

上海市宏志律师事务所

HENRY ZHUANG & PARTNERS

上海市浦东新区浦东南路 256 号华夏银行大厦 2006 室, 邮编: 200120

电话: (86-21) 5115-0828 (总机) 传真: (86-21) 5115-0806

#2006, Hua Xia Bank Tower, 256 Pudong Nan Road, Pudong, Shanghai 200120

Tel: (86-21) 5115-0828 (General Line) Fax: (86-21) 5115-0806

E-mail: info@hzlawyers.com Website: <http://www.hzlawyers.com>

NEWSLETTER

(Henry Zhuang & Partners)

28 December 2000

**JUDICIAL INTERPRETATIONS ON THE SECURITY LAW OF THE
PEOPLE'S REPUBLIC OF CHINA**

In respect of the Security Law of the People's Republic of China, China Supreme People's Court issued a judicial interpretation which has been implemented as from 13 December 2000.

The said judicial interpretation consists of 7 sections and 134 clauses, and includes quite a lot of very important judicial interpretations. The following are some examples.

1. **Approval and Registration of External Security**

1.1 According to the said judicial interpretations, an external security without approval from or registration with the relevant authority in charge will be held as an invalid security. The said judicial interpretation does not have interpretations regarding the said "relevant authority in charge". However, since the security in question is the external security, we believe that the "relevant authority in charge" should be or at least include the State Administration of Foreign Exchange ("SAFE").

1.2 As such, if a property is mortgaged to a foreign lender without approval from or without registration with SAFE, the mortgage will be held invalid even if the mortgage is registered with the relevant real estate department.

2. **Amendment and Assignment of the Principal Agreement**

After an external security is created, if the principal agreement (the loan agreement) is amended or if the lender assigns its rights under a security document, both the consent from the security party and the approval from the relevant authority in charge are required, failing to obtain any one of them will result in having the security terminated.

3. **Invalid Foreign Exchange Guarantee**

A foreign exchange guarantee will be held invalid if it is issued by a financial institution that is not specially permitted to carry on foreign exchange guarantee business, or issued by a non-financial enterprise that does not have foreign exchange income. As such, it will be important for a foreign lender to examine the capacity of a guarantor before acceptance of the foreign exchange guarantee.

4. **Restrictions on Security Party's Liability**

4.1 In case the principal agreement (the loan agreement) is valid and the security document is not valid, provided that the lender is not at fault in respect of the invalidity of the security document, the borrower and the security party shall jointly and severally be liable for the lender's damages. However, if both the lender and the security party are at fault, the portion for which the security party is liable shall not exceed one half of the outstanding amount that the borrower is unable to pay.

4.2 In case both the principal agreement (the loan agreement) and the security document are or become invalid, if the security party is not at fault, the security party shall not be liable for the lender's damages. However, if the security party is at fault, the portion for which the security party is liable shall not exceed one third of the outstanding amount that the borrower is unable to pay.

5. **Legal Representative**

If a legal representative of an entity executes a security document without power of authority, unless the lender is or should be aware of the same, the security document shall be binding on the entity.

6. **Term of Security**

6.1 In respect of a security over a property, an important interpretation is that the term of security as being agreed by the parties or registered with the registration authority shall all be ignored when determining the effectiveness of the security. In addition, according to the said interpretation, if a security is created over a

property, the lender shall be entitled to enforce its right under the security within 2 years after the expiry of the litigation prescription in respect of the indebtedness of the borrower.

6.2 In respect of a guarantee, if the term of the guarantee as agreed by the parties will be expired on or before the maturity date of the loan, the term of guarantee shall be deemed as being not agreed, and the term of guarantee shall be regarded as being 6 months after the maturity date. If a guarantee stipulates that the guarantee is a continuing security and shall remain effective until payment in full by the borrower, such a stipulation will be deemed ambiguous and the term of guarantee will be held as being 2 years after the maturity date of the loan.

7. **Priority**

If both a registered mortgage and a pledge are created over a same asset, the mortgagee will be given priority in receiving the sale proceeds of the asset when the asset is to be disposed of. If both a mortgage and a lien exist in respect of a same asset, the person who is entitled to a lien will be given priority in receiving the sale proceeds of the asset.

Upon request, we may provide you with a copy of the Guidance (in Chinese) and/or the Measures (in Chinese).

Yours faithfully,

Henry Zhuang & Partners
#2006, Hua Xia Bank Tower
256 Pudong Nan Road, Pudong, Shanghai 200120,
the People's Republic of China
Tel: (86-21) 5115-0828
Fax: (86-21) 5115-0806
E-mail: info@hzlawyers.com
Website: <http://www.hzlawyers.com>

Disclaimer

Any legal information contained in this newsletter is general in nature and laws and regulations are changing from time to time and compliance will always depend upon the particular circumstances. We have not attempted to give exhaustive descriptions of law or to give a legal opinion on specific legal issues. You should not rely on this newsletter as a legal advice for any particular purpose.