

Discussion on Existing Claims to Join the Maximum Mortgage Guarantee--Comments on the Guiding Case No.95

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Abstract

The definition of the scope of security of maximum mortgage is not clear and definite under the present legal system, meanwhile in the face of issues such as whether it is necessary to register the alteration of mortgage when the existing claim joins, it is quite common that similar cases are not treated similarly in judicial practice. This paper discusses the issues related to the addition of existing claims referring to the guiding case No. 95.

Keywords

Maximum Mortgage Guarantee; Accession of Existing Claims; Scope of Claims; Alteration of Real Right; Guiding Case.

1. The Proposition of Issue

Theoretical circles have been paying attention to the system of maximum mortgage and deepening the relevant research as the maximum mortgage is widely applied in transaction activities such as commercial bank loans, continuing commercial transactions and and so forth but the requirements of validity of the alteration of maximum mortgage have never been the focus of theoretical dispute. However, the guiding case No. 95 seems to have broken through the doctrine of Registration Effectism of the alteration of maximum mortgage of real estate and has a significant impact on the theory and practice of the theory of Real rights for security.[1]

1.1. The Guiding Case No. 95

1.1.1. The Basic Facts

The Xuancheng Longshou Sub-branch of ICBC has signed the loan contract with the Xuancheng Boguan Trading Co., LTD in April 2012 and signed a guarantee agreement with Jiangsu Kaisheng Real Estate Co., LTD. According to the guarantee agreement, Kaisheng Co., LTD established a maximum mortgage for the related four companies with a home plaza under its ownership and registered the maximum amount of debt of 40 million yuan in order to guarantee the debts of Boguan Co., LTD and other three companies to Longshou Sub-branch based on the loan contract. Kaisheng Co., LTD and Xuancheng Longshou Sub-branch signed a Supplementary Agreement which clearly transferred the claims under the loan contract signed by Longshou Sub-branch and Boguan Co., LTD in April 2012 into the claims scope of maximum mortgage later on. However, there is no replacement registration of the supplementary agreement and Boguan Co., LTD failed to repay the loans involved on schedule.

1.1.2. Key Points of Judgment and Court Decision

The court held that a claim that exists before the creation of the maximum mortgage interest may, with consent of the parties, be included in the claims secured by the maximum amount of mortgage, but this is neither the content of creating the maximum mortgage nor the content of changing the maximum mortgage. As long as the number of claims included is still in the limit of the maximum amount of claims guaranteed by the maximum mortgage, even if the maximum

mortgage has not been alteration, the effect of the maximum mortgage still reaches the claims transferred but it shall not adversely affect a third party.[2]

1.2. The Proposition of Specific Issues

In the guiding case No. 95, the Supreme Court held that the addition of the existing claims did not belong to the alteration of the scope of claims, so there was no need to register the alteration. However, in the case of China Industrial Bank and Xiangqi Inc. , the court considered that the existing claims are included in the claims guaranteed by the maximum amount of mortgage which belongs to the alteration of the scope of claims and the alteration can become effective only after the parties register the alteration. It can be seen that whether the addition of existing claims is a alteration in the scope of claims is an important bifurcation point in such cases in judicial practice. Therefore, it is necessary to discuss this issue.

2. Alteration of the Scope of Claims Guaranteed by Maximum Mortgage

2.1. The Comprehension of the Scope of Claims

The scope of claims stipulated in the maximum mortgage guarantee refers to which claims can be included in the scope guaranteed by maximum mortgage, which is the primary relations of maximum mortgage in theory.[3] As the claim guaranteed by the maximum mortgage is uncertain when the claim is created, if the scope of the claim is not clear in the maximum mortgage guarantee, it is likely to include the accidental debt such as the unjustified benefits obligation and tort obligation between the mortgage parties into the guarantee scope. Then can the primary relations become the standard to limit the scope of claims? There are three main views on this issue around the world at present.[4]

Restrictivism holds that only the claims generated based on certain primary relations can be the claims guaranteed by maximum mortgage. Unrestrictionism holds that the claim guaranteed by maximum amount mortgage is not restricted by specific basic relations, and any non-specific claim between creditor and debtor can be the claim guaranteed by maximum mortgage. There is also General Restrictionism represented by Japanese legislation which is the Japanese Civil Code does not allow the maximum mortgage to guarantee all possible claims between creditor and debtor, and requires both parties to agree on the scope of claims guaranteed in the mortgage contract. The limitation of the scope of claims depends on the free will of the parties in principle.[5] In the above three patterns, General Restrictionism is more reasonable and adopted by most countries in the world.

Article 60 of the original Security Law of China defines two kinds of claims that can be guaranteed by maximum mortgage: one is loan contract and another is contract which is created for a commodity in a certain period of continuous trading. This provision is the application of Restrictionism. The followed Article 203 of the original Property Law and Article 420 of the Civil Code made more reasonable provisions on the identification of the scope of claims which is the claims should continue to occur within a certain period, but neither of these two laws made mandatory provisions on whether the parties should agree on the type of claims in advance.

2.2. The Accession of Existing Claims and the Alteration of the Scope of Claims

2.2.1. The Legal Basis for Adding Existing Claims to the Scope of Claims

According to the article 420 paragraph 2 of civil code of the people's republic of China, a claim that exists prior to the creation of the maximum mortgage for floating claims may, upon consent of the parties, be included in the claims secured by such a mortgage. Although the claims guaranteed by the maximum mortgage is the non-specific claims, the non-specific here means that the claims guaranteed by the maximum mortgage will alteration and be uncertain before

the coming of the settlement period, and the alteration of a specific claims alone will not affect the maximum mortgage. [6] That is to say, the newly added existing claims are only part of the guarantee of the maximum mortgage, and the existing claims may also be eliminated due to some reasons, such as the debt has been paid off. The actual amount of the claims guaranteed by the maximum mortgage is uncertain before the final settlement period. Adding existing claims to the claims guaranteed by the maximum mortgage reflects the principle of autonomy of will in civil law and does not affect the legislative purpose of establishing the maximum mortgage guarantee system.

2.2.2. Whether the Accession of Existing Claims is the Alteration of the Scope of Claims

The alteration of the scope of guaranteed claims is to alteration the basic legal relationship of actual claims through negotiation between mortgagee and mortgagor, that is, to readjust the scope of claim guaranteed by maximum mortgage. Theoretical circles holds that the scope of claims alteration mainly has the following three cases. [7]

(1) Substitution: the claims guaranteed by agreement is replaced by other different claims, for example, the claim generated by the sales contract of guaranteed electrical products is alterationd to the claim generated by the sales contract of clothing products. (2) Addition: one or more types of claims are added to the original agreed scope of claims and each new type of claim is added to a new basic legal relationship (3) Reduction: some basic guarantee relations are reduced under the condition that other basic guarantee relations remain unalterationd. For example, the original agreement to guarantee the claims arising from the sales contract of electrical appliances and clothing is alterationd to guarantee only the claims arising from the sales contract of electrical products. [8]

In guiding case No. 95, the scope of claims guaranteed by the Jiangsu Kaisheng Real Estate Co., LTD and the Xuancheng Longshou Sub-branch of ICBC in the maximum mortgage contract is the claims generated by the loan contract signed by Boguan Co., LTD and other three companies with the Xuancheng Longshou Sub-branch of ICBC. The newly added existing claims are also those arising from the loan contract between Boguan Co., LTD and Longshou Sub-branch, without any alteration in the scope of claims.

3. Requirements of Validity of Claims Accession

3.1. Requirement of the Consent of the Third Party

3.1.1. Legal Basis for the Consent of the Third Party

The Article 409 Paragraph1 and the proviso of Article 422 of China's Civil Code entitle the third party to decide whether to alteration the maximum mortgage guarantee. The provisions of these two articles can be understood in this way: first, if the alteration of the maximum mortgage has an adverse effect on the subsequent mortgagee, the consent of the mortgagee shall be obtained, and the alteration registration can only be handled by holding the written materials agreed by the third party. Second, the provision can be applied by analogy to other interested third parties.

3.1.2. Transfer of the Existing Claim does not Require the Consent of the Third Party

Take the subsequent mortgagee as an example, the adverse effect on the subsequent mortgagee is manifested in the reduction of the amount of priority compensation. However, the inclusion of claims arising from normal transaction relationship into the scope of guarantee does not necessarily result in the reduction of the actual priority of the subsequent mortgagee. Since the maximum limit is determined, the subsequent mortgagee also knows the specific amount of the maximum limit when establishing the mortgage. Since establishing a new mortgage on the mortgaged property is chosen, it can be predicted that the risks that will occur in the future when establishing the mortgage. Incorporating existing claims into the scope of guaranteed

claims will occupy a certain amount of guarantee amount, but the scope of priority compensation of the mortgagee with the maximum amount is limited to the maximum amount so the risk faced by the subsequent mortgagee does not increase and the actual priority compensation may not decrease. Therefore, it is not necessary for the third party to agree to transfer the claim in the normal transaction relationship to the claim guaranteed by the maximum mortgage.

3.2. Alteration of the Requirements of Registration

For whether the existing claim needs to register the alteration, it should be analyzed based on the time point of the existing claim. If the parties agree to join the existing claims for the first time registration, there is no need to go through the registration of alteration because the scope of the registered claims already includes the existing claims that have joined. And if the existing claim is negotiated after the completion of registration and the maximum mortgage guarantee has been established, it is not an alteration of claim scope and the registration of alteration is not required. Another case is when the term of maximum mortgage guarantee expires and the final claims has been determined, the parties can negotiate to join the existing claim. Essentially the maximum mortgage guarantee has been transformed into ordinary mortgage guarantee because the maximum mortgage guarantee has been completed, so the party should undertake the alteration registration of ordinary mortgage guarantee.

4. Referential Application and Limitations of the Judgment Rule of the Guiding Case No. 95

4.1. The Applicable Strengths of the Judgment Rule of the Guiding Case No. 95

The guiding case no. 95 seems to be a partial breakthrough of the doctrine of the registration and effectiveness of the alteration of the maximum mortgage of real estate but in fact it is to expand space for the free agreement of the scope of claims of the maximum mortgage. [9] The rationality behind it lies in the advantages of maximum mortgage system. Hence the judgment rules of the guiding case No. 95 should be summarized as follows: the validity of the agreement between the parties to transfer the specified claim to the claim guaranteed by the maximum mortgage is irrelevant to registration, but the parties shall not include the claim not based on the normal transaction relation and cause unforeseeable damage to the third party. For the limitation of the scope of claims, it should be based on the normal transaction relations between the parties and exclude the claims which is irrelevant to the normal transaction.

By defining the judgment rule of guiding case No. 95 as the transfer of specific claim to the scope of guaranteed claim and implementing the principle of freedom of contract as well as expanding its reference scope to the alteration of the scope of claims, the negative position of generalized maximum mortgage can be alleviated and the system function of maximum mortgage can be further brought into play.

4.2. The limitation of the Judgment Rule of the Guiding Case No. 95

The limitation is that the rule cannot be applied by analogy if the parties agree to alteration not the scope of claims but the settlement period or the maximum amount. The logic lies in that the alteration of the scope of claims is difficult to affect the trust of an unspecified third party. Even if the scope of claims guaranteed by the maximum mortgage is recorded in the real estate register, the third party cannot judge the residual value of the mortgaged property according to the scope of claims or judge whether the maximum mortgage right has been determined which means it fails to protect trust interests but the alteration of settlement period and maximum amount will destroy the trust foundation of the third party and adversely affect its interests.

5. Conclusion

Starting from the guiding case No. 95 issued by the Supreme People's Court, this paper discusses the scope of claims guaranteed by maximum mortgage, and holds that the scope of claims in maximum mortgage guarantee refers to what kind of basic relations should be included in the scope of guarantee and the accession of existing claims is not an alteration in the scope of claims, nor will it destroy the trust basis of the third party and it doesn't require the consent of the third party. The accession of the existing claims follows the principle of contract freedom and its validity is irrelevant to registration which means the effect of alteration of real right can be produced without registration of alteration. The judgment rule of the guiding case No. 95 should be summarized as follows: the validity of the agreement between the parties to transfer the specified claim to the claim guaranteed by the maximum mortgage is irrelevant to registration, but the parties shall not include the claim not based on the normal transaction relation and cause unforeseeable damage to the third party. For the limitation of the scope of claims, it should be based on the normal transaction relations between the parties and exclude the claims which is irrelevant to the normal transaction. The above-mentioned rules can be analogously applied to the alteration of the scope of claims, namely the substitution, addition and reduction of types of claim, but cannot be analogously applied to the alteration of the final settlement period and the maximum amount.

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