF PERCEIVED VALUE IN TIKTOK SHOP IN THE VIETNAM MARKET .....32**

*Tran Nhat Vi Vu, Thi Thao Hien Bui*

**TRADE CREATION AND TRADE DIVERSION EFFECTS OF CPTPP ON VIETNAM TEXTILE AND APPAREL EXPORT: AN APPLICATION OF WITS-SMART SIMULATION MODEL .....51**

*Pham Ho Ha Tram, Tran Phuong Dung*

**TRADE EFFECTS OF NON-TARIFF MEASURES EMBEDDED WITH SUSTAINABLE DEVELOPMENT GOALS: EVIDENCE FROM FISHERY EXPORT TO EU MARKET .....52**

*Nguyen Bich Ngoc*

**EXPERIENTIAL LEARNING BASED ON FIELD TRIPS IN TOURISM  
HIGHER EDUCATION IN VIETNAM .....53**

*Nguyen Thi Quynh Trang, Le Thi Bich Hanh,  
Nguyen Thi Kim Ngan, Nguyen Thi Hao, Nguyen Thi Thu Huyen*

**DETERMINING COMPENSATION FOR EMPLOYEES ENTERING INTO  
NON-COMPETE AGREEMENTS IN THE FIELD OF LABOR .....63**

*Le Dinh Quang Phuc*

**IS POLYCULTURE FORWARD TO A SUSTAINABLE AQUACULTURE  
SYSTEM? A CASE STUDY IN TAM GIANG - CAU HAI LAGOON, VIETNAM  
.....72**

*Tran Hong Hieu, Ton Nu Hai Au, Hisashi Datai*

**THE INFLUENCE OF BEHAVIORAL INTENTION TO USE MOBILE  
APPLICATIONS (APPS) OF TOURISTS IN NHA TRANG CITY .....98**

*Le Tran Tuan*

**THE IMPACT OF ARTIFICIAL INTELLIGENCE ON BANKING HUMAN  
RESOURCE: CURRENT STATUS IN THE WORLD AND  
RECOMMENDATIONS FOR VIETNAM .....111**

*Le Thi Huong Tra*

**GREEN JOBS IN VIETNAM .....122**

*Dinh Thi Huong, Nguyen Ngoc Anh*

**FACTORS INFLUENCING THE BUSINESS EFFECTIVENESS OF UNITS IN  
VIETNAM DEFENCE INDUSTRY .....134**

*Nguyen Huu Tan, Nguyen Thu Thuong*

**ROLES OF US GOVERNMENT IN CORPORATE SOCIAL RESPONSIBILITY  
COMPLIANCE IN VEGETABLE SUPPLY CHAIN – RECOMMENDATIONS  
FOR VIETNAM .....144**

*Ngo Hoang Quynh Anh, Nguyen Khanh Linh*

**THE IMPACT OF SERVICE INNOVATION ON CATERING INDUSTRY’S  
BUSINESS CONTINUITY: THE HAI DILAO CASE .....157**

*Bui Vuong Linh, Nguyen Hai Linh, Nguyen Hoang Ha, Doan Thi My Duyen*

**IMPACT OF SALTWATER INTRUSION ON THE LIVELIHOOD  
OUTCOMES OF RURAL HOUSEHOLDS IN THE MEKONG DELTA .....169**

*Le Thi Kim Loan, Ngo Thi Thanh Truc*

**REGIONAL DIFFERENCES IN ONLINE SHOPPING BEHAVIOR: A STUDY  
ON CONSUMER ACCEPTANCE IN VIETNAM .....177**

*Nguyen Ly Kieu Chinh*

**VIETNAM'S EXPORTS OF COFFEE, TEA, MATÉ AND SPICES UNDER THE  
IMPACT OF THE ASSUMED VIETNAM – UAE CEPA: AN EX-ANTE  
EVALUATION .....194**

*Nguyen Ngoc Diep*

**RELATIONSHIP AMONG UNIVERSITY SOCIAL RESPONSIBILITY (USR),  
USR PRACTICES AND STUDENT SATISFACTION AT VIETNAMESE  
PUBLIC UNIVERSITIES .....209**

*Tuan Anh, Tran*

**CHALLENGES FROM EUROPEAN UNION'S NON-TARIFF MEASURES ON  
VIETNAMESE AGRI-FOOD EXPORT .....231**

*Mai Thi Thanh Mai, Nguyen Duc Bao, Nguyen Thi Nguyet Nuong,  
Trinh Thu Thao, Truong Thi Tu Anh, Nguyen Thi Anh, Nguyen Thi Dao*

**IMPROVED CRISIS MANAGEMENT FOR BUSINESS CONTINUITY AND  
SUSTAINABILITY POST COVID 19 LOCKDOWN IN THAI NGUYEN'S  
TRADE AND TOURISM CENTERS .....244**

*Pham Tien Manh, Nguyen Khanh Ly*

**INCORPORATING CULTURAL HERITAGE INTO LUXURY HOTELS IN  
VIETNAM: OPPORTUNITIES AND CHALLENGES .....261**

*Cuu Long Hoang, Xuan Quyet Pham, Phuong G. L. Le*

**IMPACT OF USER-GENERATED CONTENT IN CAPTURING BRAND  
EQUITY IN VIETNAMESE F&B INDUSTRY: A CASE STUDY OF GOLDEN  
GATE GROUP RESTAURANT BRANDS .....277**

*Pham Thi Minh Chau, Tran Thi Minh Chau*

**DRIVERS OF DIGITAL TRANSFORMATION IN SUPPLY CHAIN  
MANAGEMENT .....292**

*Nguyen Minh Anh, Nguyen Thi Van Trang*

**AN EMPIRICAL ANALYSIS OF VIETNAMESE EXPORTS OF COFFEE .....305**

*Do Thi Minh Hue*

**FACTORS AFFECTING GREEN CONSUMPTION BEHAVIOR OF CONSUMERS IN HANOI POST COVID 19 PANDEMIC.....324**

*Hai Yen Tran*

**INTERNET RETAILING FOR CONSUMER ELECTRONICS PRODUCTS: A COMPREHENSIVE MARKET ANALYSIS IN VIETNAM .....338**

*Nguyen Phan Anh*

**FACTORS AFFECTING IMAGES OF TOURIST ATTRACTIONS IN PHU THO PROVINCE.....349**

*Duong Hong Hanh*

**DETERMINANTS AFFECTING RECRUITMENT – RESEARCH AT AN BINH SECURITIES JOINT STOCK COMPANY.....363**

*Le Thu Hanh, Ta Quang Thang*

**FACTORS AFFECTING CONSUMERS’ PURCHASING DECISIONS OF GREEN PRODUCTS IN HANOI SUPERMARKETS .....380**

*Nguyen Anh Viet, Nguyen Thanh Phuong*

**FACTORS AFFECTING THE BEHAVIORAL INTENTION AND BEHAVIOR OF USING DIGITAL PAYMENT SERVICES IN VIETNAM .....393**

*Thi Thuy Nguyen, Van Duong Ha*

**ARTISANSHIP COMPETITION AND PRODUCT INNOVATION: AN INSTITUTIONAL LOGICS PERSPECTIVE .....416**

*Nguyen Van Dai, Nguyen Hoang Hieu, Vo Hong Nhat, Ngo Hoang Linh*

**FACTORS DRIVING BUSINESS SUCCESS: A CASE STUDY OF FEMALE ENTREPRENEURS IN VIETNAM.....430**

*Le Thi Nuong*

**THE ROLE OF VOLUNTEER TOURISM ORGANISATIONS IN SUSTAINABILITY OF SOCIO-CULTURAL IMPACTS OF VOLUNTEER TOURISM: A CASE STUDY OF VIETNAMESE FARMS.....452**

*Thuong Ho Thuong Tran, Tuan Nien Tran*

**ENHANCING THE UNDERSTANDING OF CIRCULAR ECONOMY-ORIENTED AGRICULTURAL PRACTICE IN VIETNAM.....471**

*Le Quang Minh*

**FACTORS AFFECTING ON INTERNAL AUDIT FUNCTION OUTSOURCING DECISION OF LISTED COMPANIES ON THE VIETNAM STOCK EXCHANGE.....484**

*Luong Thi Hong Ngan, Vu Thi Thu Huyen, Tran Nguyen Bich Hien*

**IMPACT OF CUSTOMER SATISFACTION ANTECEDENTS ON COFFEE CHAIN SERVICE RECOVERY IN VIETNAM .....503**

*Pham Tien Manh, Vu Thi Hien Nuong*

**CÁC YẾU TỐ ẢNH HƯỞNG ĐẾN LUÔNG THƯƠNG MẠI SONG PHƯƠNG GIỮA VIỆT NAM VÀ CÁC NƯỚC ĐỐI TÁC CHÍNH.....522**

*Lê Vũ Thu Hằng*

**ĐÁNH GIÁ CÁC YẾU TỐ ẢNH HƯỞNG ĐẾN HÀNH VI LỰA CHỌN DU LỊCH BỀN VỮNG TẠI VIỆT NAM .....540**

*Nguyễn Tuấn Anh, Lê Thị Việt Hà, Phạm Mai Uyên, Vũ Hải Đăng*

**PHÁT TRIỂN CÔNG NGHỆ XANH TRONG CÁC DOANH NGHIỆP Ở VIỆT NAM HIỆN NAY .....556**

*Lê Thị Kim Huệ*

**NHÂN TỐ ẢNH HƯỞNG ĐẾN MỨC ĐỘ HÀI LÒNG CỦA CỘNG ĐỒNG DÂN CƯ VỀ CHẤT LƯỢNG CUỘC SỐNG TẠI CÁC KHU CÔNG NGHIỆP TỈNH QUẢNG NINH.....569**

*Lê Ngọc Cường, Nguyễn Thị Thu Hằng*

**NGHIÊN CỨU CÁC YẾU TỐ ẢNH HƯỞNG ĐẾN SỰ HÀI LÒNG, GẮN BÓ VÀ CHẤT LƯỢNG CUỘC SỐNG LIÊN QUAN THANH TOÁN HÓA ĐƠN TRÊN M-BANKING: TIẾP CẬN TỪ LÝ THUYẾT CHUỖI PHƯƠNG TIỆN.....586**

*Lê Xuân Cù*

**NHỮNG NHÂN TỐ ẢNH HƯỞNG TỚI QUYẾT ĐỊNH THAM GIA CÁC CUỘC THI KHỞI NGHIỆP CỦA DOANH NGHIỆP KHỞI NGHIỆP TẠO TÁC ĐỘNG XÃ HỘI TẠI VIỆT NAM.....602**

*Đỗ Thị Trang, Nguyễn Đình Hoàng*

**ỨNG DỤNG THANG ĐO OCX NGHIÊN CỨU TRẢI NGHIỆM KHÁCH HÀNG  
MUA SẴM ĐA KÊNH .....616**

*Bùi Thị Thanh Nga*

**PHÂN TÍCH CÁC YẾU TỐ ẢNH HƯỞNG ĐẾN Ý ĐỊNH MUA SẴM TRỰC  
TUYẾN QUA ỨNG DỤNG ĐIỆN THOẠI DI ĐỘNG CỦA KHÁCH HÀNG:  
TRƯỜNG HỢP NGHIÊN CỨU TẠI THÀNH PHỐ HUẾ .....626**

*Nguyễn Như Phương Anh, Nguyễn Thị Mỹ Oanh*

**ẢNH HƯỞNG CỦA DỊCH VỤ E-LOGISTICS ĐẾN HIỆU QUẢ KINH DOANH  
CỦA DOANH NGHIỆP VÀ NHÀ BÁN TRÊN SÀN THƯƠNG MẠI ĐIỆN TỬ  
TẠI VIỆT NAM .....644**

*Trần Thu Thủy, Nguyễn Thanh Phương, Phan Thị Minh, Trần Công Thắng*

**THỰC TRẠNG PHÁT TRIỂN DU LỊCH TẠI VÙNG ĐÀM PHÁ HUYỆN PHÚ  
VANG, TỈNH THỪA THIÊN HUẾ .....660**

*Nguyễn Thế Thìn, Đào Thị Cẩm Nhung*

**Quản trị hành chính công và tăng trưởng kinh tế tại Việt Nam giai đoạn 2018-  
2020: hồi quy phân vị .....668**

*Trịnh Thị Hương, Nghiêm Thị Lịch, Đào Phương Nguyên  
Đào Thúy Ngân, Trần Thị Thu Hà, Đặng Thu Hiền*

**TÁC ĐỘNG CỦA THỰC THI CÁC HIỆP ĐỊNH THƯƠNG MẠI TỰ DO THẾ  
HỆ MỚI (FTA) ĐẾN NỀN KINH TẾ VIỆT NAM.....683**

*Hà Thị Hằng*



# DETERMINING COMPENSATION FOR EMPLOYEES ENTERING INTO NON-COMPETE AGREEMENTS IN THE FIELD OF LABOR

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## Abstract

*The non-compete agreement in the field of labor has been recognized by many countries around the world for a long time. These countries have also put in place regulations to ensure the interests of the parties and social justice. However, in Vietnam, this kind of agreement has not been officially recognized by law. In practice, either the court or the commercial arbitration often does not consider the issue of compensation for employees if the agreement does not provide this issue in the process of dispute resolution. This situation might lead to risks for employees in case the employer abuses his position to force the employee to enter into an unfair agreement. In this article, the author studies a number of legal theories and experiences of different countries to propose the improvement of Vietnamese law on determining compensation for employees entering into non-compete agreement in the field of labor.*

**Keywords:** *non-compete agreement; compensation; consideration; unfair agreement.*

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## 1. INTRODUCTION

Entering into a non-compete agreement is considered one of the measures to help enterprises protect business secrets against the risk of leakage from employees. When enterprises could protect their business secrets, they would feel secure to invest in science and technology as well as other fields to create competitive advantages, contribute to help businesses compete successfully, promote to create new knowledge for society. In addition, the non-compete agreement in labor relations also encourages enterprises to invest more in training and improving the skills of employees, as they will not worry that employees will use those skills to find another place to work, even work for their competitors.

However, in another aspect, the non-compete agreement restricts employees' rights to work. When employees are bound by a non-compete agreement, they would not be able to work for a competitor of the enterprise for a period of time after the termination of the employment contract with the former employer. Additionally, the bargaining position of the employee is often inferior to that of the employer, leading to the fact that the employee is often forced to enter into unfair agreements in order to get the job offer or to maintain the current job. Therefore, the law needs to be adjusted to ensure the balance of interests between the parties, thereby, implementing

social justice.

Compensation is seen as a return to employees in exchange for their non-competitive obligations. For example, an employee may receive 50% of their previous salary in exchange for performing the non-compete obligation. Compensation helps limit employees' damages, while ensuring that enterprises are still able to protect their interests. The laws of some countries around the world also consider that compensation is a condition of the validity of non-compete agreements.

Due to the fact that Vietnamese law has not been provided yet for the non-compete agreement, the issue of compensation to employees has not yet been specified in the Vietnamese law. Article 21(2) of the Labor Code 2019 only stipulates in a general way that the employer has the right to reach a written agreement with the employee to protect business secrets. This provision also requires the parties to agree on the interests in this agreement. However, this regulation does not clarify what these rights are, therefore, it is difficult to apply it in practice (Do Van Dai and Le Ngoc Anh, 2019).

Through studying a number of cases related to non-compete agreements that have been tried by courts or commercial arbitration, compensation has not yet been considered when assessing the reasonableness of non-compete agreements. For example, the Vietnam International Arbitration Center (VIAC) issued Arbitral Award No. 75/17HCM on February 19, 2018 to settle the case between Company X and Ms. Do Thi Mai T related to the non-compete agreement. Although the content of this non-compete agreement does not specify the amount of compensation that Ms. T is entitled to be bound to the non-compete obligation. However, the Arbitration Council did not consider this issue and accepted the validity of the non-compete agreement between Company X and Ms. Do Thi Mai T. Then, Ms. T requested the People's Court of Ho Chi Minh city annuls the arbitral award. The People's Court of Ho Chi Minh city issued Decision No. 755/2018/QD-PQTT dated June 12, 2018 with the content that it did not accept Ms. T's request and did not consider compensation as a factor to assess the reasonableness of the non-compete agreement.

In this article, the author analyzes the regulations of some countries on determining compensation for employees entering into non-compete agreements. Then, the author makes some recommendations to improve the law of Vietnam. Recommendations focus on legal solutions to both promote businesses to invest in new technology development and protect the rights of employees. Thereby, we can aim for sustainable economic growth.

## **2. LITERATURE REVIEW, THEORETICAL FRAMEWORK AND RESEARCH METHODS**

### **2.1. Literature review**

The issue of determining compensation for employees entering into non-compete agreements in Vietnam has been studied by a number of scholars:

- Doan Thi Phuong Diep (2015), in her research, proposes guidelines for the implementation of the provisions of the Labor Code on non-compete agreements. Accordingly, in the case of non-compete agreements without compensation for employees, from the experience of French case law, she suggests to consider this agreement null. However, this issue

has been only mentioned at a preliminary level and did not have an in-depth analysis in her research.

- It is believed that compensation for employees should be considered as one of the validity conditions for non-compete agreements (Do Van Dai & Le Ngoc Anh, 2019). In their research, the authors compared the provisions of Vietnamese law with those of Japan, the United States and France. As a result, the employees' income and life could be affected by the restriction on the right to work. Therefore, Vietnamese law should acquire experiences of these countries in the direction of requiring employers to pay an adequate amount of money to employees during the period of performance of the non-compete obligation. However, the study does not indicate how this regulation should be designed and how much is reasonable.

- Similarly, according to Truong Trong Hieu (2020), it is necessary to set a requirement on paying the compensation for the limitations of the right to work that employees have to bear. The content of non-compete agreements should stipulate the amount of compensation in exchange for the non-compete obligation of the employees. However, like the above studies, this study only mentioned this issue as a preliminary suggestion.

On the basis of the studies of the scholars, the author identified the research gap. Accordingly, in this study, the author proposes a method to determine the compensation on the basis of comparison with the laws of some countries.

## **2.2 Theoretical framework**

### *2.2.1. Theory of justice in transactions*

Justice is a term associated with the development of human society, as well as the goal that progressive societies want to achieve. Aristotle is considered to be the first thinker to discuss the issue of justice in transactions. He made a distinction between corrective justice and distributive justice. Accordingly, corrective justice is concerned with how the court corrects the wrong done by one party to another. Distributive justice is concerned with the fairness of each person according to what they deserve. In modern times, Rawls' theory of justice has profoundly influenced the study of justice and equity in contemporary philosophy. Rawls (1999) has argued that justice is the primary norm of social institutions and of human activities. Laws and institutions, no matter how well established, need to be reformed or abolished if they are unjust. Developing and supplementing Rawls' theory of justice, Benson (2019) comprehensively explained the ethics of contractual relationships in his book "*Justice in Transactions: A Theory of Contract Law*". Throughout his book, Benson (2019) has argued that a contract is a relationship between two or more parties and that contract theory should consider the fairness of that relationship.

In Common Law, the theory of justice in transactions is considered by courts of justice to protect vulnerable parties such as the poor or the uninformed (Liew & Yu, 2020). In Civil Law, the theory of justice in transactions is also applied in the process of formulating the provisions of the written law. For example, Section 138(2) of the German Civil Code mentioned the issue of unreasonable agreement as follows: "*In particular, a legal transaction is void by which a person, by exploiting the predicament, inexperience, lack of sound judgement or considerable weakness of will of another, causes himself or a third party, in exchange for an act of*

*performance, to be promised or granted pecuniary advantages which are clearly disproportionate to the performance*". In this article, the author studies the theory of justice in transactions, which is a theory of contracts, to analyze the experience of some countries and propose recommendations to improve the law of Vietnam.

### 2.2.2. Doctrine of consideration

The origin of the doctrine of consideration is still debated by scholars. According to Shatwell (1954), the doctrine of consideration arose in the 16th century as an answer to common law judges' thinking about how the issue of *assumpsit* should be applied in enforcement of bilateral agreements without recognizing the legal validity of unilateral agreements. Unlike Shatwell, Holdsworth (1937) views the doctrine of consideration as having its roots in the way in which the issue of *assumpsit* developed under the early influence of *quid pro quo* doctrine and the indirect influence of the principles of equity discussed later.

Consideration is a very separate concept of Common Law. Nguyen Ngoc Dien (2012, p. 115) said that the main idea of this doctrine is: "*an object of economic value is transferred, an act of bringing economic benefits is done in exchange for another thing, another thing; one promise is kept just for the sake of another promise - must also be kept*". According to Black (1968, p. 379), consideration is: "*The cause, motive, or impelling influence which induces a contracting party to enter into a contract. The reason or material cause of a contract*". In the context that Vietnamese law has not yet mentioned the issue of consideration, the author examines the doctrine of consideration as a basis for proposing that compensation to employees should be considered as a validity condition for non-compete agreements.

### 2.2.3. Theory of causality

Theory of causality is believed to have originated in Roman law (Lorenzen, 1919). The Romans believed that *causa* (cause) is the source of obligation (Léon & Mazeaud, 1956). Cause could be understood as the purpose that a promisor wants to achieve when entering into a contract (Nguyen Ngoc Dien, 2012). It is essential to distinguish between the causes of the contract and obligation. Accordingly, "*The cause of contract is the reason, cause or reasons that determine each party to enter into the contract*" (Original: "*La cause d'un contrat est la raison, la cause ou les raisons qui déterminent chaque partie à conclure un contrat*") (Léon & Mazeaud, 1956, p. 7). In contrast, "*The cause of obligation is the reason why a contracting party performs his obligation*" (Original: "*La cause d'une obligation est la raison pour laquelle la partie contractante exécute son obligation*") (Léon & Mazeaud, 1956, p. 7). Unlike the doctrine of consideration, the theory of causality still assumes the validity of a unilateral contract. In a unilateral contract, the counter-obligation does not exist, so the cause of the obligation could not be determined by relying on the counter-obligation. In this case, the cause of the obligation must be determined based on the reasons and motives that motivated the promisor to decide to be bound by this obligation (Nguyen Ngoc Dien, 2012).

In France, while drafting the Civil Code, the drafters used the phrase "*cause de la convention*" and declared invalid contracts without cause, or on a false cause, or on an illicit cause, or on an unethical cause (Léon & Mazeaud, 1956). The current French Civil Code does not stipulate that cause is a condition for a valid contract. However, Article 1162 of the French Civil Code provides that: "*The contract cannot derogate from public order either by its*

stipulations or by its purpose, whether the latter was known or not by all the parties” (Original: “*Le contrat ne peut déroger à l'ordre public ni par ses stipulations, ni par son but, que ce dernier ait été connu ou non par toutes les parties*”). This provision is the basis for French judges to evaluate the cause to determine whether the contract is valid or not. In the case of an obligation without cause, or on a false cause, or on an illegal cause, the contract may be considered a violation of public order.

There are certain similarities in the French legal system and the Vietnamese legal system. Therefore, the author studies the theory of causality, which is applied in France, to evaluate the causes of non-compete obligation of employees. From which, the author proposes various solutions to force employers to pay a count of compensation to receive the non-compete promise of employees.

### **2.3 Research methods**

In this article, the author uses different research methods:

- *Comparative law*: This method is used to identify the similarities and differences between Vietnamese and foreign laws regarding the provisions relating to determine compensation for employees entering into non-compete agreements. The result of the comparative study is to assess the shortcomings of the current Vietnamese law and to derive more effective solutions to the relevant legal problem.

- *Doctrinal analysis*: This method is adopted to clarify the doctrine of consideration and the theory of causality that are the basis for the author’s proposing to improve the Vietnamese law on determining compensation for employees entering into non-compete agreements.

- *Statute law analysis*: This method is implemented to analyze the current situation of the provisions of the statute law of Vietnam. On the basis of identifying the current legal situation, the research results of the article will also propose solutions to improve the Vietnamese law on determining compensation for employees entering into non-compete agreements.

## **3. REGULATIONS OF SOME COUNTRIES’ LAW ON COMPENSATION FOR EMPLOYEES ENTERING INTO NON-COMPETE AGREEMENTS**

### **3.1. The United States of America (USA)**

The USA is one of a number of countries in the Common Law tradition. Therefore, the doctrine of consideration is also recognized in this country. Under the USA law, a valid contract or agreement must satisfy the following requirements: “*The promise or obligation of each party must be supported by consideration (such as the payment of money, the delivery of goods, or the promise to do or refrain from doing some lawful future act) given by each party to the contract*” (Ashcroft & Ashcroft, 2008, p. 49). Thus, for non-compete agreements, in principle, consideration could be seen as one of the validity conditions of these agreements.

As a federal state, each state in the USA has a relatively independent legal system. Consequently, each state of the USA also has different requirements for consideration that an employee must receive in order for the non-compete agreement to be valid. In some states, consideration of employees must be material compensation (such as Texas). In some other states, at-will employment is considered the consideration of employees (such as Wisconsin)

(Garmaise, 2011). Even for at-will employees of the enterprise, the employer's agreement to continue to extend the employment contract may also be considered the consideration of employees for entering into a non-compete agreement in some states (such as Florida) (Seyfarth Shaw LLP, 2021).

### **3.2. The French Republic**

French law does not have the same concept of consideration as the USA law. However, French law applies the theory of causality to evaluate the validity of a contract. On the basis of this theory, the cause of the non-compete obligations of employees is determined to be the benefits that they receive when entering into a non-compete agreement. Therefore, if an employee enters into a non-compete agreement just because he/she is forced to do so, the agreement is null.

In France, the legal basis governing non-compete agreements is Case Law No. 00-45.135 of the Court of Cassation (Cour de Cassation) in 2002 (Do Van Dai & Le Ngoc Anh, 2019). Accordingly, the content of this Case Law states: “...a non-compete clause is lawful only if it is essential for the protection of the legitimate interests of the company, limited in time and space, that it takes into account the specificities of the employee's job and includes the obligation for the employer to pay the employee financial compensation, these conditions being cumulative” (Original: “...une clause de non-concurrence n'est licite que si elle est indispensable à la protection des intérêts légitimes de l'entreprise, limitée dans le temps et dans l'espace, qu'elle tient compte des spécificités de l'emploi du salarié et comporte l'obligation pour l'employeur de verser au salarié une contrepartie financière, ces conditions étant cumulative”). Thus, in France, financial compensation is considered as one of the mandatory conditions for a non-compete agreement to be valid.

The amount of financial compensation will be considered by the judge (Muller, 2021). In Case Law No. 04-46.721 of 2006, the Court of Cassation clearly stated the point of view: “derisory financial compensation for the non-compete clause contained in an employment contract is equivalent to an absence of compensation” (Original: “...une contrepartie financière dérisoire à la clause de non-concurrence contenue dans un contrat de travail équivaut à une absence de contrepartie”). Also in this case, the Court of Cassation decided that financial compensation of an amount equal to 1/10th of the gross monthly salary received by the employee was derisory. In a recent case, the Court of Appeal of Rouen (Cour d'appel de Rouen) applied Article 7.4 of the National Agreement of 23 January 1986 relating to permanent employees of temporary employment companies to consider a financial compensation for the non-compete clause (Cour d'appel de Rouen, 2021). Accordingly, in the case of termination of the employment contract at the initiative of the employer other than in the event of serious or gross negligence, for the duration of the non-competition, financial compensation which may not, in any event, be less than a monthly amount equal to 20% of the average monthly salary of the employee during his last three months of presence in the company, for the first year and 10% for the second year.

### **3.3. The People's Republic of China**

The Labor Contract Law 2008 marked an important reform in China's laws governing labor relations. This Act has raised a number of issues that have not been adjusted by previous

laws, including the issue of non-compete agreements in the field of labor. Article 23 of this Act allows employers and employees to enter into non-compete agreements to protect business secrets. Accordingly, the employer must pay the employee a monthly amount for the duration of the employee's non-competitive obligations. Although the Labor Contract Law 2008 requires employers to pay employees a financial compensation, this amount of money is not specified in China's written law. As a result, the determination of the amount of compensation is based on the agreement of the parties. The court only evaluates the reasonableness of these agreements to make a decision to recognize or invalidate.

In 2012, the Judicial Committee of the Supreme People's Court adopted the Interpretation (IV) of the Supreme People's Court of Several Issues on the Application of Law in the Trial of Labor Dispute Cases. Accordingly, the court requires the employer to pay the employee monthly compensation which is not less than 30% of the average monthly salary for the twelve months prior to the termination of the employment relationship. In case the calculated amount is lower than the regional minimum wage, the minimum monthly compensation must be equal to the regional minimum wage.

#### **4. PROPOSING TO IMPROVE THE VIETNAMESE LAW ON DETERMINING COMPENSATION FOR EMPLOYEES ENTERING INTO NON-COMPETE AGREEMENTS**

The concept of non-compete agreement has not been officially recognized in the Vietnamese legal system. Therefore, in an understandable way, the regulations related to determining compensation for employees entering into non-compete agreements have not been specifically mentioned by the law. Furthermore, Vietnamese judges are not in the habit of using legal doctrines to resolve disputes. Hence, either the doctrine of consideration or the theory of causality also seems strange to Vietnamese judges. Thus, a non-compete agreement without compensation to employees can still be valid in Vietnam. This leads to the risk of employers abusing their position to establish unfair non-compete agreements with employees.

From the experience of some countries, it can be seen clearly that it is necessary for Vietnamese law to develop regulations on compensation for employees entering into non-compete agreements. In other words, Vietnamese law needs to stipulate compensation for employees as one of the requirements for the non-compete agreement to be valid. The author believes that, with the socio-economic characteristics of Vietnam, Vietnamese law should stipulate for financial compensation during the period the employee performs the non-compete obligation (at-will employment should not be seen as compensation for a non-compete obligation).

Regarding the amount of compensation, in principle, the employer and employee could agree and stipulate in the content of the non-compete agreement. However, due to the unequal negotiating position between the employer and the employee, to avoid the situation of the employer abusing the bargaining power to force the employee to sign unfair agreements, the law should stipulate for the minimum amount of compensation that an employer must pay an employee for a non-compete obligation. The minimum amount of compensation can be specified as a specific amount or a formula of calculation. The author believes that the regulation of the calculation formula will be consistent with the current regulations on labor, such as calculating

pensions or unemployment benefits. This provision could be stipulated in Degree of Government or Circular of Ministry of Labor, War Invalids and Social Affairs or Case Law of Supreme People's Court of Vietnam.

## 5. CONCLUSION

In summary, non-compete agreements play an important role in protecting legitimate interests of employers and ensuring a fair competition in the economy. However, in order to ensure the rights of employees and social justice, the law needs to set out conditions for the non-compete agreement to be valid. In particular, the employee needs to receive the financial compensation to perform non-compete obligations arising from the agreement.

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# **PROCEEDINGS ICYREB 2023 - THE 9TH INTERNATIONAL CONFERENCE FOR YOUNG RESEARCHERS IN ECONOMICS AND BUSINESS (VOLUME 3)**

*Author:*

Many Authors

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*Responsible for publication:*

*Editor*

**Assoc.Prof. Nguyen Ngoc Dinh**

*Responsible for the Manuscript:*

Department of Research Administration - International Relations  
(University of Economics Ho Chi Minh city)

*Publishing associate:*

**Department of Research Administration - International Relations  
(University of Economics Ho Chi Minh city)**

59C Nguyen Dinh Chieu, Vo Thi Sau Ward, Dist.3, Ho Chi Minh city

**Publishing House of Economics Ho Chi Minh city**

279 Nguyen Tri Phuong, Ward 5, Dist. 10, Ho Chi Minh city

Website: [www.nxb.ueh.edu.vn](http://www.nxb.ueh.edu.vn) – Email: [nxb@ueh.edu.vn](mailto:nxb@ueh.edu.vn)

Tel: (028) 38.575.466 – Fax: (028) 38.550.783

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Print 50 copies, size 20.5 x 28.5 cm at Sieu Toc Printing - Service -  
Trading Company Limited

43A Dao Tong Nguyen, Nha Be Town, Nha Be Dist., Ho Chi Minh city

Register No for publication: 4493-2023/CXBIPH/05-61/KTTPHCM

Decision No for publication: 112/QĐ-NXBKTTPHCM dated 13th Dec 2023

Printing and depositing in 2024

**ISBN : 978-604-346-251-7**

# PROCEEDINGS ICYREB 2023



[icyreb.ueh.edu.vn](http://icyreb.ueh.edu.vn)

ISBN: 978-604-346-251-7



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