LIÇÕES

TRILATERAL CONTRACTS — THE MACAU EXPERIENCE OF LEGAL IMPLANTATION*[1]

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I. Introduction

Given that our audience is made up of common lawyers at large, perhaps it is a good idea to start with a brief introduction about the Macau legal system before we proceed with the trilateral contracts:

a) The Macau legal system:

The article 5 of the MSAR Basic Law provides: "The socialist system and policy shall not be practiced in the MSAR, and previous capitalist system and way of life shall remain unchanged for 50 years". Article 8 adds that: "The laws, decrees, administrative regulations and other normative acts previously in force in Macau shall be maintained, except for any that contravenes this law, or subject to any amendment by the legislature or other relevant organs of the MSAR in accordance with legal procedures[2]".

It was under such constitutional guarantees that the Macau legal system succeeded the majority of Portuguese law in force immediately before the transition of sovereignty. In this process, the localization of Civil Code was one

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1 I would like to take this opportunity to express my gratitude to Prof. Sze Ping Fat, my learned colleague, who spent hours for the proof reading of this article and gave precious opinions.

2 Macau Basic Law, article 8.

of the pillar-stones. As a result, the Macau Civil Code, with necessary adaptation, retains almost 90% of the original Portuguese Civil Code of 1966.

It is therefore fare to say that Macau legal system, at least in the area of civil law, and the Portuguese legal system remain substantially similar. As a member of the Civil Law family, the Portuguese Civil Code had formally adopted the model of the German Civil Code, which contains a General Part, and a specific part with four divisions, namely, Things, Obligations, Family and Succession. Some modern legal concepts and techniques, such as juristic person, juristic relationship, and juristic transaction etc., developed by German jurists were adopted in the Portuguese Code. However, if anyone concludes from the above formal aspects that the Portuguese Civil Code (or Macau Civil Code) is a copy of the German Civil Code, it might be arguably an over simplification. Notwithstanding its formal and technical similarities with the German Civil Code, a famous scholar of comparative law, Konrad Zweigert, insists classifying the Portuguese Civil Code as a member of the Roman Law family and not the Germanic family[3].

In certain aspects, such an impression is not without ground. In the area of Property Law, the Portuguese Civil Code neither adopts the Principle of Abstraction - which is renowned as a characteristic of German Law - for the transfer of ownership; nor the objective concept of possession. In the area of Obligations, the Portuguese Civil Code of 1966 stipulates in detail the regime of "preliminary contract", which is quite unknown in the German Civil Code. In the areas of Family and Succession, the Portuguese Civil Code preserves a number of traditional rules. If we look into the substantial rules of the Portuguese Civil Code, one cannot help thinking its relationship with both the Italian Civil Code and the French Civil Code.

Without going into further detail, one may conclude that the Macau legal system belongs to the Civil Law Family, which legal rules are mainly made up of statutory law; its Civil Code has benefited from the modern legal science developed from the basis of Roman Law by the French, German, and Italian lawyers. In the domain of property law, this code is characterized by the strict classification of Obligational Rights and Real Rights.

b) The trilateral contract

A trilateral contract is a legal device widely used in real estate transactions in Macau since the late 1980's. It is usually celebrated among three parties, namely, the Promissory Vendor, the Promissory Purchaser, and the Bank financing the transaction.

3 Konrad Zweitgert und Hein Kötz, Einführung in die Rechtsvergleichung, auf dem Gebiete des Privatrechts, Band I: Grundlagen, Chinese Version, pg. 166-167, Law Press, 2003.

The utilization of trilateral contract is normally attached to the transaction of residential or commercial buildings under construction. In this device, normally the promissory vendor promises to sell and the promissory purchaser promises to buy. However, it is the case that most purchasers will pay on a loan, thus bank financing is usually involved in such transactions. It is trite to say that bankers rarely lend money without any guarantee. Therefore, in those transactions, the interests of the bank are to be secured by being joined a party to the same transaction.

In these so called trilateral contracts, a number of relationships are at issue, in accordance with Law 15/2001 of the Macau SAR, published in the 3rd of September 2001[4]: a) the relationship between the promissory vendor and the promissory purchaser, which is classified as a preliminary contract of sale and purchase; b) the relationship between the promissory purchaser and the Bank, which is a contract of loan; and c) a preliminary contract of voluntary hypothec.

At this juncture, the device of trilateral contract is alien to the Portuguese Law. Neither the original Portuguese Civil Code nor the Macau Civil Code has made provision for it.

II. The origin of the trilateral contracts and circumstances leading to the implantation

So far, we have discussed that the device of trilateral contracts which, as mentioned above, was not directly inherited from the Portuguese Law. The next question is: what was the origin of this device and why was it adopted in Macau in the first place?

Adverting to the first question, its reasonably clear that the trilateral contract is a product of legal implantation from Macau's closest neighbor – Hong Kong. This finding appears to be corroborated by the following additional considerations:

- First of all, the transactions supposedly regulated by the "trilateral contracts" in Macau and the "Equitable mortgages of units yet to be completed" are basically the same – that is to say, being transactions related to residential or commercial units under construction. Until the late 80's, Macau never had any experience for this kind of transaction. On the contrary, as early as the 50's, some real estate companies in Hong Kong had already started to promote the sale of "units under construction" by installment[5]. Since the economic links between

4 The trilateral contract is now officially named as "A contract of loan attached with a preliminary contract of purchase and sale and a preliminary contract of hypothec".

5 Lu Qiong, A study of the Mortgage of Units in Uncompleted Development, in "Study of Chinese Property Law", Vol. I, pgs. 300 onwards, Law Press, 2002.

Hong and Macau are always close, it is very probable that the Hong Kong model of transaction has been transmitted to Macau.

- In the second place, the author witnessed a good number of trilateral contracts having been used in the late 1980's and the early 1990's for the sale and purchase of properties in Macau[6], with the title "Contract of Purchase and Sale with Mortgage". It must be noted that the concept of mortgage (按揭) is not the equivalence of Hypothec in the Civil Law, it is a common law legal concept (the translation of this concept into Chinese was the contribution of Hong Kong Lawyers).

- In the third place, and most importantly, such transactions involved the participation of the Bank. Since Macau is a small city and Hong Kong the financial center of Asia, many banks had established their headquarters in Hong Kong. The whole set of Banking system operating in Macau at the moment was adopted from its Hong Kong counterpart.

Even with the above consideration, one may be tempted to ask why such a device rooted in common law would be implanted to the established elements of the Civil Law, after all, this is not an easy task. Therefore, apart from the foregoing explanation, which are not by themselves decisive, we are obliged give other supports. For this purpose, we point to the social and legal environment of Macau at the moment when the implantation allegedly took place.

It's worth recalling the Open Policy of China in the late 1970's, which has lead to a sudden and massive increase in the population in Macau[7]. Such a sharp increase in population naturally increased the demand for residential flats. The real estate market in Macau was thus exasperated since the late 1980's.

Such a sudden increase in real estate transactions would require an efficient and safe legal mechanism which is able to balance the interest of all the parties involved. As this was a new issue in Macau, no legal device has been specially developed for the purpose[8]. There appeared the model of "Equitable mortgage of units in uncompleted

6 With the title of "Sale and Purchase Contract with Mortgage".

7 Official data demonstrated that form 1960- 1980 the population of Macau increased only 40% to 241,950; then from 1980 to 1985, the figure jumped to 290,633; and from 1985 - 1990, the figure jumped again to 339, 510; from 1990-1993, the figure is already 395,304. See data provided by the Statistics and Census Service of Macau; Li Pengre, Capacidade de Ambiente e Pressão da População de Macau, Lotus – Revista do Ambiente, no. 22, 2002.

8 The fundamental device provided by law for the transfer of real property was regulated in the Civil Code. However, it deals only with existing and specific things. In this respect, juristic acts that involve the transfer of ownership or the constitution of hypothec in immovable's, which are considered modifications of real rights, have to be notarized. For the purpose of notarization, the vendor has to provide documents to prove his title; on the other hand, the purchaser has to pay the property transfer tax. In both cases, the negotiating parties need to present a number of applications in different government departments in order to gather all those documents required. The issuance of such documents could take months.

developments" which had been functioning in Hong Kong for years.

III. The legal structure of the implanted mechanism in Hong Kong Law

We have concluded that the trilateral contract was originated from the "Mortgage of Units in uncompleted development" in Hong Kong. Therefore, in order for us to have a better understanding of the process of implantation and the legal structure of the trilateral contracts, a brief survey of its relevant law is useful.

Having said that, I have to confess that the audience is much better qualified than me in this particular area. So please correct me if I have mis-stated.

In legal terms, "Units in uncompleted development" is an equitable estate. This statement inevitably leads us to ask what an estate is, and later on, what an equitable estate is.

As far as I understand it, the concept of estate in English Law is not simple and strict forward. It got much to do with the feudal system developed since the middle age and usually comes together with the concept of tenure.

Briefly stated, the concept of "tenure" refers to the process of infeudation; it denotes the type or extent of proprietary rights; whereas the concept of "estate" explains the period of tenure, namely, the period within which the tenant can exercise his right in land[9]. As one famous English jurist K. Gray put it: "...English law cannot be understood except in light of its history and it is the doctrines relating to tenures and estates that the historical roots of English land law are to be found[10]".

The concept of estate is defined by the Black's Law Dictionary as: "The

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9 Both the concepts of tenure and estate have strong historical flavour. In 1066, the King acquired the radical title to all land in the country. Since the English Monarchy succeeded until today, the concept by which the Crown holds the radical title is still valid. It does not mean that the British crown really holds Roman like absolute ownership or proprietary title, but only denotes that the crown has political powers to grant interest in the land and prescribe the residue of unalienated land. TheCrown's radical title also hold together the theory of tenure.
"Under the concept of feudal tenure, the crown's radical title served as a means by which smaller rights of ownership could vest in other persons. These smaller rights were not absolute ownership but instead limited forms of ownership. The principle of feudal tenure worked on the basis that the crown grants possession of land for a defined period of time in return for services of some kind."
"Initially the King could grant land to a lord in return for services of a military nature. The lord was regarded as the tenant of the Crown and in this respect held land from the Crown. The relationship between the Crown and the lord was one of tenure and the period for which the lord held the land was determined by the estate vested in him. The idea of estate was a time in the land rather than a physical piece of land given to the lord. The doctrine of tenure allowed the lord to grant smaller estates to other people, a process called subinfeudation, in return for services.".
See Sukhninder Panesar, General Principles of Property Law, Pearson Education Limited, 2001; pg. 48; E. H. Burn, Cheshire and Burn's Modern Law of Real Property, fifteenth edition, Butterworths, 1994, pgs. 11-20, 25-37.

10 K. Gray, Elements of Land Law, 1993, 2nd ed., pg. 51.

interest which everyone has in lands, or in any other subject of property".

As we can see, the so called "estate" is actually a bundle of rights grouped around a piece of Land or other subject of property.

The English Land Law was restated and modernized by the Law of Property Act of 1925. This act stipulates two types of "estates": the first is "fee simple absolute in possession"[11], which is granted with a fee simple and allows an indefinite period for the exercise of rights in Land; the second one is "term of years absolute" or "leasehold estate"[12], it represents an interest in the land.

Since the alluded definition of estate points to the concept of property, and for a Civil Lawyer like me, may find the two concepts a bit puzzling. In so far as the concept of property may bear upon the concept of estate, Black's Law Dictionary provides the following definition for property: "An aggregate of rights which are guaranteed and protected by the Government."; "commonly used to denote everything which is the subject of ownership, corporeal or incorporeal, tangible or intangible, visible or invisible, real or personal; everything that has an exchangeable value or which goes to make up wealth or estate."; "The term is said to extend every species of valuable rights & interest."[13]. Sukhninder Panesar attempts to explain the concept as the following: "Property is not the thing itself but the right in or over the thing or object in question.". Actually he agrees with Professor Macpherson that the equation of property as things is a misconception[14].

It is therefore obvious that, in Common Law, the legal concept of property is not "things", but rights over things. The so called rights over things are not a single item of right, but a bundle of rights.

Common lawyers sometimes also uses the term "property rights" to denominate the bundle of rights grouped under the concept of property. However, "the legal system does not provide a prescribed method by which property rights should be classified.". "These criteria, developed implicitly by jurist, look to the dominant factors that have influenced the development of property law. These factors are: 1) the nature of the object in question; 2) the sphere of enforceability of the property right in question, and 3) the function performed by the proprietary right in question[15].

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11 E. H. Burn, Cheshire and Burn's Modern Law of Real Property, fifteenth edition, Butterworths, 1994, pg. 91-92; Sukhninder Panesar, General Principles of Property Law, Pearson Education Limited, 2001, pg. 51.

12 The concept of leasehold estate was not originated from feudal doctrines of estate, but as a part of personal property Law. See Sukhninder Panesar, General Principles of Property Law, Pearson Education Limited, 2001, pg. 53.

13 Black's Law Dictionary, 4th Edition, West Publishing Company, 1951, pgs. 1382-1382.

14 Sukhninder Panesar, General Principles of Property Law, Pearson Education Limited, 2001, pg. 7.

15 Sukhninder Panesar, General Principles of Property Law, Pearson Education Limited, 2001, pg. 44.

It is under the first limb that that the concept of real property has developed; as to the nature of the object, we can first distinguish between land and other properties. When the object is land, the proprietary right in question is termed real property.

From the foregoing discussion, we can conclude that both "property" and "estate" are rights. Property can be considered as patrimonial rights, and when these rights refer to land - that is when the object is a piece of land - property is called real property. Estate as such is a type of real property, which content is to determine the time-frame for the exercise of real property. For me, estate is arguably a sub-categroy of property.

Having clarified the concept of estate, we may proceed with the concept of mortgage.

In English law, mortgage is a security for the repayment of a loan.

Depending on the nature of the property in question and the form, mortgage can be legal or equitable. The distinction between legal and equitable mortgage has much to do with the concept of equity and its separation from the Common Law, which also links to English legal traditions[16].

"Units yet to be completed" is equitable property; therefore, it can only be

16 The tradition of this part of the English can be traced back to the Norman Conquest of 1066. The Conquerer at the moment introduced a new legal system to England, however, did not destroyed the original legal system. The existence of two sets of legal rules naturally required two application body, namely, two courts. Such a circumstances gave way to the development of two court systems, which became matured in the end of the 13th century in England. The first of which is the Local court; the second is the Royal Courts, also known as the courts of common law. Whenever the litigant felt he did not received justice in the local court, he had the right to petition to the King and ask for his case to be heard in the royal courts. People later discovered that, who really administered the justice is the royal prerogative. According to common law, the commencement of an action in the royal court required a writ (which is the authorization to commence proceedings). For this purpose, those petitions were usually dealt with by the Chancellor (who was normally a bishop). However, the Chancellor at this point was not a judicial organ. His job was limited to hear the application of the plaintiff and issue the appropriate writs. The grant of writ did not mean that the plaintiff was successful. On the other hand, the writs for the proceedings to commence were normally pre-established. The Chancellor had limited power to invent new writs. Gradually, it was founded that the rigid mechanism of writs could not satisfy the need of pursuing rights. By the contrary, the power of the Chancellor to create new writs had been recognized as a powerful means to achieve this purpose. Therefore, when the restriction was so strong that the Chancellor cannot issue new writs, he started to act directly in the name of the King. Later, in 1474, the he even act directly in his own name. Those cases, decided directly by the Chancellor without the intervention of the Court of Common Law were called cases of equity. The accumulation of those cases gradually developed a set of rules (also with the name equity) parallel to the Common law. From the above, we can see clearly that the equity, like common law, are case law. See Sukhninder Panesar, General Principles of Property Law, Pearson Education Limited, 2001, pg. 61-62; Shen Zhongling, The General Theory of Comparative Law, , Law press, 1994, 2nd ed, pg. 172-174.

the object of an equitable mortgage[17].

Such proprietary rights may be given special meanings in equity, among others, actionable *in personam*.

In common law, it is a general principle that legal proprietary rights are good against the whole world. A judgment of the common law courts is a judgment *in rem* which attaches to the specific *res* or thing in question rather than to a specific person[18].

For Civil Lawyers the distinction between common law and equitable rights is comparable to the classification of patrimonial rights into Real and Obligational Rights.

However, such a comparison may not necessarily work satisfactorily. The point is this, the "equitable property rights" in English law is not simply a right that is good against one person or a small number of persons. It can also be good against a large number of interested parties. By the doctrine of notice, the number of persons bound by the "equitable property rights" may be so large that the difference is of little practical significance.

From the above analysis, we can see that, in Anglo-american Law, the division of Real Rights and Obligational rights has no clear cut. Either "legal property title" or "Equitable property title" can be seen as real rights in the eye of Civil Lawyers.

Transactions over "units yet to be completed" cannot satisfy the requirements and formalities set forth by common law for the acquisition and transfer of legal title. However, since "equity regards that as done which ought to be done", "units yet to be completed" can be the object of "equitable proprietary rights". Moreover, the protection conferred to such rights in equity is almost as strong as in the case of legal property rights.

IV. How the alien device was localized

In our previous discussion, we have stressed that the trilateral contract is an implantation of the legal device of common law and stated the circumstances leading to the implantation.

However, we have not explained yet how, in concrete, the solution in common law was localized and turned into a mechanism fitted to the Macau Law.

Here we go.

First of all, we would like to emphasize that in this so called process of implantation, the Macau Law did not copy the device of equitable mortgage, what

17 "Conveyancing and Property Ordinance" of 1st November 1984.

18 Sukhninder Panesar, General Principles of Property Law, Pearson Education Limited, 2001, pg. 67-75.

was implanted was the overall solution – a contractual relationship with regard to the transaction of uncompleted units with financing and security.

Indeed, the transaction of real property is nothing new. Even the purchase and sale of uncompleted units is not a new matter for the Macau Law. As early as in the 19th century, when the Portuguese Civil Code of 1867 was extended to Macau, the regime of purchase and sale of future objects and the regime of "preliminary contract" already existed, for such purpose.

The new idea really brought forward by the Hong Kong model is the security constituted in favor of the financing bank – that is, the equitable mortgage.

In Continental Law, the favorite security employed in the transaction of immovable is hypothec. According to the principle of speciality, only existing and specific things can be the object of real rights. Hypothec is a real right of guarantee. Therefore, it cannot be constituted over future things – such as residential or commercial units under construction.

As the above discussion has shown, the social and economic needs are the strongest motivators for the development of law. Despite all these difficulties in the legal aspects, transactions had been done through the vague idea of contract – even the legal effects of such contract were not certain at the moment.

Under such circumstances, attempts have been made to tackle this problem. Successive court decisions tried to explain the device through the old concept of "preliminary contract".

While in Hong Kong Law, the transaction is regarded as an equitable mortgage of an equitable estate; it is now interpreted in Macau as a promise of purchase and sale with a loan agreement and a promise of hypothec. Under such an arrangement, the purchase and sale of the equitable estate takes the shape into a preliminary contract of purchase and sale; while the equitable mortgage becomes a preliminary contract of hypothec.

At first glance, it seems that the idea of preliminary contract in Macau Law performance the role of equity mortgage. However, the truth is just the contrary. While the equitable mortgage, with the help of the doctrine of notice, has an effect similar to the *rights in rem*, the device implanted to the Macau Law and constructed through the concept of preliminary contract is strictly *in personam*. This is so because the preliminary contract in Macau Law is purely an obligational contract. It establishes a relation between the parties involved and creates between them the legal rights and duties. According to the definition of the Macau Civil Code, preliminary contract is: "... the convention by which someone is obliged to celebrate certain contract...". In other words, a preliminary contract is an agreement whereby the contracting parties are obliged to celebrate a future contract. This duty created by the preliminary contract is a human action, namely, a declaration of intent, a performance. Therefore, with the advent of the

preliminary contract, the Macau law does not have to deal with the issues of "real rights" and the question of non-existence of object at the time of contracting; the law and practice relating to the sale and purchase (and financing) of units yet to be completed has thus acquired a new dimension.

Such a device, duly recognized in court decisions in Macau, did not attract the attention of the legislature at the beginning. Indeed, the legislature took its first move only in 1988, by the Law 20/88/M. unfortunately, however, such an enactment, with questionable draftsmanship (the scope of application is not abundantly clear), could not achieve its goal.

Only in 2001, by virtue of law no. 15/2001, of the Macau SAR, was the trilateral contract recognized as a contract *in specie*.

A propos however, this enactment has not changed the fundamental structure of the trilateral contract. The intervention of legislation has been limited to the following aspects: 1) recognition of a pre-existing commercial custom; 2) clarification and standardization of the legal effects of the device; 3) imposition of some minor formal requirements.

V. Conclusion

Without going into further detail, the above experience of legal implantation demonstrates at least the extent to which the law has changed in response to social and economic needs and development, particularly in the private sector. When there is a need, sooner or later, there will be a practice, and then, a law validating it.

VI. Epilogue: As to why this topic was chosen

One may wonder why such a local and minor topic was chosen to present in this special occasion.

Nevertheless, if he looks into the origin of the "preliminary contract", all his doubts shall be removed. The regime of preliminary contract in Portuguese Law derived exactly from the regime of "la promesse de vente", first regulated in the French Civil Code, in articles 1589 and 1590.

Therefore, we can also pronounce in loud voice that, trilateral contract is an heir of the French Civil Code, albeit with a bit of the Anglo-Saxon blood.