

Legal Status of the Seller in a Retention of Title Sale of Movables

1. Legal status of the seller in a retention of title sale of movables in a reorganization proceeding (Supreme Court, awarded on April 10th, 2014, 2013Da61190)

A. Issue

The plaintiff agreed to supply goods to the defendant and to retain the title of the goods until the full payment was made. The defendant's reorganization proceeding began while the defendant had not yet completed a part of the payment, despite the plaintiff's supply. The plaintiff filed this lawsuit against the defendant claiming that the delivery of the movables was based on the alleged ownership of the goods, and arguing that as the contract had a retention of title clause, as the defendant had not fully completed the payment, the plaintiff retained ownership of the goods. Both the first and second trials dismissed this filing, as the plaintiff had filed this lawsuit without following reorganization proceedings on the premise that the plaintiff was a reorganizational mortgagee. The plaintiff appealed to the Supreme Court.

B. Headnote

The retention of title sale of movables is a special agreement where the ownership of the seller is reserved when selling and delivering movables until full payment is made. Through such an agreement, the seller intends to obtain and reserve collateral on the claimed price until full payment is made. In the case of a retention of title sale of movables, the ownership that the seller reserved carries the substance of security. Therefore, it should be

treated as a reorganizational mortgage in a reorganization proceeding. This should be done in the same manner as the transfer of collateral. Consequently, the seller cannot exercise the right of repossession of the object of sale (dismissal of appeal).

C. Commentary

Regarding the legal characteristic of the retention of title clause on the sale of movables, there is 1) a suspensive conditional transfer of ownership theory, which interprets the clause as a legitimate agreement on the object of sale, under suspensive condition of full payment. Immediately upon full payment, the buyer will acquire ownership; before full payment, the seller is the owner, and the buyer has the expectant right that they will acquire ownership of the object upon payment; and 2) security by means of transfer after the theory of ownership transfer, which interprets that the buyer will acquire the ownership of the object upon its transfer, and the buyer has merely offered the object to the seller as collateral for security by means of transfer in order to secure the price claim. The court bases its decision on the suspensive conditional transfer of ownership theory in case where insolvency procedures have not been initiated (Supreme Court, awarded on September 7th, 1999, 99Da30534). The court maintains that immovable and movable goods requiring registration cannot be an object of the retention of title sale (Supreme Court, awarded on February 25th, 2010, 2009Do5064). If the suspensive conditional transfer of ownership theory is applied on the insolvency procedure, the seller can exercise the right of repossession as the owner. However, previously, the court's practice of reorganization has treated the seller in retention of title sales as a reorganizational mortgagee. The present ruling acknowledges the legitimacy of the conventional practice of reorganization. The present ruling also holds that the seller of the retention of title sale is not the rightful holder of repossession, but a reorganizational mortgagee. This places emphasis on 'the substance of contract' rather than the 'legal form' after the insolvency procedure is initiated. In principle, the substantive legal status of the creditor before the initiation of the insolvency procedure should be maintained and respected after the initiation of the insolvency procedure. However, in cases like this, it must be noted that the substantive legal

status of the seller before the initiation of the insolvency procedure can be altered after the initiation of the insolvency procedure when considering the purpose of the insolvency procedure.

2. Characteristics of the damages for a delay claim owing to the bankruptcy trustee's delay of the claim for wages before the declaration of bankruptcy (Supreme Court, awarded on November 20th, 2014, 2013Da64908 en banc)

A. Issue

The plaintiff was an employee of Corporation X. Corporation X did not pay the plaintiff's salary and severance pay. The plaintiff filed a lawsuit against Corporation X, which sought to pay for unpaid wages, severance pay, and damages resulting from the delay in payment. During the pendency of litigation, the bankruptcy proceedings of Corporation X were initiated, and the defendant was appointed as a bankruptcy trustee. The original trial stated that the damages for the delay claim were accrued before the declaration of bankruptcy as **the bankruptcy claim** per the Debtor Rehabilitation Act Article 423. Therefore, the damages for the delay claim was dismissed, as the bankruptcy claim could be exercised in the bankruptcy proceedings. However, the damages for delay claim after the declaration of bankruptcy were cited, as they were **the plaintiff's foundational claim**. The defendant appealed.

B. Headnote

[Court Opinion] The Debtor Rehabilitation Act, Article 473 (4) defines **'the claims caused by the trustee's act about the bankrupt foundation'** as the foundational claim. The object of the article is to protect the person interested and proceed with the bankruptcy fairly. This is done by allowing the bankruptcy trustee the authority to manage, dispose of, and frequently pay off the claims during their duty process. Therefore, 'the action of the bankruptcy trustee related to the bankrupt foundation' includes not only the legal act of the bankruptcy trustee, but also the illegal act related to their

duties. **The default of obligation related to the bankruptcy trustee's duties is also included.** The trustee should frequently pay off the employee's wage, which is the part of the foundational claim. The damages for delay of this claim are also part of the foundational claim, as they refer to 'the claims that accrued by the action of the bankruptcy trustee related to the bankrupt foundation' in the Debtor Rehabilitation Act, Article 473 (4) (dismissal of appeal).

[Separate Opinion] The employees' unpaid wages and severance claims are protected as the foundational claim, regardless of when bankruptcy was announced. Furthermore, the damages for delay are the accessory rights that accrued with specific proportions of the original claims. Thus, **both damage claims from the delay of unpaid wages and severance before and after the declaration of bankruptcy are foundational claims, as they belong to the 'wages, severance pay and accident compensation of employees' clause of the Debtor Rehabilitation Act, Article 473 (10).**

[Dissenting Opinion] The Debtor Rehabilitation Act, Article 446 (1) ((2)) defines '**the damages and penalty for delay after the declaration of bankruptcy**' as a subordinated bond. This means that the rights and penalty for damages occur after the declaration of bankruptcy as a result of the continuing relationship of periodic payment of damages because of the nonfulfillment of property claim by debtors prior to declaring bankruptcy. Thus, the damages for delay of unpaid wages (which were accrued before the declaration of bankruptcy and continue afterwards) are **the subordinated claims**, unless there are rules outlined specifically in the law.

C. Commentary

If the separate opinion applies, the employee benefits will be strongly protected, and other creditors' benefits will be relatively damaged. The employee will receive the least amount of protection when the dissenting opinion applies. The employee protection level from the court opinion is lower than that incurred through the separate opinion but greater than that gained through the dissenting opinion. So far, the lower courts' opinions have been divided. Therefore, in practice, this judgement is meaningful in concluding the controversy.

The dissenting opinion criticizes the court's opinion, highlighting the

importance of 'the literal rule' of statutory interpretation. In other words, even if a trustee delays a payment obligation in demand of wages and severance pay, which are estate claims, after declaring bankruptcy, and a claim for damages results from the delay, the claim is not from the act of the trustee regarding 'the bankruptcy estate' as defined in the Debtor Rehabilitation and Bankruptcy Act, Article 473 (4), but from the act of the trustee regarding 'the estate claims.'

In this regard, the court opinion underscores the systematic and teleological approach of legal interpretation. First, the provision of evidence stated by the dissenting opinion appears to be applied to this case in words, but as one of the clauses ruled in the chapter titled 'the bankruptcy claims,' it is not applicable to subject matter referred to as 'the estate claims,' which is stipulated in a separate chapter (the systematic approach). Additionally, whether the trustee performs the payment obligation on demand of estate claims directly or indirectly affects the bankruptcy estate, therefore the default of the trustee regarding the estate claims is equivalent to the act of the trustee regarding 'the bankruptcy estate.' This is in accordance with the purpose of the act, which is protecting the original claim (wage and severance pay claims) by regarding it as an estate claim (the teleological approach).

It is believed that the court opinion is reasonable in that it pursues moderation among dissenting and concurring opinions.

3. Before the commencement of the rehabilitation procedure for the contractor, the construction had already been completed. However, the damages caused by the defect of the completed object occurred after the commencement of the rehabilitation procedure for the contractor. In this case, what is the legal nature of the client's claim for damages against the contractor? (Supreme Court Decision 2011Da109388 decided April 23, 2015)

A. Issue

The defendant (contractor) signed a contract under a guarantee for

repairing defects at the Korea Housing & Urban Guarantee Corporation (Corporation X). Regarding the recourse amount obligation that the defendant must pay in the event that Corporation X performs the obligation to guarantee defect repairs to the client, the plaintiff provided a joint guarantee. Before the rehabilitation procedure commenced, the defendant completed the construction and handed the completed building over to the client. Following the commencement of the rehabilitation procedure for the defendant, defects occurred in the building; therefore, Corporation X implemented a repair guarantee obligation to the contractor, and the plaintiff also performed a joint guarantee obligation to Corporation X. The plaintiff filed a lawsuit claiming for a recourse amount for the defendant. The plaintiff declared that its recourse amount claim is equivalent to a claim for public interests as a claim to the debtor because of the commencement of the rehabilitation procedure.

B. Headnote

1) Rehabilitation claims should include the future claim of the obligations referred to in the Debtor Rehabilitation and Bankruptcy Act, Article 138 (2). In cases in which the joint surety of the debtor secures recourse after the commencement of the rehabilitation procedure by entering into a joint guarantee obligation, such as paying the rehabilitative creditor, who is also the main creditor, if the joint surety contract is signed prior to the commencement of the rehabilitation procedure, the joint surety relationship, which is the main cause of the recourse, is established prior to the commencement of the rehabilitation procedure. Therefore, recourse based on a joint surety contract shall be regarded as a rehabilitation claim, and also as a future claim.

2) If the construction agreed upon in the construction contract has already been completed, it is no longer possible to cancel the construction contract unless there are special circumstances. If it is no longer possible to cancel the construction contract prior to the commencement of the rehabilitation procedure due to the completion of construction and delivery, the contractor shall be deemed to have fulfilled the contract prior to commencement of the rehabilitation procedure.

In this case, even if the damages caused by the defects of the object

occurred after the commencement of the rehabilitation procedure for the contractee, unless there is anything unusual, the contractor's right to claim for damages replacing repairing defects is equivalent to a rehabilitation claim, because it is reasonable to say that the main cause of the claim for damages was provided prior to commencement of the rehabilitation procedure.

C. Review

The logic of the above case is as follows. The contractor's right to claim damages from the defendant is a rehabilitation claim. (See the point of judgment in the 2nd case.) On one hand, X concluded a repair guarantee contract before the commencement of the rehabilitation procedure and reimbursed the defendant for the recovered claim under the contract after the commencement. Therefore, the reimbursement claim to the plaintiff of X is also a rehabilitation claim. On the other hand, before the commencement of the rehabilitation procedure, the defendant concluded a joint guarantee contract with X for the reimbursement claim to the plaintiff, which is a type of rehabilitation claim, and the defendant fulfilled their obligation under the joint guarantee contract after commencement of the rehabilitation procedure. Therefore, the defendant's reimbursement claim to the plaintiff is also a rehabilitation claim. (See the point of judgment in the 1st case.)

The point of judgment in the 1st case is a repetition of the content of the previous case and does not represent new content. It is necessary to pay attention to the judgment point in the 2nd case as new judgment. Even if the claim had not yet occurred at the commencement of the rehabilitation procedure, **the claim may become a rehabilitation claim as a future claim, if the basis or legal cause of the claim already exists** {Debtor Rehabilitation and Bankruptcy Act, Article 138(2), Article 118(2)}. If the construction had already been completed at the commencement of the rehabilitation procedure, it can be said that the basis of the right to claim for damages replacing repair defects occurring only after that time has already been provided. Therefore, the right to claim for damages is not a public claim but a **rehabilitation claim**.

However, if a fault occurs only after a considerable period of commencement of the rehabilitation procedure, it may be practically

impossible for the contractor to report their right to claim for damages to replace the repair defects. The court allows for **a follow-up of the report of the rehabilitation claim** in preparation for this situation (Supreme Court Decision 2014Da82439 decided November 25, 2016).