

ISSUES OF SELLING MOVABLES PLACED IN PUBLIC WAREHOUSE BY AUCTIONS

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1. INTRODUCTION

Different issues arise from selling the tangible assets placed in public warehouse by auction. During the public (executive) auction of personal properties, the protection of proprietary rights and the protection of creditors' interests may conflict. And because the real owner and the effective possessor of goods is not the same person, moreover, public warehouses may have their own creditors claiming for compulsory execution, thus, it is worth reviewing some aspects of this legal situation. In the present study the author summarizes the characteristics of public auctions, the representatives of the public warehouse transaction and the specialties of the legal fate of the chattels placed in public warehouse.

According to the regulations of the *Civil Code* on public auctions, the purchaser in good faith may acquire the ownership of tangible assets from the owner (or become an owner if the asset has not been the property to anybody, in case of original method of acquisition). In this respect, the new *Hungarian Civil Code* did not brought essential changes. As the acquisition by auction constitutes original acquisition, a declaration by the previous owner is not needed.¹

A particularity of the warehouse auction compared to the Civil Code is that in such circumstances the ownership of the goods may also be acquired, even if the depositor was not the owner. However, the rules on the public warehouse auction were determined by the *Act XLVIII of 1996 on the public warehouse as lex specialis*. During the execution procedure it is prohibited as of law to put the goods placed in public warehouse on auction (as well as these goods are not subject to the property of the public warehouse according to the *Act on Bankruptcy Proceedings and Liquidation Proceedings*).

2. POSSIBLE PARTICIPANTS, SUBJECTS AND RISKS OF WAREHOUSE TRANSACTIONS AND THE EXECUTION PROCEDURE

Let us have an overview on the possibility for warehouse goods being the subjects of execution and on the parties or possible participants of the execution procedure. The act on execution has separate provisions on those assets which are exempt from execution² and expressly removes goods and merchandise placed in public warehouse from executable tangible assets.³ Chattel is obviously not the same as the deed issued in relation with the chattel called warehouse warrant, which may be subject to execution and in case of insolvency proceedings it shall be considered an asset of the organization under bankruptcy or liquidation procedure. (Otherwise the liquidation of the weight note possessor may not prevent the possessor of the warrant to claim for sale of the goods according to the provisions of this Act by the public warehouse, the bankruptcy and liquidation of the warrant possessor may not have effect on the right of the weight note possessor.⁴)

The depositor receives a commercially negotiable deed, the so-called warehouse warrant, which is issued by the public warehouse in the form and with the content stipulated in the warehouse act. The warehouse warrant consists of weight note and warrant, and the joint possession of both notes grants the license of the delivery of goods. These tickets – contrary to goods placed in public warehouse as escrow – may be acquired by auction and enforcement, however, the goods itself in public warehouses shall not be drawn into the auction by the executive, or cannot be subjects of a seizure. This also means that with this

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¹ *Act IV of 1959 (old Civil Code)*. The former Hungarian Civil Code had been in force until March 16th, 2014, Section 120.

² *Act LIII of 1994 on judicial execution*, Section 89, Para. (1): It cannot be under seizure – even with the consent of the debtor – those assets which are exempt from execution by the law. (2) If the law stipulates alternatively the round of those assets which are free from execution, the exemption is on the appointed assets by the debtor presented on the seizure. (3) According to the order of the court even not executable goods may get under seizure due to the enforcement of the purchase price, the given loan for the purchase price for the goods, and furthermore for the preparation and repair fee of the goods.

³ *Act LIII of 1994*, Section 96, Para. (1) and (2).

⁴ *Act XLVIII of 1996 on public warehousing*. Section 38, Para. (4) and (6).



original acquisition mode the ownership of goods may not be acquired directly through the auction but “only” by the acquisition of the warehouse warrant.

The main characteristics of warehouse transactions are worth reviewing and we shall also analyze the following problems: Who owns the goods placed in public warehouses? What kind of goods may be placed in public warehouses? Why are goods placed in the public warehouses? What do public warehouses do and what is allowed to do with the goods? How goods are removed from public warehouses? Whose interests would be harmed by the transfer of ownership of movable property by execution auction?

It is also to be monitored against which party of the warehouse transaction may the enforcement procedure proceed; and the problem that whose goods – owned or possessed– may or may not be subject to execution of each execution auctions, shall be construed according to this. The act on enforcement procedure expressly removes the chattels and goods placed in public warehouses from the executable properties, however, does not do so with the warehouse warrant or the public warehouse’s own, executable movable property.

The goods and merchandise that may be subject to execution shall be examined in terms of possible legal acts in the given execution process that is, against whom the enforcement procedure is going on, the public warehouse or the former depositor (or possibly the possessor of the ticket which authorizes disposal). Accordingly, execution procedure may be:

i) *against warehouses* (who is the real possessor of the goods) *as debtors*, where the aim is to take securities on the public warehouse’s owned and possessed asset in the protection of the public warehouse’s creditors,

ii) *or against such person who has a warehouse warrant* (one is entitled to the handover of goods upon the delivery from the public warehouse), thus, may be considered as the owner of goods who is not the possessor and has a creditor but is not warehouse himself.

In both cases the execution may seem problematic, since in the first case the chattel is not owned by the public warehouse, although it possesses it, in fact, it is also possible that it was not owned by the depositor either before it was placed into the public warehouse. Thus, the owner of the goods possessed by the public warehouse in the moment the execution procedure was initiated, may be theoretically unknown as well. According to the act on public warehousing, public warehouses are not entitled and nor obliged to consider whether the depositor is the owner of the goods, and the transfer of warehouse warrants may not be announced to the warehouse either. This fact turns out by the presentation of the warehouse warrant’s endorsement. The warehouse transaction secures that upon the goods placed into the public warehouse the ownership may change several times without moving the goods only by endorsement.⁵

In the second case the creditor tries to acquire the goods from the debtor during the enforcement procedure against the takeover entitled owner. However, instead of the goods, the owner “only” possesses the value note of the goods, the chattel itself is in a safe keeping escrow, as a matter of fact, may be presented in the note issuer public warehouse. In addition, only the joint possessor of the weight note and the warrant may be regarded as a full owner without any restrictions.

2.1. Execution against the warehouse as debtor

In the first case, the warehouse is that commercial organization against which enforcement procedure may be initiated by a creditor on a sort of legal ground. The executive, according to the duly submitted claim of the creditor, which means the request of the claimant possessing the entitled appropriate material may initiate the enforcement procedure.

In public warehouses not only the warehouse’s own asset but escorts placed in the public warehouse may also be found. On the basis of the warehouse act, the public warehouse shall separately store the deposited chattels from its own asset, right up on the protection of the creditors, so the public warehouse

⁵ The warehouse warrant is a negotiable instrument. This means that it is transferable by endorsement as well as the bill of exchange, and the transfer even occurs if the transfer is not in accordance with its notice. The warehouse warrant is transferable together and even with the separate transfer of the warrant and the weight note. The warehouse warrant shall be endorsed upon transfer.

shall state the warehoused stock substance on the value represented on the warehouse warrant monthly, by the 15th day of the following month after the month under review in its financial accounts.⁶

According to the warehouse act, goods placed by the depositor do not become own properties of the public warehouse (only temporary, well separated and registered trust). Therefore, it is necessary to clearly demonstrate it in the act on enforcement that goods placed in public warehouses may not be taken under execution procedure against the public warehouse.

2.2. Execution against the real owner of goods as debtor

Enforcement procedures may be filed against the owner, as debtor as well, who is not a public warehouse but the goods in its property have been previously placed into a public warehouse. This is attested by the warehouse contract and the warehouse warrant issued at the initiation of the custodial escrow. Goods get out of the possession of the owner into the warehouse and the proprietary rights are attested by the negotiable warehouse warrant which certifies the right of delivery. The executive cannot acquire the goods, only the warehouse warrants through seizure if it still in the possession of the owner against whom an enforcement procedure has been brought.

This restraint of enforcement outstands whether the enforcement procedure is against the public warehouse, whether the enforcement procedure is against such third party who claims him/herself as owner or who is entitled to dispose over the goods. Accordingly, the ownership is exclusively expressed by the joint possession of the issued and market circulated warehouse warrant (weight note and warrant), which is an obligation of the public warehouse to deliver the goods.

It is mentioned here that the enforcement auction as a legal instrument of the original acquisition of ownership since the *Hungarian Civil Code* may not be applicable as contracting technique for private auctions.⁷ Recently, the rules of contract law of the Hungarian Civil Code and besides general rules also provisions of agency contracts and contracts of carriage shall be applied, thus, in the case of private auctions it shall only be referred as derivative acquisition of ownership method. Usually, first and foremost may be from the owner, unless exceptions are allowed by the law. Consequences arising from the principle of '*nemo plus iuris*'⁸ and questions of the implied warranty and warranty of title may be geared to this. In this present case the applicability of exemptions allowed by the enforcement law are examined in connection with public warehouse auctions and due to these aspects question of taking goods placed into public warehouses into auction along the above mentioned logic shall be examined.

Public warehouses are such private limited companies or a foreign seated company's branch offices in Hungary which are licensed and are under the supervisory of the State, where goods may be temporarily placed into the custody of public warehouses under contract. Public warehouses' activity is to store and trust the goods under the provisions of the warehouse contract and according to the act on warehouses and issue the warehouse warrant and deliver goods. The public warehouse activity does not mean the right to dispose over the ownership of goods, only their possession and treatment within the applicable legal framework, which means the custody due to the contract, the appropriate treatment during the custody (the preservation of the quality and quantity), and then at the end of the duration of custody it may include the obligation for delivery.

The main feature of public storage operations is precisely a legal ground for a long term but not with a permanent effect, the ownership and the possession of goods (chattels placed in public warehouse) may separate from each other and the ownership may be transferred without the move, transport, or delivery of goods due to the release of warehouse warrants.

Any negotiable asset as following from the warehouse act may be placed into the public warehouse and be public warehouse goods except for cash and security. This is clearly stated in several sections in the act on public warehousing. This is a kind of guarantee against "hiding" money of security for enforcement procedure. The possession of certain goods, may be subject to authority permission. Those may be placed into warehouse only in compliance with the relevant rules of law and on the grounds of an authority permission.⁹

⁶ Act on public warehousing, Section 4/A, Para. (3).

⁷ Légrády, Gergely: *Az árverésről – gondolatok egy Janus-arccú szerzőismódról* [On the Auction – Thought on a Janus-faced Method of Acquisition]. *Polgári Jogi Közlemények*, Vol. 9 (2003) No. 1, 18.

⁸ *Nemo plus iuris ad alium transferre potest, quam ipse habet*. (Ulp. D. 50, 17, 54.)

⁹ *Act XLVIII of 1996*, Section 2, Para. (8).

Due to the exclusive and other exclusionary character of the ownership it shall be protected *eo ipso*, since the autonomy and independence of the individual may suffer harm without the protection of the already acquired assets.¹⁰ The right to property¹¹ secured by the Hungarian *Fundamental Law* may not be harmed either during any enforcement procedure or auction or during public warehouse storage, thus, it would be against the Fundamental Law if the act on public warehousing, the act on implementation and the Hungarian Civil Code were regardless of the ownership of goods involved in warehouse transactions.

Public warehouses draw interested parties' attention to these circumstances. Therefore, goods do not become the property of the public warehouses, only become their possession. However, during the period of public storage operations, goods placed into public warehouses will be replaced by the warehouse warrant in the depositor's assets, since during bankruptcy procedure against the depositor it shall be recorded as assets, and during enforcement procedure, goods placed into public warehouse may not be confiscated, only the warehouse warrant is reserved. Goods placed into public warehouses do not fall within the scope of liquidation procedure.

3. POSSIBLE SUBJECTS OF PUBLIC WAREHOUSE GOODS – THE POSSIBLE TANGIBLE ASSETS OF EXECUTION

The act on public warehousing negatively regulates the question that which goods may be placed into public warehouses. It does not say what tangible asset may be deposited as public warehouse goods but it stipulates that cash and negotiable instruments are not subject to public warehousing.

It is interesting that the German *Civil Code* (BGB) and the *Commercial Code* (HGB) contains provisions not only regarding public warehousing¹² but regarding commercial purchase and loan transactions, as well.¹³ Moreover, in case of further delay, (or, if the chattel may not be eligible to be deposited by its nature) after a new and proper notice, the chattel may be delivered to auction on its market value by the proper entitled person (or even by a free purchase to a third party). In the Hungarian law system similar deposit options for late commercial transactions cannot be found.

In the Hungarian legal system the prohibition of public storage of cash and negotiable instruments is specific. It derives from this negative, exclusion based regulation that anything that is not cash or negotiable instrument may be deposited as moveable asset in public warehouses. This ascertainment is very important as enforcement law contains very specific provisions regarding enforcement actions and how the executive shall carry it out, depending on the possible tangible asset as subjects of the execution. However, if this good is a chattel or merchandise placed into public warehouse, these provisions may not be applicable. Thus, for example, a stock or business shares of a company are deemed as negotiable instruments, those may not be placed in public warehouses.

During the seizure of for example gold, platinum, silver and currencies, the executive takes in the assets and pays the seized foreign currency into the executives' deposit account on the following working day. During the seizure of gemstone and typographically produced negotiable instrument, the executive also takes the assets and deposits it into judicial escrow.

In case of seizure of dematerialized securities, the executive notifies the account managing investment supplier of the debtor, who puts the reserved securities into a locked sub-account according to the statutory provisions of the act on securities until further action by the executive. During the seizure of cash, the executive takes the seized cash and on the following working day it is paid into the executive's deposit account. When museum pieces, books or other things of historic interest or archival material are seized, the executive shall send the prompt notification with a copy of the seizure minutes to the competent museum, library or archives according to the nature of the subject matter. In case of the seizure of vehicles, the executive shall also seize the car documents, registration book, etc.

Therefore, all these acts can only be carried out by the executive if the asset. Whereas, goods placed into public warehouses are not in the possession of the owner of the public warehouse, the seizure may not be

¹⁰ Téglási András: A tulajdonhoz való alkotmányos védelem – történeti áttekintés [The Constitutional Protection of Property – Historical Overview]. *Jog- és Politikatudományi Folyóirat*, Vol. 2 (2008) No. 4, 3.

¹¹ *The Fundamental Law of Hungary*. Article XIII. (1) Every person shall have the right to property and inheritance. Property shall entail social responsibility. (2) Property may only be expropriated in exceptional cases and in the public interest, in legally defined cases and ways, and subject to full, unconditional and immediate indemnity.

¹² HGB §§416, 420

¹³ BGB 372.§ and 383.§ (1).

interpreted on them because the goods may and shall be taken from the owner debtor in order to seizure. However, the warehouse warrant possessed by the debtor may be seized as materialized, typographically construed securities.

According to the provisions of the act on enforcement, the reserved and non-expendable tangible asset – pursuant to the fundament principle – should be left in the custody of the debtor, which may be used by the debtor without the harm of texture or use of material, but may not have the right to alienate or encumber. The breach of these by the debtor is a crime according to the Criminal Code, as well.¹⁴ Another legal difficulty is that in public warehouses it is not the owner who uses and safekeeps the movables, since by giving the goods into deposit only the possession falls out – in totally legitimate way with a conclusion of a warehouse contract – of the hands of the owner to the custodial deposit.

Regarding the movables originally placed in the public warehouse by the debtor it may lawfully arise that during the proper commercial marketing not the former depositor is entitled to dispose over it. Towards the thorough examination of this problem we shall mention auction as a legal title called original acquisition in the Hungarian Civil Code, which is a typical procedural act of the official enforcement procedure.

4. THE ENFORCEMENT OFFICIAL AUCTION AS ORIGINAL PROPERTY ACQUISITION METHOD

According to our former Hungarian Civil Code; the one who acquired the chattel by authority decision or auction in good faith becomes the owner regardless who the former owner was.¹⁵ In the *New Hungarian Civil Code*¹⁶ which came into force in 2014, this provision is unaltered and continually exists. The transfer of the possession of goods is necessary on the auction in order for the auction buyer to obtain the ownership of the chattel. Very important circumstance is the buyer's good faith, since the acquisition requires the declaration and co-operation of the original owner, however entering into contract with him/her is not necessary.

The original acquisition mode, mentioned in the Hungarian Civil Code, comes to an effect only if the auctioneer is an authority, not an individual or a private organization. The official auctioning has two main criteria: *by means of duress* and the process has an official aspect itself that is *a qualified authority body that conducts the auction*.¹⁷

Although, via auction not only ownership and possession is acquired by the acquiring party but also third party rights having encumbered the goods are terminated, in case the purchaser was really acting in good faith. These provisions were not directly included in the former Hungarian Civil Code but the legislative power found it necessary to state these legal details in the New Codex during the re-drafting of the Civil Code reforms.

Actions mentioned in the Hungarian Civil Code mean the transfer in the judicial execution procedure in which the auction buyer with the highest offer may be considered as acquirer. (Here, mentioned regulation of the Hungarian Civil Code may not be applicable for private auctions, moreover, the Hungarian Civil Code has no specific regulations for that at all, however, the general rules of contract law shall be applied.¹⁸ So private auctions – for example auctions on art treasures and books – are not considered as the above analysed original acquisition mode, thus, restrains stipulated during the judicial execution procedure may not be automatically applicable for those either, for example that goods placed in public warehouses may not be taken to auction (court auction).

The Hungarian legal system mentions more than a dozen type of auctions (tax enforcement, restitution auction, business share auction, liquidation auctions, auction on privatization, etc.), and out of them the judicial execution auction is considered as public auction.¹⁹ Public auction is obviously considered as forced liquidation, thus, for example, an ordered auction during the liquidation procedure, as well as the

¹⁴ *Act C of 2012 on the Hungarian Criminal Code*, Section 405, Para. (1): Any person who conceals his assets serving as cover for a debt existing under a contract-made in writing, and thereby prevents settlement of the debt in full or in part is guilty of a misdemeanour punishable by imprisonment not exceeding one year.

¹⁵ 'Previous' *Civil Code*, Section 120, Para. (1).

¹⁶ *New Civil Code* (in effect) Book 5, Section 41.

¹⁷ Légrádi: *op. cit.* 9.

¹⁸ *Ibid.*

¹⁹ *Ibid.* 10.

sale of assets of liquidated organizations (for example a ruined public warehouses), whose rules show significant similarity with court auction rules.²⁰

5. SPECIFIC RULES OF THE PUBLIC WAREHOUSE AUCTION – NO PUBLIC AUCTION

The auction in the act on public warehousing as forced liquidation procedures does not constitute of such elements like public auctions discussed above. The public warehouse is not an authority and even though this auction also includes as many forced items as enough to be ordered without the consent of the depositor, it does not mean an official auction. In case of the existence of the defined legal conditions, the possessor/holder of the warehouse warrant may reclaim the purchase of the goods and the settlement of his/her claim from the purchase price.²¹

Therefore, in this case a specially controlled auction procedure takes place where the rights of third parties are not infringed, the possessor of the warehouse warrant is a party of the public warehouse relationship and the auction is in accordance with the regulations of the act on the warehouses.²² Accordingly, not only the creditors' (warehouse warrant holder) interests are under eligible protection but also the owner of goods during the legal accounting relation stipulated by legislation loses its ownership and reduces its debt to the creditor.

Unlike the official auction, regarding the public warehouse act, on such auction the auction buyer acquires ownership even if the lender was not the owner of goods placed in the warehouse, since the public warehouse may not be obliged to verify the ownership of goods.²³ The public warehouse is only obliged to ensure the quality, quantity and the origin certified by the depositor of goods placed in the warehouse but not the ownership.²⁴

The specific provisions of the warehouse auction in act on public warehousing neither refer to the Hungarian Civil Code, nor does the implementation law determine the date of the transfer of the ownership, it only clarifies the auction, the method of keeping the minutes, the asking price, the knock down and the framework rules of the mandatory contract.²⁵ Both the buyer and the creditor shall be notified about the place and time of the auction, in fact, the seller and the buyer may also make a bid on the auction. (In case of the absence of the notification the debtor is liable for the damages of the creditor.)

6. SUMMARY

According to the above described review it may be concluded that the primary purpose of the law regulating the judicial execution procedure, which is a type of the official auction, is to protect creditors interests even in case of auctioning the assets of debtors.

Contrarily, the act on warehouses allows a non-owner lender to put a chattel into public warehouses (but only those which are not originated from a crime, excluding cash or securities) allowing such situation in which the property of a third person is placed into a temporary escrow custody, where the owner is not or just subsequently notified about the contract (the warehouse contract) between the safekeeper and the depositor.

²⁰ Act IL of 1991 on bankruptcy and liquidation procedure, Section 49.

²¹ *Act XLVIII of 1996*, Section 32, Para. (1): If, the amount stated on the warehouse warrant is not paid to the possessor of the warrant within three days after the expiration, he/she may require the sale of the public warehouse placed goods and the satisfaction from the purchase price. The first endorser has the same right against the possessor of the warrant if he/she redeemed the warrant.

²² *Ibid.*, Section 34, Para. (1) If the goods shall be sold, and on the warehouse warrant stipulated data meets with the conditions of the rules of Budapest Stock Exchange, the public warehouse may sell the goods on the stock market. Subsection (2): If the goods cannot be sold on the stock market, or if the sale failed to seven days following on the stock exchange, the goods shall be purchased by auction. Subsection (3): The buyer acquires ownership even if the depositor was not the owner of the goods both by stock market and auction sale.

²³ *Ibid.* Section 23, Para. (1).

²⁴ *Ibid.* Section 15.

²⁵ *Ibid.* Sections 35-36.

Among others, this is the reason why the act on judicial execution shall contain a clear prohibition, which states that goods placed into public warehouses shall not be the subject of judicial execution procedure (auction). According to the act on public warehousing – since the public warehouse is not the owner but the temporary possessor and custodian of the possessed assets –, is not possible for a creditor's requested and initiated judicial execution procedure (which aims at the debtor's assets) that a custodian may issue such property, whose ownership was not required to be considered during the reception into deposit.