SPC Guiding Case No. 250: Lixin County [X]da Financing Guarantee Co., Ltd. v. Anhui [X]an Construction Group Co., Ltd. and Lixin County [X]teng Real Estate Co., Ltd. (Third-Party Revocation Action)

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Unofficial English translation prepared for reference only. The official Chinese text prevails.

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Keywords

Civil / third-party revocation action / priority right to be paid for construction project price / relative waiver / order of satisfaction

Holding

Where a contractor of a project under construction promises the mortgagee of the project to waive its priority right to be paid for the construction project price, the people's court shall examine whether the waiver harms the interests of construction workers. Where it harms the interests of construction workers, the waiver is invalid; where it does not harm the interests of workers, the waiver is valid, but it only produces the effect that, with respect to that mortgagee, the priority right to be paid for the construction project price is subordinated to the mortgage in the order of satisfaction. Where other creditors of the developer rely on this to claim that the contractor does not enjoy the priority right to be paid for the construction project price, the people's court shall not support such claim.

Basic Facts

From 2011 to 2012, Lixin County [X]teng Real Estate Co., Ltd. (“[X]teng Real Estate”) carried out tendering for the Phase I works of Zone C and Zone D and the Phase II works of Zone C of a real estate project in Anhui. Anhui [X]an Construction Group Co., Ltd. (“[X]an Construction”) won the bid and entered into a construction contract for the construction project with [X]teng Real Estate to undertake the project works involved.

In January 2016, [X]teng Real Estate commissioned a third party to apply to a Lixin commercial bank in Anhui for a one-year project loan of RMB 29 million (same currency hereinafter). Lixin County [X]da Financing Guarantee Co., Ltd. (“[X]da Guarantee”) provided a guarantee for the loan, and [X]teng Real Estate mortgaged part of the housing (108 housing units in total) of Building 10 of Zone D of the real estate project under development to [X]da Guarantee as counter-guarantee collateral for the loan. In the same month, [X]an Construction, as the construction party, issued a Declaration of the Builder for Mortgage of the Project Under Construction, undertaking: “1. The Company fully understands and believes that the borrowed funds are used entirely for the construction of the real estate project; 2. Prior to the satisfaction of all claims secured by the guarantee provided by [X]da Guarantee, the Company waives the priority right to be paid from the realization value of the buildings constructed by it arising from the settlement of project funds, and unconditionally cooperates with [X]da Guarantee in exercising its mortgage right in accordance with the law.”

In May 2017, because the third party failed to repay the aforementioned loan within the time limit, [X]da Guarantee completed the subrogation payment. In June of the same year, [X]da Guarantee brought a lawsuit with the Bozhou Intermediate People's Court of Anhui Province on a claim for recovery, requesting [X]teng Real Estate and others to repay the subrogation payment principal and interest and liquidated damages. Thereafter, the parties reached a mediation agreement, and the court confirmed and issued Civil

Mediation Statement (2017) Wan 16 Min Chu No. 212, under which [X]teng Real Estate and others shall repay the subrogation payment principal and interest and liquidated damages.

In 2018, the construction of the project involved was completed. Later, due to a dispute over the project price, [X]an Construction brought a lawsuit against [X]teng Real Estate on a construction contract dispute, requesting an order that [X]teng Real Estate pay [X]an Construction the outstanding project price and overdue interest, and confirming that [X]an Construction enjoyed a priority right to be paid over the auction or sale proceeds of the project involved (Zones C and D of the Anhui real estate project) within the scope of the aforementioned project price. On April 17, 2020, the Bozhou Intermediate People's Court of Anhui Province rendered Civil Judgment (2019) Wan 16 Min Chu No. 248: [X]teng Real Estate shall pay [X]an Construction the outstanding project price of RMB 48,733,386 plus interest, and [X]an Construction enjoyed a priority right to be paid over the auction or sale proceeds of Zones C and D of the Anhui real estate project within the scope of the outstanding project price owed by [X]teng Real Estate. After appeals by [X]teng Real Estate and [X]an Construction, the Anhui Provincial High People's Court rendered Civil Judgment (2020) Wan Min Zhong No. 831 on December 22, 2020: the appeals were dismissed and the original judgment affirmed.

Thereafter, [X]da Guarantee brought a third-party revocation action (i.e., this case), claiming that [X]an Construction had failed to truthfully state in the aforementioned construction contract dispute that it had made a declaration of waiving its priority right to be paid, and that the aforementioned judgments impeded the full satisfaction of [X]da Guarantee's claim during the enforcement of Civil Mediation Statement (2017) Wan 16 Min Chu No. 212. It therefore requested the revocation of the items of Civil Judgment (2019) Wan 16 Min Chu No. 248 and Civil Judgment (2020) Wan Min Zhong No. 831 concerning the confirmation of [X]an Construction's priority right to be paid for the construction project price.

Judgment

On December 30, 2021, the Anhui Provincial High People's Court rendered Civil Judgment (2021) Wan Min Che No. 2: the litigation claims of Lixin County [X]da Financing Guarantee Co., Ltd. were dismissed. After the judgment was pronounced, Lixin County [X]da Financing Guarantee Co., Ltd. was dissatisfied and appealed. On November 18, 2022, the Supreme People's Court rendered Civil Judgment (2022) Zui Gao Fa Min Zhong No. 233: the appeal was dismissed and the original judgment affirmed.

Reasoning

The focus of the dispute in this case was: how to determine the validity of [X]an Construction's promise to [X]da Guarantee to waive its priority right to be paid for the construction project price.

Article 23 of the Interpretation (II) of the Supreme People's Court on Several Issues Concerning the Application of Law in the Trial of Cases of Disputes over Construction Contracts for Construction Projects (Fa Shi [2018] No. 20) provides: “Where the developer and the contractor agree to waive or restrict the priority right to be paid for the construction project price, harming the interests of construction workers, and the developer relies on that agreement to claim that the contractor does not enjoy the priority right to be paid for the construction project price, the people's court shall not support such claim.” Accordingly, the key to determining the validity of a contractor's act of waiving the priority right to be paid for the construction project price lies in whether it harms the interests of construction workers.

In this case, although the Declaration of the Builder for Mortgage of the Project Under Construction involved was made by the contractor [X]an Construction to [X]da Guarantee, a creditor of the developer, rather than directly to the developer [X]teng Real Estate, its core content was still [X]an Construction's disposition of the priority right to be paid for the construction project price, and the determination of its validity should still be governed by the aforementioned judicial interpretation. Upon investigation, [X]an Construction promised the mortgagee [X]da Guarantee to waive the priority right to be paid for the construction project price over the mortgaged housing, the purpose of which was to obtain [X]da Guarantee's provision of a guarantee for the project construction loan and to ensure that the project construction obtained the necessary financial

support; it did not have the illegal purpose of harming the interests of construction workers. Moreover, the 108 housing units to which the promised waiver of the priority right to be paid for the construction project price related accounted for only approximately 4.5% of the total project area undertaken by [X]an Construction, with an assessed value of RMB 22,373,538. [X]an Construction still enjoyed the priority right to be paid for the construction project price over the remaining housing accounting for 95.5% of the total project area. Therefore, the promised waiver did not affect the satisfaction of its claim for RMB 48,733,386 in project price and interest against [X]teng Real Estate, and would not harm the lawful interests of construction workers. In the absence of other grounds for invalidity, the waiver should be found valid.

The priority right to be paid for the construction project price confers on the contractor's project price claim the effect of priority satisfaction over the realization value of the building, relative to mortgage rights, ordinary claims and the like. Where project price claims, mortgage rights, ordinary claims and other rights coexist over a construction project, the project price claim enjoys a relatively prior order of satisfaction. In this case, [X]an Construction did not make any expression of intent to other creditors of [X]teng Real Estate to waive its prior order of satisfaction, so the waiver was relative and partial. Therefore, the above act only produced the consequence that [X]an Construction's project price claim over the 108 housing units involved could not be satisfied in priority to [X]da Guarantee's mortgage right, and did not result in the absolute extinction of [X]an Construction's priority right to be paid for the construction project price. Relative to other mortgagees and ordinary creditors of [X]teng Real Estate, [X]an Construction still enjoyed the priority right to be paid for the construction project price in accordance with the law. Therefore, the confirmation in Civil Judgment (2019) Wan 16 Min Chu No. 248 and Civil Judgment (2020) Wan Min Zhong No. 831 that [X]an Construction enjoyed a priority right to be paid over the auction or sale proceeds of Zones C and D of the Anhui real estate project within the scope of the outstanding project price owed by [X]teng Real Estate conformed to the law. As for the order under which [X]da Guarantee's mortgage right was satisfied in priority to [X]an Construction's project price claim, it was not affected in accordance with the law, and its interests in that order could be safeguarded during actual enforcement.

In summary, the people's court did not support [X]da Guarantee's claim to revoke the items of Civil Judgment (2019) Wan 16 Min Chu No. 248 and Civil Judgment (2020) Wan Min Zhong No. 831 concerning the confirmation of [X]an Construction's priority right to be paid for the construction project price.

Relevant Legal Provisions

Article 807 of the Civil Code of the People's Republic of China (Article 286 of the Contract Law of the People's Republic of China, effective October 1, 1999, applied in this case)

Article 42 of the Interpretation (I) of the Supreme People's Court on Several Issues Concerning the Application of Law in the Trial of Cases of Disputes over Construction Contracts for Construction Projects (Fa Shi [2020] No. 25) [Article 23 of the Interpretation (II) of the Supreme People's Court on Several Issues Concerning the Application of Law in the Trial of Cases of Disputes over Construction Contracts for Construction Projects (Fa Shi [2018] No. 20), effective February 1, 2019, applied in this case]

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