

The Application of The Arm's Length Buyer Rule in The Context of The Civil Code

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Abstract: Based on the consideration of protecting the interests of transactions, article 404 of the civil code extends the normal business buyer rule to the chattel mortgage and stipulates the constituent elements of the rule. The business activities cannot exceed the scope of the business license, and the goods are for continuous sale; Actual payment is required, but not limited to monetary form; Ownership is required, but actual possession is not required. As for the excluded application, the continuous sale of production equipment is not included in the excluded application; The existence of control relationship does not necessarily exclude the application; Bona fide elements can be added to the identification of the cover clause. The application of this rule can block the recovery of chattel mortgage, but it is still bound by paragraph 2 of article 406.

Keywords: Normal operation buyer, Trading interests, Retroactive effect, Gold supernumeration.

1. Introduction

The establishment of the normal buyer rule is of great significance to protect the interests of market transactions, while its legal effect of blocking the retroactive effect of property rights makes the academic community pay more attention to the rule. The expansion of the scope of application of the normal buyer's rule from floating mortgage to general mortgage of movable property in the Civil Code has led the legislator to make corresponding provisions on the conditions of application of the rule in Article 404 of the Civil Code and Article 56 of the Judicial Interpretation on Security, many details of which still need further discussion. Such as whether the business activities can exceed the scope of business recorded in the business license; whether the acquisition of the subject matter requires actual possession; whether the subjective good faith of the buyer is required; and how to determine the quantity of goods purchased by the general buyer.

2. Consideration Based on Transaction Interests

According to Article 404 of the Civil Code, a buyer who acquires mortgaged property by paying a reasonable price in the course of normal business activities is subject to a mortgage on movable property. This article extends the scope of application of Article 189(2) of the Property Law to mortgages on movable property, which forms the basis for the rule of arm's-length buyer in the era of the Civil Code. Opponents argue that the establishment of the arm's-length buyer rule would shake the foundation of the mortgage security system because blocking the retroactive effect of a chattel mortgage would undermine the credit of a security right created for financing or other transactions prior to the sale of the chattel[1]. There is some truth to this argument, but the legislator chose the latter over the transactional interests represented by the arm's length buyer rule, making it an exception to the retroactive effect of a chattel mortgage. The interests of the transaction represented by the rule include the following two main points:

First, the exemption of consumers from the obligation to

inquire about transactions. According to Article 406, paragraph 1, of the Civil Code, movable property encumbered by a mortgage is transferable and the mortgage is not affected by the transfer. In this context, if the arm's-length buyer rule does not apply, a consumer who wishes to acquire a movable asset free of encumbrances must search the security register before the transaction to determine whether the movable asset is encumbered by an encumbrance, thus creating a duty of search for the consumer. The importance of the arm's length buyer rule is that it exempts consumers from the obligation to search prior to the transaction, allowing buyers who meet the conditions for application of the rule to acquire unencumbered title.

Second, to maintain transaction security, reduce transaction costs and enhance transaction efficiency. According to the movable mortgage registration system, the movable mortgage can be recorded in the security register against third parties, which means that the consumer has to bear the risk of the mortgage of the goods. If the buyer's goods are encumbered by a chattel mortgage, the mortgagee may receive priority payment for the goods purchased by the buyer according to the retroactive effect of the mortgage, which will seriously affect the security of the transaction. Consumers have to search the security register before purchasing goods, which is obviously not in line with consumer habits and will bring heavy burden to consumers, and if the goods are subject to a mortgage, the mortgagee has to be notified, which will undoubtedly increase transaction costs and reduce transaction efficiency. Consumers are relieved of their obligation to search under the normal business buyer's rule, which reduces transaction costs and improves transaction efficiency; they obtain unencumbered ownership and improve transaction security.

It is important to emphasize that the object of protection of the normal business buyer rule is to a large extent the legitimate interests of consumers[2]. But from the legal provisions of the understanding, the normal business buyer is not limited to consumers, all paid a reasonable price and has acquired the ownership of the movable property transactions of natural persons, legal persons or other organizations belong to the subject of the application of the rule. Such as the purchase of goods for profit merchants are also the subject of

the application of the rules. The buyer in normal business activities is not limited to consumers, but also includes commercial subjects; the purpose of consumption is not limited to life, but also includes production, although there are differences in the subject but the needs in the interests of the transaction is the same. In the context of the increasing variety of movable property transactions and the increasing frequency of transactions, it is the reasonable choice of the legislator that the buyer of normal business activities acquires the ownership of movable property without the burden of rights by paying a reasonable price.

3. The Elements of The Application of The Normal Business Buyer's Rule

3.1. The Applicable Circumstances for Normal Business Activities

The relevant provisions of the normal business buyer rule, in addition to Article 404 of the Civil Code, are supplemented by the Judicial Interpretation on Guarantees, which sets forth two requirements with respect to normal business activities:

First, the seller's business activities belong to its business license clearly recorded in the scope of business. In line with the premise of the scope of the record is the seller has a business license, which can be reversed to the identity of the seller's operator, where the "operator" can refer to the application of the Civil Code, Article 312 of the good faith acquisition of lost property with business qualifications of the "operator". The requirement of having a business license to the applicable subject eliminates the possibility of applying the rule to natural persons without a business license, such as second-hand transactions between natural persons and natural persons are not applicable to the normal business buyer rule, through the "salted fish" and other second-hand trading platform completed by the individual to individual second-hand movable property transactions, although there is a network platform as The rules are not applicable even though there is a network platform as a medium.

On the judicial interpretation requires the seller's business activities in its business license clearly recorded within the scope, some scholars believe that the provisions are too strict. Because the practice of business behavior and business license business scope does not match the phenomenon of a few, the effectiveness of this legal act is not clearly denied by law; will be strictly limited to business activities in the business license business scope to a certain extent contrary to the rules to improve the efficiency of the original legislative intent. The view has a strong practical significance, engaged in business activities with the business license scope of different business activities in real life is very common, and even more, first arbitrarily registered business scope and then consider the type of sales of goods, if the strict implementation of the "clear" standard, the role of the rule will be greatly reduced.

However, although the law does not directly deny the effectiveness of operating beyond the scope of business license, but also did not recognize the legality of operating beyond the scope. Beyond the scope of business may produce a violation of the administrative license business behavior, or even illegal business behavior. For the violation of the administrative license, legal norms of business behavior to provide blocking the legal protection of the retroactive effect of the mortgage is obviously unreasonable. The rule requires

that business activities must be within the scope of the business license also has the role of excluding the application of the rule for violations, illegal business behavior. In addition, in the judicial trial in strict compliance with the "clear" provisions have a strong convenience, usually against the business license is to identify the seller's business activities are normal the simplest way[3]. In judicial practice, based on whether the operator of the goods sold in the scope of the business license to determine whether the seller is engaged in business activities are normal, simple and clear with strong operability.

Second, the continued sale of similar goods. The goods should be in the scope of the business license records and for movable property. In judicial practice can refer to the "inventory" standard, to determine whether the seller of goods sold in line with the continuous sale of similar goods elements. The seller of goods sold should have continuity, that is, in a period of continuous sales of certain types of goods, such as food sales sellers, should be in a period of continuous sales of food commodities, if there is an interval, or at a point in time interrupted the sale of food commodities may affect the "continuous" determination, as to how long the interval, how to determine the point in time. How long the interval, how to determine the time point, the judicial interpretation does not provide, which also leaves room for the discretion of the judge. In addition, the way in the transaction of goods, should be in line with their own or the industry's customary practices[4].

3.2. The Buyer Has Paid A Reasonable Price

The reasonable price paid by the buyer is the main means to balance the interests of the mortgagee, the buyer and the seller in the context of the rule. If the buyer and the seller have entered into a contract but the buyer has not paid a reasonable price, the normal business buyer rule cannot be applied. The judicial interpretation does not provide for "reasonable", and it is generally believed that the interpretation of reasonable should include:

First, it can be interpreted in the same way as the "reasonable price" in Article 312 of the Civil Code, that is, the principle of equal price should be applied, and the price paid should be approximately equal to the price of the goods. Whether the price is reasonable, some scholars believe that it can be measured based on the normal market price, the parties' agreement, the delivery method, whether the movable property is unique and the transaction habits and other factors[5]. In addition, reference can be made to the relevant provisions that the reasonably fluctuating price of the transfer does not exceed thirty percent of the guide price of the place of transaction or the market transaction price, and not less than seventy percent.

Secondly, the price paid is not limited to the form of money, but other alternatives to money are also possible, and it is worth discussing whether in-kind is also included. It should be considered that the payment in kind can also be a way to pay the price, whether it is in money or in kind, it has property properties for the seller, and the bartering method is not much different from the payment in money.

Third, the payment of reasonable price does not require the payment of the full price, the buyer if the buyer has paid most of the price can also apply the normal business buyer rule, it is worth discussing whether the deposit has been paid can constitute the payment of reasonable price, the author believes that only the payment of the deposit does not meet

the requirements of the payment of reasonable price. On the one hand, the deposit usually accounts for only a relatively small part of the reasonable price to be paid, which does not achieve the role of balancing interests, and although the deposit can prove the possibility of full payment by the buyer, it cannot guarantee that the buyer will definitely pay the remaining price in full; on the other hand, for the purpose of preventing malicious collusion between the seller and the buyer to the detriment of the mortgagee, if the deposit is paid, it is in line with the requirement of paying a reasonable price, which means that On the other hand, for the purpose of preventing malicious collusion between the seller and the buyer to the detriment of the mortgagee, if the payment of deposit meets the requirement of paying a reasonable price, it means that the buyer only needs to pay a small part of the actual price to acquire the ownership of the movable property free of the encumbrance.

Fourth, it is required that the price has actually been paid. If the defaulted payment has obtained possession of the movable property but still cannot apply the normal business buyer rule, for the sake of balancing interests and to prevent malicious collusion between the seller and the buyer, the price must have been actually paid, such as arrears, playing notes and other acts do not constitute actual payment.

3.3. The Subject Matter Is Movable Property and The Buyer to Obtain

The normal business buyer rule applies to all movable property, but does not include real estate, property rights. That is, the seller is required to sell goods should be movable property, housing, construction land use rights, sea use rights, etc. are not applicable to the normal business buyer rules.

The movable property sold should be acquired by the buyer, the judicial interpretation does not explain the "acquisition", but it is generally believed that the "acquisition" refers to the acquisition of ownership of movable property[6], that is, the buyer has completed the transfer of ownership based on the transfer of ownership rules, has acquired from the seller The buyer has acquired ownership of the movable property sold. If the buyer has not yet acquired the ownership of the movable property sold, that is, the ownership of the movable property has not been transferred to the seller, then the issue of the retroactive effect of the blocking mortgage will not arise, only when the buyer has acquired the ownership of the movable property sold, then the issue of the retroactive effect of the blocking mortgage attached to the movable property sold will arise. It can be seen that the acquisition should refer to the acquisition of the ownership of the movable property, and the mere possession of the movable property is not included in the semantics.

What needs to be discussed is whether direct possession is also required of a buyer who has acquired title to the movable property. The general view of the academic circle is that only the buyer in ordinary course of business is required to acquire the ownership of the movable property, and there is no requirement on whether to take possession of the movable property. On the one hand, when the buyer in normal operation has acquired the ownership of the movable property, the retroactive effect of the mortgage will be blocked, and it is no longer important whether to take possession or not. On the other hand, the requirement of taking possession of the movable property while acquiring ownership is too strict for the buyer in normal operation, and is also a restriction on the mode of delivery, when the seller and the buyer take

possession of the movable property by way of re-determination and proposed delivery, and do not take direct possession of the movable property. Requiring the buyer to take direct possession of the movable property implies a restriction on the use of delivery methods such as possession modification and proposed delivery, which is obviously unreasonable.

3.4. Exclude the Application of Circumstances

Article 56 of the Judicial Interpretation on Warranties provides five circumstances that preclude the application of the arm's-length buyer rule.

First, the quantity of goods purchased significantly exceeds that of the general buyer. Here, the number of goods purchased by the general buyer is used as the judgment standard, and the number of goods purchased by them can be judged based on multiple factors such as industry norms, market environment, geographical characteristics, and seasonality. The judgment of the general buyer also differs depending on the identity of the buyer, for example, the quantity of goods purchased by enterprises and institutions is generally more than the quantity of goods purchased by ordinary consumers. The judgment of the number of goods purchased by the general buyer is complex, difficult to abstractly generalize, and difficult to have uniform regulations. In practice, the parties may combine a variety of factors mentioned above to prove the evidence.

Second, the purchase of the seller's production equipment. The production equipment in this subparagraph refers to equipment used by the seller to produce goods rather than equipment sold as goods. If the seller sells the production equipment as merchandise and continues to sell it, then this subparagraph cannot be used to exclude the application of the arm's length buyer rule. Article 404 of the Civil Code alone already excludes the application of the purchase of the seller's production equipment because the sale of production equipment by the seller is no longer a normal business activity. First, the scope of the business license would not normally include the seller's production equipment; second, the production equipment could not be sold continuously. Judicial interpretation will be listed in this case, one is because this situation in practice is very common, the second is generally higher production equipment security amount, the mortgagee's interests are more damaging.

Third, the purpose of the contract is to guarantee the performance of the debt by the seller or a third party. In this case, although it has the appearance of a sales contract, its essence should be a security contract, which is inconsistent with the purpose of the normal operating buyer's rules to protect the interests of the transaction, and should be excluded from the protection of the normal operating buyer's rules. Contracts entered into for the purpose of securing the performance of a debt shall be subject to the relevant provisions on the subordination of the validity of a mortgage by reference to Article 414 of the Civil Code. It is difficult to judge the true purpose of a sales contract, and in practice, it needs to be considered based on the content of the contract, the affiliation between the seller and the buyer, and other factors.

Fourth, the buyer has a direct or indirect control relationship with the seller. Control relationship refers to the dominant and decisive influence on personnel, financial, business and other important management matters of other enterprises. In most cases, the control relationship is reflected

in the shareholding ratio, but judging whether there is a control relationship based on the shareholding ratio is only one of the ways, and because different companies have different equity settings, it is difficult to reach a fixed value of the shareholding ratio of the control relationship, in practice, should combined with the shareholding ratio, senior management, director seats, the existence of control agreements and other factors to determine the existence of the control relationship[7]. Practice should also pay attention to the difference between affiliated relationship and control relationship, affiliated enterprises do not mean that there is a control relationship. When the buyer and the seller have a controlling relationship, the two sides have the possibility and convenience of colluding in bad faith to damage the mortgage, but the controlling relationship between the buyer and the seller does not necessarily produce the effect of damaging the mortgage, if the buyer has paid a reasonable price and the transaction has the rightfulness, for the purpose of protecting the interests of the transaction, the normal operation of the buyer rule should not be excluded.

Fifth, the buyer should search the mortgage registration but did not search other circumstances. As the bottom clause of the exclusion of the normal business buyer rule, the provision leaves room for the legislator to supplement the exclusion of the circumstances, so as to facilitate the exclusion of the circumstances found in practice, to supplement the provisions. However, this provision also leaves a hidden danger for the judicial practice of the trial judge to exclude the application of the normal business buyer rule. Some scholars suggest that the standard of the buyer's good faith can be used as the standard, that is, the buyer knows that its purchase will infringe the mortgage right, the normal operation of the buyer rule can be excluded from the underwriting clause.[8] This view deserves recognition. The good faith criterion can be one of the considerations that should be inquired but not inquired, but the subjective good faith element imposed on the buyer can only be one of the reference factors for the application of the tout clause, because Article 404 of the Civil Code does not require the subjective good faith of the normal business buyer, and if subjective good faith is the general principle, it is easy to make people think that the buyer does not satisfy the subjective good faith to exclude the application of the rule. The bona fide element should not be the only factor to be considered for the underwriting clause, and the specific judgment should be made by considering the circumstances of the case and measuring the degree of damage to the mortgage.

4. The Legal Effect of The Normal Operation Buyer's Rule

4.1. Exceptions constituting Article 403 and Article 406, paragraph 1 of the Civil Code

The important legal effect of the arm's length buyer is to create an exception for the arm's length buyer in the effect of the mortgage on movable property[9], so that the relevant effect of the mortgage does not affect the interests of the arm's length buyer and does not harm the interests of the arm's length buyer. The exception, in particular, is:

First, the exception of the registration of the adversarialism of movable mortgage. Article 403 of the Civil Code provides for the adversarial system of registration of movable mortgage, and the movable mortgage can be registered against third parties. Although the Civil Code does not

indicate which of Article 404 and Article 403 should take precedence, based on the legislative purpose, it is not difficult to infer that the normal operating buyer is not among the third parties against whom the registered movable mortgage can be registered, i.e., the movable mortgage can be registered against third parties in the security register, but according to the normal operating buyer rule, the "third parties " does not include the normal business buyer. Here, it should be clear that Article 404 of the Civil Code does not require the existence of subjective good faith of the buyer, and when the rule is applied, regardless of whether the chattel mortgage is registered or not[10], and regardless of whether the normal operating buyer is in good faith or not, any buyer who meets the requirements of the normal operating buyer rule can counter the retroactive effect of the chattel mortgage.

Second, the exception of "agreement of the parties". According to Article 406(1) of the Civil Code, the parties to a mortgage contract may agree on the transfer of the mortgaged property, such as agreeing that the mortgaged property is not transferable, or agreeing on the way to restrict the transfer of the mortgaged property. However, this agreement is only binding between the mortgagor and the mortgagee and does not have effect on third parties. The "third party" includes the normal business buyer, that is, the agreement of the parties on the transfer of the mortgaged property is not effective on the normal business buyer, and the normal business buyer is not bound by the retroactive effect of the mortgage, and the mortgaged property shall be movable property. If the parties to the security contract agree that the mortgaged property is not transferable and the mortgagor still transfers the mortgaged property, the mortgagee may pursue the mortgagor's liability for breach of contract according to the contract[11], but may not deny the effectiveness of the transfer contract according to the agreement, and the mortgagee may not exercise the retroactive effect of the mortgage when the object of the transfer is the buyer in normal operation. The mortgagee may not exercise the retroactive effect of the mortgage right, and may not discount, auction or sell the mortgaged property for priority payment.

4.2. The Mortgagee May Claim Subrogation in Rem of The Price

Article 404 of the Civil Code shall not be opposed to Article 406, paragraph 2, which states that the mortgagee shall not be entitled to priority in payment for the mortgaged property transferred by the arm's-length buyer, but may request the mortgagee to claim early settlement of the debt for the price paid by the buyer. The reasons are as follows: Firstly, from the perspective of the application of the law, the rule of the arm's length buyer can be regarded as "the transfer of the mortgaged property may impair the mortgage right", which meets the requirements of paragraph 406(2). Secondly, although the Civil Code does not specify the order of application of Article 404 and Article 406, paragraph 2, nor does it use the proviso, from the perspective of protecting the legitimate rights and interests of the mortgagee and balancing the interests of the buyer, the mortgagee and the mortgagee, it should be considered that Article 404 cannot be opposed to Article 406, paragraph 2. Thirdly, when the mortgaged property is transformed into the price, i.e., it loses its specificity, the realization of the mortgage right loses its security. If the mortgagee is not granted the right to be paid in advance for the price paid by the buyer, the interests of the mortgagee will be extremely vulnerable to damage.

Paragraph 2 of Article 406 involves the application of the normal operating buyer and the following issues should be noted: First, the burden of proof that the transfer of the mortgaged property may cause damage to the mortgagee shall be borne by the mortgagee, but the burden of proof shall be lighter, when the retroactive effect of the mortgage is blocked by the normal operating buyer rule and the buyer acquires full ownership, the mortgagee shall be deemed to have completed the proof. Secondly, the paragraph does not presuppose that the mortgagee is notified in time, and if the mortgagee learns of the fact of transfer through other means, he may also request early liquidation and purification. The reason is that the paragraph requires the mortgagee to fulfill the obligation of notice in order to facilitate the mortgagee's timely claim for priority payment of the price paid by the buyer, so as to reduce the possibility of damage to the mortgage, rather than creating an obligation for the mortgagee. If the mortgagee learns of the timely request for early settlement through other means, it should be supported. Thirdly, the amount of the request shall be based on the mortgagee's claim, and if the price paid by the buyer is not enough to satisfy the debt, the mortgagee shall make up the amount, and the excess shall belong to the mortgagee.

The claim of subrogation in rem is the main means for the mortgagee to realize the satisfaction of the claim after the retroactive effect of the mortgage is blocked, and it is also an effective means to protect the interests of the mortgagee after the application of the normal operation buyer's rule. For the sake of protecting the interests of the mortgagee, the request of the mortgagee for subrogation in rem should be supported after the retroactive effect of the mortgage is blocked, so that the reasonable price paid by the buyer can actually satisfy the debt, so as to achieve the purpose of balancing the interests of the buyer, the mortgagee and the mortgagee in practice.

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