SPC Guiding Case No. 95: The Xuancheng Longshou Sub-branch of Industrial and Commercial Bank of China Co., Ltd. v. Xuancheng Boguan Trading Co., Ltd. and Jiangsu Kaisheng Real Estate Co., Ltd. et al. (Financial Loan Contract Dispute)

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SPC Guiding Case No. 95

Discussed and adopted by the Judicial Committee of the Supreme People's Court; issued on June 20, 2018

Keywords

Civil; financial loan contract; security; maximum amount mortgage

Holding

Where the parties separately reach an agreement to bring a claim that already existed before the establishment of the maximum amount mortgage into the scope of claims secured by that maximum amount mortgage, so long as the amount of the claim brought in remains within the maximum claim amount secured by the maximum amount mortgage, the effectiveness of the maximum amount mortgage shall still extend to the claim brought in even if no change registration has been completed for the maximum amount mortgage, provided that no adverse effect is produced on third parties.

Basic Facts

On April 20, 2012, the Xuancheng Longshou Sub-branch of Industrial and Commercial Bank of China Co., Ltd. (hereinafter "ICBC Xuancheng Longshou Sub-branch") and Xuancheng Boguan Trading Co., Ltd. (hereinafter "Boguan Company") signed a "Small Enterprise Loan Contract," agreeing that Boguan Company would borrow RMB 3 million from ICBC Xuancheng Longshou Sub-branch for a term of seven months, commencing from the actual drawdown date, with RMB 1 million repayable on November 1, 2012, and RMB 2 million repayable on November 17, 2012. The contract also agreed on the loan interest rate, margin, and other matters. On April 24 of the same year, ICBC Xuancheng Longshou Sub-branch disbursed the above loan to Boguan Company.

On October 16, 2012, the shareholders' meeting of Jiangsu Kaisheng Real Estate Co., Ltd. (hereinafter "Kaisheng Company") passed a resolution agreeing to mortgage to ICBC Xuancheng Longshou Sub-branch the company's property located at No. 118 Jiangshan Avenue, Suyu District, Suqian City, Jiangsu Province — Suqian Hongxing Kaisheng International Home Plaza (room number: B-201; property ownership certificate number: Suyu Zi No. 201104767), for the financing mortgages handled by the four enterprises Boguan Company, Minhang Company, Hangjia Company, and Jinyida Company, which were merchants of Yirongda Company, with ICBC Xuancheng Longshou Sub-branch, and that all economic disputes arising therefrom would be borne by Kaisheng Company. On October 23 of the same year, Kaisheng Company issued to ICBC Xuancheng Longshou Sub-branch a letter of commitment for property mortgage security, agreeing to provide mortgage security with the above property for the financing of the four enterprises with ICBC Xuancheng Longshou Sub-branch, and undertaking that if the four enterprises failed to perform their debts to ICBC Xuancheng Longshou Sub-branch on schedule and the value of the mortgaged property after disposal was insufficient to repay all the debts, Kaisheng Company agreed to repay the remaining debts with other property. Both the letter of commitment and the above shareholders' meeting resolution were signed by all shareholders of Kaisheng Company and affixed with Kaisheng Company's official seal. On October 24, 2012, ICBC Xuancheng Longshou Sub-branch and Kaisheng Company signed a "Maximum Amount

Mortgage Contract," agreeing that Kaisheng Company would use the shop premises under the real property ownership certificate Su Fang Quan Zheng Suyu Zi No. 201104767 to provide mortgage security for the claims that ICBC Xuancheng Longshou Sub-branch held against the debtors under the loan contracts and other principal contracts signed with Boguan Company, Minhang Company, Hangjia Company, and Jinyida Company during the period from October 19, 2012, to October 19, 2015, within a maximum balance of RMB 40 million, regardless of whether such claims had matured at the expiration of that period and regardless of whether such claims had already arisen before the establishment of the maximum amount mortgage. The secured scope included the principal amount of the principal claims, interest, costs of enforcing the claims, and so on. On the same day, the parties completed mortgage registration for the mortgaged property in accordance with the law, and ICBC Xuancheng Longshou Sub-branch obtained the real property other-rights certificate Su Fang Ta Zheng Suyu No. 201204387. On November 3, 2012, Kaisheng Company again passed a shareholders' meeting resolution and at the same time issued a property mortgage commitment letter to ICBC Xuancheng Longshou Sub-branch; the contents, signatures, and seals of the shareholders' meeting resolution and the commitment letter were the same as before. On the same day, Kaisheng Company and ICBC Xuancheng Longshou Sub-branch signed a "Supplementary Agreement," clarifying that the secured scope of the "Maximum Amount Mortgage Contract" signed by the parties included the claims under the four loan contracts signed on April 20, 2012, by ICBC Xuancheng Longshou Sub-branch with Boguan Company, Minhang Company, Hangjia Company, and Jinyida Company.

Boguan Company failed to repay the loan in question on schedule, and ICBC Xuancheng Longshou Sub-branch sued in the Xuancheng Intermediate People's Court, requesting an order that Boguan Company repay the principal and interest of the loan and the costs of enforcing the claim, and that Kaisheng Company bear mortgage security liability with the real property under the real property ownership certificate Su Fang Quan Zheng Suyu Zi No. 201104767 that it had mortgaged.

Judgment

On November 10, 2013, the Xuancheng Intermediate People's Court rendered Civil Judgment No. (2013) Xuan Zhong Min Er Chu Zi No. 00080, ordering: (1) Boguan Company shall pay ICBC Xuancheng Longshou Sub-branch loan principal of RMB 3 million and interest within five days from the date the judgment took effect; ... (4) if Boguan Company failed to perform the above payment obligation in item (1) within the period determined in the judgment, ICBC Xuancheng Longshou Sub-branch shall have priority of compensation from the property under the real property ownership certificate Su Fang Quan Zheng Suyu Zi No. 201104767 provided by Kaisheng Company, whether by discounting the property or from the proceeds of its auction or sale... After the judgment was pronounced, Kaisheng Company, on the ground that the matters agreed in the "Supplementary Agreement" had not been subject to change registration of the maximum amount mortgage, appealed to the Anhui Higher People's Court. On October 21, 2014, that court rendered Civil Judgment No. (2014) Wan Min Er Zhong Zi No. 00395, rejecting the appeal and affirming the original judgment.

Reasoning

The court in its effective judgment held that Kaisheng Company and ICBC Xuancheng Longshou Sub-branch signed the "Maximum Amount Mortgage Contract" on October 24, 2012, agreeing that Kaisheng Company voluntarily used the property in its name as mortgaged property to provide maximum amount mortgage security for the principal and interest of the loans borrowed by Boguan Company from ICBC Xuancheng Longshou Sub-branch during the period from October 19, 2012, to October 19, 2015, within a maximum balance of RMB 40 million, and completed mortgage registration; ICBC Xuancheng Longshou Sub-branch lawfully obtained the mortgage right over the property in question. On November 3, 2012, Kaisheng Company and ICBC Xuancheng Longshou Sub-branch also signed a "Supplementary Agreement," agreeing that the principal claims secured by the above maximum amount mortgage extended to the claims under the "Small Enterprise Loan Contract" signed on April 20, 2012, by ICBC Xuancheng Longshou Sub-branch and Boguan Company. The "Supplementary Agreement" not only bore the signatures and seals of both parties

but was also corroborated by Kaisheng Company's shareholders' meeting resolution and the property mortgage security commitment letter it issued. Therefore, the "Supplementary Agreement" was an expression of Kaisheng Company's true intent, and the contents agreed therein complied with Article 203(2) of the Property Law of the People's Republic of China (hereinafter the "Property Law"), did not violate the mandatory provisions of laws or administrative regulations, and was lawfully formed and valid. As a constituent part of the original maximum amount mortgage contract, it had the same legal effect as the original maximum amount mortgage contract. Accordingly, the claims under the "Small Enterprise Loan Contract" of April 20, 2012, involved in this case had been brought into the scope of the principal claims secured by the above maximum amount mortgage with a maximum amount of RMB 40 million. As to whether the matters agreed in the "Supplementary Agreement" required the completion of corresponding change registration procedures for the above maximum amount mortgage, the Property Law had no express provision, and this should be determined by reference to the characteristics of the maximum amount mortgage and the relevant legal provisions.

Under Article 203(1) of the Property Law, a maximum amount mortgage has two salient characteristics: first, the amount of claims secured by a maximum amount mortgage is subject to a determined maximum limit, but the amount of claims actually arising is indeterminate; and second, a maximum amount mortgage provides security for claims that will arise continuously within a certain period. Thus, the specific claims secured at the time a maximum amount mortgage is established are generally not yet determined. Based on the principle of respecting party autonomy, Article 203(2) of the Property Law provides a proviso to the preceding paragraph, permitting, with the parties' consent, claims that already existed before the establishment of the maximum amount mortgage to be brought into the scope of claims secured by the maximum amount mortgage; this is neither the re-establishment of a maximum amount mortgage nor the content of a change of the maximum amount mortgage as provided in Article 205 of the Property Law. Similarly, under Article 53 of the Measures for House Registration, the bringing of claims existing before the establishment of a maximum amount mortgage into the scope of claims secured by the maximum amount mortgage is not a matter that must be recorded in the other-rights certificate for the establishment registration of the maximum amount mortgage or in the house registration book, and therefore is not a statutory circumstance for which a change registration of the maximum amount mortgage should be applied for.

In this case, ICBC Xuancheng Longshou Sub-branch and Kaisheng Company merely brought the claims that already existed before the establishment of the maximum amount mortgage into the scope of claims secured by that maximum amount mortgage by separately reaching a supplementary agreement. The amount of the claims in question so brought in remained within the maximum claim amount of RMB 40 million secured by the maximum amount mortgage. The determined claims so brought in were not matters that had to be recorded in the other-rights certificate for the establishment registration of the maximum amount mortgage or in the house registration book. On the premise that no adverse effect would be produced on other mortgagees, this act of party autonomy should be respected. In addition, under commercial transaction rules, what is not prohibited by law is permissible — that is, where the law is unclear, no obligation to apply strict transaction rules by analogy should be imposed on market transaction subjects. Moreover, with respect to the bringing of the claims under the loan contract of April 20, 2012, into the scope of claims secured by the maximum amount mortgage, Kaisheng Company not only formed a shareholders' meeting resolution and issued a property mortgage security commitment letter, but also reached a "Supplementary Agreement" with ICBC Xuancheng Longshou Sub-branch, expressly bringing the existing loan in question into the scope of the principal claims secured by the above maximum amount mortgage with a maximum amount of RMB 40 million. Kaisheng Company's appeal argument that the matters agreed in the "Supplementary Agreement" could create a mortgage right only after a change registration of the maximum amount mortgage was completed not only lacked legal basis but also contravened the principle of good faith.

In summary, ICBC Xuancheng Longshou Sub-branch and Kaisheng Company reached a "Supplementary Agreement" to bring the claims under the loan contract of April 20, 2012, into the scope of the principal claims secured by the above maximum amount mortgage. Although no change registration of the maximum amount mortgage was completed, the effectiveness of the maximum amount mortgage still extended to the claims under the loan contract in question that were brought in.

(Judges of the effective judgment: Tao Henghe, Wang Yusheng, Ma Shipeng)

Relevant Legal Provisions

Articles 203 and 205 of the Property Law of the People's Republic of China

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