



Basic of Security Interest under Thai Law (1/2)

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Overview

A security interest is a legal right from a debtor given to a creditor upon the asset or property of debtor, usually refers to as the collateral, which enables the creditor to have recourse to the property if the debtor defaults in performing payment obligation. In many countries, the asset to be legally used as collateral might be varied to tangibles and intangibles in some extent. Nevertheless, in Thailand, security interest might be limited to only some kind of assets. This newsletter would clarify you well enough on the scope and implementation under financial mechanism of property eligible for performing as collateral in deeper perspective, especially, for real property, movable assets and shares. In the next newsletter, the readers would see more on another interesting concept for security upon intellectual property, business, and receivables, to help readers see through Thai legal concept and its limit of asset to be financed as security in the whole picture and to help tackle with financial business planning in Thailand.

I. Security Interests over Real Property

Immovables or real property¹, such as land and building, under Thai law are applicable for security by means of mortgage, which is a common way of financing in Thailand. Introducing the concept of mortgage under Thai law, the provision of mortgage not only cover the extent of real property but also some registered movables; including, ships of

¹ Immovable property denotes land and things fixed permanently to land or forming a body therewith. It includes real rights connected with the land or things fixed to or forming a body with land (See Civil and Commercial Code of Thailand, Section 139).

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five tons and over, floating houses, beast of burden, and other movables which the law may provide registration for that objective, of which would be further explained in *Part II - Security Interests over Movable Asset*.

What is the basic nature of mortgage in Thailand? Under the Civil and Commercial Code of Thailand (“CCC”), the mortgage is a contract that a mortgagor shall *assign* a property to a mortgagee as security, *without delivering* the property to the mortgagee². The mortgage will be legitimate only upon the contract being made in writing and registered with the competent authority i.e. Department of Land for the case of real property³. To further extract the basic nature of mortgage, these following details in the table may serve the purpose:

◆	Mortgaged property must be mortgaged by the owner during such time being only⁴. However, please also note that the owner of such property is eligible to do the mortgage ⁵ <i>within the right and condition they are binding (if any)</i> ; that is to say, the owner whose right of ownership over a property is subject to a condition may mortgage such property only subject to such condition ⁶ .
◆	The mortgagee has the right of debt payment over the mortgaged property in preferential to ordinary creditors without the need to deliver such property to the mortgagee and regardless of the fact whether the ownership of property has been transferred to the third person or not⁷. On the other hand, if the property is not assigned but the mortgagor only delivers the title document of the property to the mortgagee, the execution as such does not deem as the mortgage. However, per precedent cases, even if it is not the mortgage, the creditor is entitled to confiscate the title documents until the payment is made, according to the agreement ⁸ . However, there is potential risk that the owner of property may declare to the authority that the title document is lost and apply for the new one and transfer the property to the innocent third party. As a result, the creditor may have no choice but may need to take action against the debtor (owner of property) for debt repayment.
◆	The owner of property could mortgage his property for the obligation performance of other persons⁹
◆	Property mortgaged to one person may be mortgaged to another during previous contract’s continuance¹⁰.

To what extent that mortgage can be applicable in Thailand? The mortgaged property is a security for the performance obligation, which also includes its accessories as well, i.e., (1) the interest; (2) compensation for non-performance obligation; and (3) mortgage enforcement cost¹¹. Generally, the mortgage would cover to the extent of all things connected with the mortgaged property e.g. the land also covers to the extent of building on such land if it already exists

² CCC, Section 702.

³ CCC, Section 714.

⁴ “During such time being only” means property shall be owned by the person who mortgage at the time of mortgage. For instance, the mortgagee could not claim to use property of which his right of ownership would be effective in the future e.g. the property held under hire-purchase that the ownership on property would not yet transferred until the complete payment is made (See Supreme Court Ruling of Thailand, 503/2504 (1961)).

⁵ *Id.* at Section 705.

⁶ *Id.* at Section 706.

⁷ *Id.*

⁸ Supreme Court Ruling of Thailand No.1369/2510 (1967).

⁹ *Id.* at Section 709.

¹⁰ *Id.* at Section 712.

¹¹ Civil and Commercial Code of Thailand, Section 715.

before or at the time of mortgage contract, regardless of the fact that existing building is erected by mortgagor or other persons (however, it shall be proved that the existing building at the time-being of mortgage is owned by the land owner)¹², except the case as follows:

- *Mortgage over land* would not extend to the buildings erected by the mortgagor *after* the date of the mortgage¹³ (except the mortgage contract has a special clause stipulated otherwise to that effect)¹⁴;
- *Mortgage over buildings* does not extend to the land in case the mortgage of buildings constructed in other persons' ownership of land, not the mortgagor himself¹⁵; and
- *Mortgage does not extend to the fruits of the mortgaged property*, except after the mortgagee has notified the mortgagor or the transferee of his intention to enforce the mortgage¹⁶.

¹² For further clarification on the building erected *before or at the time of mortgage contract*, according to Section 144 of the CCC, it states that "A component part of a thing is that which, according to its nature or local custom, is essential to its existence and cannot be separated without destroying, damaging or altering its form or nature. The owner of a thing has ownership in all its component parts." As such, any building erected on the land shall be component parts of the land, that is to say, the owner of land is the owner of building under Section 144. However, in practice, the Land Department usually rejects to approve the mortgage registration of land to be extended to the building erected on such land if the land owner could not provide the evidence proof of building ownership, i.e., the acquisition of building document or any evidence proving that the building is also of the land's owner, under the ground of juristic act. Since the ownership of land can be owned by either juristic act (which the Land Official always requests the evidence document) or legal ground per the principle of "component part" under Section 144 of the CCC; thus, in the case where the official investigates and sees that there is no juristic act but there is legal ground, i.e., *the fact shown undoubtedly reason proven that the building is owned by the land owner, not any third parties at the time-being of land ownership transfer*, according to Section 144 instead which does not require any evidence in paper, the land official shall not be able to reject such registration upon the building that attached to the land upon the ownership transfer. In this case, the land official would endorse in the registration in the wording i.e. "the ownership upon the building is by way of component part's principle, not by way of juristic act under the registration with the land official" which is the guideline of the Land Department (See Notification of the Land Department No. MorTor 0515/Wor 1893 dated 20 January 2557 (2014) and No. MorTor 0515.1/Wor 22737 dated 15 August 2554 (2011)). According to aforementioned guidance and principle, for mortgage registration, in practice, the mortgage contract would *specify* that the mortgage would be for land or land together with building for the sake of appraisal of value of mortgage in commercial practice. Further, if the building is also included in the mortgage, the mortgage contract would usually attach the evidence showing the detail of building in the contract also as its appendix for contract party in terms of mortgage value. In absence of the clear stipulation that the mortgage would also cover the building as well as the evidence that the building is owned by the land owner and the building detail, the mortgagee, especially bank or any financial institution, would not accept that the building would be also mortgaged. Therefore, that leads to the next step for the mortgage registration with the Land Department that, in practice, the mortgage registration of land to be extended to the building, upon the absence of mortgage contract to specifically stipulate that the mortgage of land also includes the building as well as the absence of the attachment to the contract of building detail for the sake of its value, the mortgage registration of land would only effective upon the land and not extend to the building.

¹³ In such case, upon the mortgage enforcement, the mortgagee can have such buildings sold with the land under the scope of his preferential right against the price obtained for the land only (CCC, Section 719).

¹⁴ *Id.* at Section 719.

¹⁵ *Id.* at Section 720.

¹⁶ *Id.* at Section 721.

How to ensure that the mortgage contract is valid and enforceable under Thai law?

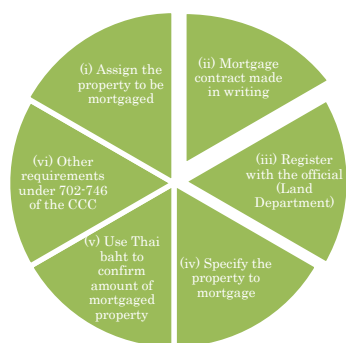


Figure (i): Factor for the Validity of Mortgage Contract

Based on the simple explanation through Figure (i), the reader may follow the check list that firstly, the mortgage contract under Thai law must be made in writing and registered with the official, i.e., Department of Land. Further, it shall also specify the property to be mortgaged specifically, such as the land with detail of its land title deed’s number. Besides, Thai currency shall be used in a contract of mortgage for which the mortgaged property is assigned as security¹⁷. In supplementary for contract drafting upon mortgage in terms of payment, fundamentally, the mortgage could be paid by installments; however, in case that the parties thereto does not wish to do so, they may stipulate in the contract otherwise¹⁸.

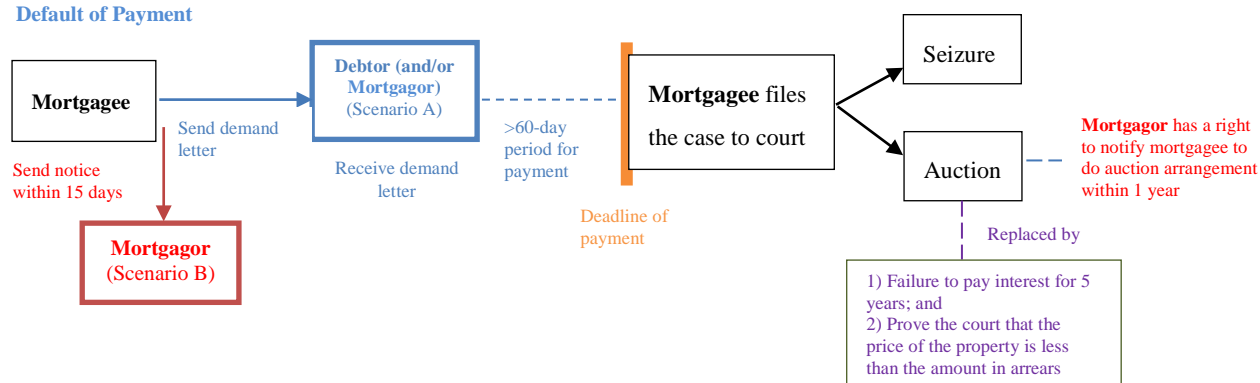
How to execute the enforcement of mortgage if mortgagor is default?

Figure (ii): Mortgage Enforcement Flow Chart

Scenario A: Mortgagor mortgages his own property as security for his own performance obligation

Scenario B: Mortgagor mortgages his own property as security for other person’s performance obligation

Default of Payment



Elaborating Figure (ii), to enforce the mortgage, the mortgagee shall send the notice in writing to the debtor in advance to demand for performance obligation, of which the time period requesting for payment shall be not less than 60 days from the date of receiving the notice by debtor. Failing which, the mortgagee might file the complaint to the competent court asking for judgement order for mortgaged property seizure, or alternatively, public auction¹⁹. In case where mortgagor mortgages his own property as security for other person’s performance obligation, the mortgagee shall additionally deliver the notice (the same content as sending to debtor) to the mortgagor within 15 days from the date of notice delivering to the debtor. Failing which, the mortgagor shall be released from liability upon interest and compensation unpaid by the debtor, including charge accessory to such obligation after the expiry of such 15-day period expires²⁰. In case there is no other mortgages or preferential rights registered on the same mortgaged property, the mortgagee might

¹⁷ Id. at Section 708.

¹⁸ Id. at Section 713.

¹⁹ Id. at Section 728, paragraph 1.

²⁰ Id. at Section 728, paragraph 2.

file a case to competent court for the foreclosure of the mortgaged property in lieu of public auction under the conditions that the debtor's failure to pay interest for 5 years and the mortgagee could satisfy the competent court with the proof that mortgaged property price is less than the amount in arrears²¹. Moreover, in the case where the mortgagee intends to enforce the mortgage against the transferee of a mortgaged property, the mortgagee shall send the writing notice notifying the transferee in advance for not less than 60 days to enforce such mortgage²².

At the end, the mortgage could be extinguished in various scenario, as the case may be, such as the event of extinction of obligation secured, release of mortgage in writing, discharge upon mortgagor, mortgage being removed, auction due to court order, or mortgage foreclosure²³. Anyhow, the enforcement upon mortgage by the mortgagee could still be made even after the secured obligation has been barred by prescription; however, arrears of interest on the mortgage cannot be enforced for more than five years²⁴.

II. Security Interests over Movable Asset

Movable asset could be used as security by way of mortgage, pledge or by the concept under the Business Security Act, B.E. 2558 (2015) ("Business Security Act"), depends on nature of asset to be financed. In Part II, this newsletter would divide the security upon movables into three parts as shown below since the obligation from each security interest is significantly different. This clarification would help the reader visualize more on its differences.

Part 1 – Movables as Security by means of Mortgage

As mentioned in section I above, apart from immovables that are covered by the provision of mortgage as previously explained in *Section I - Security Interests over Real Property*, some of registered movables also can legally be mortgaged under Thai law as well, which includes following properties:

- Ships of five tons and over;
- Floating houses²⁵;
- Beast of burden²⁶²⁷; and
- Other movables which the law may provide registration for that purpose.
 - Machine under registration²⁸;
 - Vehicle such as caravan, road roller, and tractors under registration²⁹; and

²¹ *Id.* at Section 729.

²² *Id.* at Section 735.

²³ *Id.* at Section 744.

²⁴ *Id.* at Section 745.

²⁵ Floating houses are similar in concept and can be defined as houses which are constructed on water in a way that the load of the structure is equal or less than the uplift force of the water. Usually, Thai people in the past lived in floating water since the main public transportation back them is via river transportation.

²⁶ For instance, elephant, horse, cow, buffalo, mule or donkey of which are registered with the authority.

²⁷ Beast of Burden Act, B.E. 2482 (1939).

²⁸ Machine Registration Act B.E. 2514 (1971), Section 5.

²⁹ Vehicle Act, B.E. 2522 (1979), Section 17/1.

- o Vessel of sixty tons gross or over which is self-propelled with or without other powers and whose nature of the use is for marine use³⁰.

The provision of mortgage would apply to abovementioned movables as same as applies to immovables. Further, for aircraft as well as other high-value assets that are not listed above, they are not yet accepted under Thai law under principle of mortgage. As financing property in Thailand by means of mortgage is limited to only some applicable property, financing arrangement shall opt for other alternatives instead, e.g., pledge or business security which would be further visualized in Part 2 and 3 below.

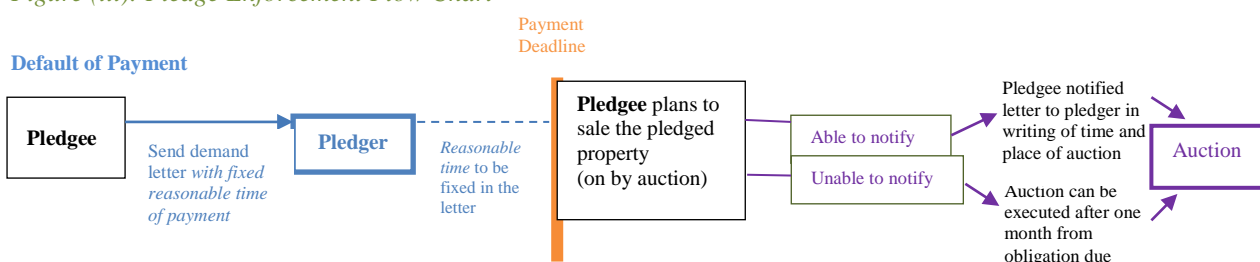
Part 2 – Movables as Security by means of Pledge

Any movable property not falling under the scope of mortgage as mentioned in Part 1 would be able to finance itself as security by means of pledge. Basically, a pledge is a contract whereby the pledger delivers a movable property as a security for performance obligation to the pledgee, unlike mortgage where the mortgaged property is not obliged to do so. However, alternatively, it could be mutually agreed between parties whether they would like to have pledged property be kept by a third person instead³¹. Notwithstanding, for pledge over instrument, share and other rights, would have additional obligations pertaining to the delivery of which pledge over share would be elaborated more in *Part III*, while pledge over rights, would be in our next newsletter.

Pledge is a security for the performance of the obligation and for its accessories; including, (1) interest; (2) compensation for non-performance obligation; (3) pledge enforcement costs; (4) expenses preservation of pledged property; and (5) compensation for injury caused by pledged property’s non-apparent defects³²- compared to mortgage, accessory coverage is more due to difference in delivery obligation. Besides, unless the contract mutually agrees otherwise, if the pledged property produces legal fruits, the pledgee shall allocate such fruits for interest payment that may be due³³. If no interest is due, it shall be appropriate to the principal payment of obligation secured, respectively³⁴.

How to execute the enforcement of pledge if pledger is default?

Figure (iii): Pledge Enforcement Flow Chart



³⁰ Mortgage and Marine Preferential Right B.E. 2537 (1994), Section 7.

³¹ CCC, Section 749.

³² *Id.* at Section 748.

³³ The law does not compel the creditor to use the fruit incurred from pledged property to deduct the outstanding debt, but in the case where the creditor opts to execute as such upon fruits, they shall use the fruit to deduct in the sequence as requested by law (See Supreme Court Ruling No. 1528/2554 (2011)).

³⁴ *Id.* at Section 761.

Elaborating Figure (iii), to enforce pledge, the pledgee shall send the notice in writing to the pledger in advance *with fixed reasonable time* requesting for payment to performance obligation³⁵, default for the payment would enable the pledgee to sale the pledged property by means of auction after sending the notice to pledger in writing of time and place of auction³⁶. Unlike mortgage, to proceed with auction, the pledgee is not required to file the complaint to competent court prior to executing the auction³⁷. In case the notice is impracticable; for instance, the address of pledgor could not be found or the pledgor has changed the address to where the pledgee is incapable of sending the notice to them which causes the obstacle to proceed with auction process as required by law. In this sense, in order to avoid deadlock circumstance upon such impracticality, Thai law imposes the solution that the pledgee may proceed with action after one month from obligation due³⁸. At the end, for pledge extinction, the pledge would trigger to be extinguished upon the extinguishing of obligation or when the pledgee allows returning the pledged property back to the pledger's possession³⁹.

Part 3 – Movables as Security under Business Security Act

At present, there is the new concept of law introducing in Thailand pertaining to the business security under Business Security Act with the propose to widen the scope of asset that has business value but could not be secured by neither mortgage nor pledge. As such, some movables which fall under the eligibility of the Business Security Act would then be able to benefit from this provision. A business security agreement is an agreement that security provider places a property with security receiver as a security to secure a payment or other performance obligation of the security provider himself or others, whereby giving up possession over said property to security receiver *is not* be required. Further, similar to mortgage, the business security agreement shall be made in writing and register with the competent authority i.e. Department of Business Development for its validity. The property for business security, however, only limited to asset including:

- ◆ *Movable property use by security provider in business operation e.g. machinery without registration, inventory or raw materials used in the manufacture of goods*
- ◆ *Immovable property that security provider operates directly in real estate business*

In the case where immovable property is eligible under the Business Security Act, the same property could be used to be financed under mortgage as well. Thus, the benefit to be subject to the business security is that the security provider would, upon the secured property, have the right of disposition, place the secured property under mortgage, and create another security interest over the secured property⁴⁰, which would enable the security provider more to finance upon the asset.

³⁵ *Id.* at Section 764.

³⁶ *Id.*

³⁷ Supreme Court Ruling of Thailand No.875/2523 (1980).

³⁸ *Id.* at Section 765.

³⁹ *Id.* at Section 769.

⁴⁰ The security provider shall have the right to possession, make use of, exchange, disposition, place the secured property under a mortgage, create another security interest over the secured property, use the property in manufacturing process, commingle, using it in the case of occupying for usage thereof, as well as obtaining the fruits of the secured property, except where the contracting parties have agreed otherwise. The security provider may not pledge the secured property under this Act as a security against payment of future debt, otherwise the said pledge shall be invalid. (See Business Security Act, Section 22).

◆ *Perennials*⁴¹.

Further; other assets and intangibles such as *account receivable, business and intellectual property* are also applicable as business security as well; notwithstanding, further detail upon these three assets would be released on the next newsletter in deeper perspective.

Unlike mortgage and pledge, to be eligible for securing property under this provision, the security receiver *must be a financial institution* or others as prescribed in the ministerial regulations, i.e., special purpose vehicle for securitization, trustee, securities company, mutual fund, bond holder representative, juristic person incorporating derivatives' business and factoring business, asset management company and etc⁴². In addition, the security provider might opt to place a property under his possessed right at present or *to be acquired in the future*, as the security for performance obligation; however, the right under business security agreement would exist only when the security provider *duly acquired* the property⁴³.

III. Security Interests over Shares

Under Thai law, share or debenture could be used as security by means of pledge as well. In this implementation, the share certificate would be use as secured property. For shares of limited company, the creation of pledge to be entered into the company's share register book, failing which such pledge could not be set up against the company itself or any third parties⁴⁴. Depending on the requirement of the parties, the pledgee may additionally require the possession of share certificate from the pledgor and stating in the share certificate for the record that "this share certificate is under the pledge" in some practice of some company. However, such possession over the share certificate has no impact on the effectiveness of shares pledge or right of the pledgee. Under the law, it is good to be reiterated that only the creation of pledge in the share register book of the company is required in order for the pledgee to be able to set up against the company and any third parties. For share of public limited company, if it is not listed company, the pledge is also required to be recorded in the company's share register book. For the case of listed company with scripless, shareholder as pledger must contact securities company (broker) to proceed with the pledge registration in the system of the Thailand Securities Depository Co., Ltd.

⁴¹ Perennials is the plant which is considered as having economic value, accepted under Thai law to be used as security for 38 kinds such as *Tecotono grandis* L.f., *Dalbergia cochinchinensis* Pierree, *Dalbergia oliveri* Gamble ex Prain and etc. (See Ministerial Regulation prescribing other asset as a security, B.E. 2561 (2018) and the list attached to Forest Plantation Act, B.E. 2535 (1992)).

⁴² Ministerial Regulation prescribing other persona as security receiver, B.E. 2559 (2016).

⁴³ Business Security Act, Section 9.

⁴⁴ CCC, Section 753.

Summary

In Thailand, in order to use asset as a financing mechanism, there is three ways for using property as security, that is, mortgage, pledge and business security, depends on the category of asset and its condition thereto. As mentioned, mortgage does not only cover to the extent of real property such as *land and building*, but also movable asset in some extent as applicable; including, *ships, floating houses, beast of burden, machinery, vehicle and vessel* as applicable under condition prescribed in the law. As security financing upon mortgage is very limited and not include other high-valued asset in Thai industry, it is inevitable that the business operator shall seek other alternatives of financing instead, e.g., pledge or business security. Pledge is commonly known in the business sector; however, even if the rest of movables does not cover by the provision of mortgage would fall under the pledge instead, such as *any movables, shares, instrument or other rights*, other kinds of high-value asset in the industry is not applicable to be secured under neither mortgage nor pledge. Notwithstanding, there is more room for business operator to tackle with facilitating its financial liquidity by means of business security nowadays. The business operator may opt to secure their *intellectual property* as well as other high-valued assets such as *receivables, business, machinery, inventory or raw materials used in the manufacture of goods used in the industry* in order to facilitate the financial flow in their business sector thereupon.



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