STRIKING THE BALANCE BETWEEN CONTRACTUAL RIGHTS AND OBLIGATIONS: RESTRUCTURED CONTRACT LAW IN THE NEWLY ENACTED CHINESE CIVIL CODE

Mo Zhang[†]

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Abstract

Contract legislation in China experienced a significant change as a result of the Civil Code's enactment in 2020. With a focus on civil rights and private interests, contract law and other areas of law are expected to help promote the development of a rights-based society under the Civil Code—a much wanted shift from the traditionally obligation-based society. In this context, the Civil Code is hailed in China as a milestone in the country's legal landscape.

The Civil Code consolidated the 1999 Contract Law with judicial practices and restructured the legal framework governing contracts by modifying or adding provisions aimed at achieving balanced rights and obligations between the contractual parties. Although the Civil Code demonstrates the progresses made in upholding civil rights and private interests, it remains to be seen how such rights and interests are to be effectively protected, especially when an authoritarian government power is involved. There are many obstacles ahead.

I. INTRODUCTION

On May 28, 2020, China's top legislative body, the National People's Congress ("NPC"), passed the Country's first-ever Civil Code since the Communist Party-led government took power in 1949.[1] The Civil Code, which appears to be quite an ambitious legislative endeavor, consists of 1,260 articles. It is considered a comprehensive codification of all civil affairs in the nation.[2] Effective January 1, 2021, the Civil Code is expected to be a main pillar of legislation governing civil and commercial matters in the Chinese legal system. Given its broad and extensive coverage, the Civil Code is hailed in China as a legal encyclopedia prescribing the Country's social life and civil activities.[3]

Civil law was not rooted in China, though its current legal system is described as one within the civil law family. The traditional Chinese legal system was a criminal law-based system in which punishment was the primary legal means to maintain societal order.[4] There was barely any independent or separate civil legislation until China was forced to open up to the outside world in the mid-1800s.[5] In 1907, as part of the Nation's legal reform, the imperial government initiated an effort to draft new laws while also revising the existing ordinances.[6] A major piece of the legal drafting was a civil code. The first draft was

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† Professor of Law, Temple University Beasley School of Law.

1 The Civil Code of the People's Republic of China was adopted by the National People's Congress ("NPC") on May 28, 2020. It contains seven parts plus supplementary provisions, covering General Provisions, Property, Contract, Personality, Marriage and Family, Succession, and Torts. Minfadian (民法典) [Civil Code] (promulgated by the Nat'l People's Cong., May 28, 2020, effective Jan. 1, 2021) (China), http://www.npc.gov.cn/npc/c30834/202006/75ba6483b8344591abd07917e1d25cc8.shtml, *translated in* http://www.npc.gov.cn/englishnpc/c23934/202012/f627aa3a4651475db936899d69419d1e/files/47c16489e186437eab3244495cb47d66.pdf [hereinafter 2020 Civil Code].

2 *See* Wang Chen, *Explanations to the Draft Civil Code* (May 22, 2020), http://www.npc.gov.cn/npc/c30834/202005/50c0b507ad32464aba87c2ea65bea00d.shtml.

3 *See* Wang Liming, *The Significance of the Civil Code*, PEOPLE'S PROCURATION DAILY (Aug. 17, 2020), http://www.china.com.cn/opinion2020/2020-08/17/content_76607955.shtml.

4 *See* ZHANG JIFAN, EVOLUTION OF CHINESE LEGAL CIVILIZATION 23 (1999).

5 *See* XIN CHUNYING, CHINESE LEGAL SYSTEM AND CURRENT LEGAL REFORM 5 (1999).

6 *See id.* at 6–8.

completed in December 1910 and finalized in 1911.[7] The draft, however, never became law due to the fall of the Qing dynasty that year.[8]

An important feature of the first draft civil code was the civil law influence. Based primarily on the German model, the draft consisted of five parts and thirty-six chapters with a total of 1,569 articles.[9] The five parts included general principles, rights of *obligatio*, property rights, domestic relations, and inheritance.[10] Despite its failure, the first draft of the Civil Code provided a useful blueprint for China's later civil law legislation.[11] An example was the concept of "*obligatio*," a term used in civil law to refer to the civil rights and obligations that are created either by agreement or by operation of law.[12] Ever since it was provided in the first civil code draft, the law of *obligatio* has become an important component of the Country's civil law legislation.[13]

The first Civil Code in China was enacted in 1930 by the Nationalist Government. Known as the 1930 Civil Code of the Republic of China, it contained 1,225 articles in five books, including: General Principles, *Obligatio*, Rights Over Things, Family, and Succession.[14] Prior to the adoption of the 1930 Civil Code, there was also an attempt to pass a civil code in the 1920s.[15] A draft was completed in 1925, but was eventually aborted due to the political chaos in the Country under the warlord governments.[16]

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7 *See* WANG JIAFU, CIVIL LAW OBLIGATIO 16 (1991); *see also* YUKON CHANG, CIVIL CODE OF THE REPUBLIC OF CHINA (STUDIES IN CHINESE GOVERNMENT AND LAW) x-xi (Joseph En-pao Wang ed., Ching-Lin Hsia & James L. E. Chow, trans., 1930).

8 *See* CUI JIANYUAN ET AL., GENERAL THEORY OF CIVIL LAW 9 (3d ed. 2019).

9 *See* CHANG, *supra* note 7, at xi.

10 *See id.*

11 *See* JIANYUAN ET AL., *supra* note 8, at 9.

12 *See* David Ibbetson, *Obligatio in Roman Law and Society*, *in* THE OXFORD HANDBOOK OF ROMAN LAW AND SOCIETY 43.3 (Paul J. du Plessis, Clifford Ando, & Kaius Tuori eds., 2016); *see also* George Long, *Obligationes*, U. CHICAGO (Jan. 2020), https://penelope.uchicago.edu/Thayer/E/Roman/Texts/secondary/SMIGRA*/Obligationes.html.

13 *See* CUI JIANYUAN, GENERAL PROVISIONS OF OBLIGATIONS 2–3 (2013).

14 *See* LAWS & REGULATIONS DATABASE OF THE REPUBLIC OF CHINA, LEGISLATIVE HISTORY OF THE CIVIL CODE OF 1929, https://law.moj.gov.tw/ENG/LawClass/LawHistory.aspx?pcode=B0000001.

15 *See* JIANYUAN ET AL., *supra* note 8, at 9.

16 *See id.*; *see also* CHANG, *supra* note 7, at 19.

Note, however, each book in the 1930 Civil Code had a different enactment date because the five books were promulgated separately at different times. Book I was promulgated on May 23, 1929, effective the same year.[17] Books II and III were adopted on November 22, 1929 and November 30, 1929, respectively, and both became effective on May 5, 1930.[18] The last two Books were enacted on December 26, 1930 and became effective May 5, 1931.[19] The 1930 Civil Code remains effective (as amended) in Taiwan, but it was abolished in Mainland China when the People's Republic of China was founded in 1949.

The adoption of a new civil code in China experienced a decades-long battle, although the need for it arose right after the annulment of the 1930 Civil Code. From 1949 to 1979, there were two failed attempts to adopt a civil code.[20] The first drafting work officially began in 1954 and was completed in 1956, with a draft containing 525 articles that covered three general provisions: ownership, *obligatio*, and inheritance.[21] The 1956 draft essentially followed the 1922 Soviet Civil Code.[22] Unfortunately, the anti-rightist movement against intellectuals that began in 1957 led to a complete halt of all legislation in China.[23]

The drafting work resumed in 1962 and produced a second draft of the Civil Code in 1964.[24] Compared to the first draft, the second draft was much shorter and had only three parts: general provisions, ownership, and property transfer, with 262 articles in total. In contrast to the first draft of the Civil Code, a notable distinction of the second

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17 LAWS & REGULATIONS DATABASE OF THE REPUBLIC OF CHINA, *supra* note 14.

18 *Id.*

19 *Id. See* FOO PING SHEUNG, INTRODUCTION TO THE CIVIL CODE OF THE REPUBLIC OF CHINA xiv–xv (Ching-Lin Hsia, James L. E. Chow & Yukon Chang trans., 1930), https://archive.org/details/civilcodeofrepub00chin/page/n9/mode/2up.

20 *See* JIANYUAN ET AL., *supra* note 8, at 10.

21 *See* Wan Yi, *The History and Recent Development of Civil Legislation in China*, NPC NET (Sept. 18, 2012), http://www.npc.gov.cn/npc/c222/201209/aec24a7d5c0e477c8c1b056e59bb4e41.shtml.

22 *See id.*

23 *See* Huang Lansong, *The Brief History of the Compilation of the New China Civil Code*, CHINA SOC. SCI. NEWS (Nov. 23, 2016, 4:41 PM.), http://www.cssn.cn/sf/bwsf_fx/201611/t20161123_3287568.shtml; s*ee also The Historical Evolution of the Civil Code of New China*, PEOPLE'S DAILY (Oct. 26, 2016), http://www.npc.gov.cn/zgrdw/npc/lfzt/rlyw/2016-10/26/content_1999692.htm.

24 *See* Yi, *supra* note 21.

draft was that it was structured to serve two purposes: to depart from the former Soviet model and to distance China from the influence of capitalist countries.[25] As a result, the second draft appeared to be neither fish nor fowl despite its imbedded civil law characteristics.[26]

But the fate of the second draft of the Civil Code was no better than that of the first one. In 1966, the notorious Cultural Revolution broke up and sent the Country into a decade-long chaos.[27] Therefore, the second draft of the Civil Code was never placed on the Nation's legislative agenda.[28] It was the economic reform that prompted the third attempt to draft the Civil Code. As early as August of 1979, the Standing Committee of the NPC began to form a group for the civil code drafting.[29] An initial draft was completed in May of 1982, and it contained 8 parts, 43 chapters, and 465 articles.[30]

Due to the lack of consensus on various issues arising from the economic reform, however, the focus of the drafting work was soon shifted from adoption of a comprehensive civil code to the enactment of individual law.[31] The underlying idea was that those individually enacted laws would be consolidated to form a single code at a time that is deemed ripe. Since then, a series of laws in the civil area were enacted, including, among others, the 1986 General Principles of Civil Law,[32] 1999 Contract Law,[33] 2007 Property Law,[34] 2009 Tort

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25 *See* Lansong, *supra* note 23.

26 *See* Liming, *supra* note 3.

27 For a Western view of the Cultural Revolution, see Austin Ramzy, *China's Cultural Revolution, Explained*, N.Y. TIMES (May 14, 2016), https://www.nytimes.com/2016/05/15/world/asia/china-cultural-revolution-explainer.html.

28 *See* Yi, *supra* note 21.

29 *See id.*

30 *See* Liming, *supra* note 3.

31 *See* Yi, *supra* note 21.

32 The General Principles of Civil Law were adopted by the NPC on April 12, 1986, and took effect January 1, 1987. For an English translation, see Whitmore Gray & Henry Ruiheng Zheng, *General Principles of Civil Law of the People's Republic of China*, 34 AM. J. COMP. L. 715–43 (1986).

33 The 1999 Contract Law was promulgated by the NPC on March 15, 1999, effective on October 1, 1999. Hetong Fa (合同法) [Contract Law] (promulgated by the Nat'l People's Cong., Mar. 15, 1999, effective Oct. 1, 1999) (China), http://www.gov.cn/banshi/2005-07/11/content_13695.htm [hereinafter 1999 Contract Law].

34 The Property Law was adopted by the NPC on March 16, 2007 and went to effect on October 1, 2007. Property Law (promulgated by Nat'l People's Cong., Mar. 16, 2007, effective Oct. 1, 2007), P.R.C. LAWS 62 (China) http://www.npc.gov.cn/zgrdw/englishnpc/Law/2009-02/20/content_1471118.htm [hereinafter 2007 Property Law].

Liabilities Law,[35] and the 2017 General Provision of Civil Law.[36] Those laws paved the way for the final adoption of the Civil Code in 2020, the most extensive single legislation in China's recent history.

The Civil Code is not a simple consolidation of the existing civil law legislations,[37] but rather it significantly modifies and changes those legislations. A striking example is the inclusion of the rights of the personality as an independent part (Book IV) of the Code.[38] The modification and changes reflect the latest development of legislative preference in conjunction with the views of the courts in their practices. Broadly, the comprehensiveness of the Civil Code demonstrates China's endeavors in the past decades to rebuild its legal system.

The new Civil Code made a great deal of changes to Chinese contract law. The changes involve both structure and substance of the contract legislation. Compared with the Contract Law, the Civil Code drops 37 articles, adds 136 new articles, and modifies 153 articles. Although contract law is just one of the seven parts in the Civil Code, it contains 525 articles, nearly half of the 1260 articles of the Civil Code. A heavy focus on contract law in the Civil Code implicates its importance and also demonstrates the significant role of contracts in China's modern economy—defined as the "socialist market economy."[39]

The changes made to the contract law in the Civil Code include: the rules of performance of contract under the concept of "*obligatio*,"

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35 The Tort Liability Law was promulgated by the Standing Committee of the NPC on December 26, 2009, and took effect July 1, 2010. Tort Liability Law (promulgated by Nat'l People's Cong., Dec. 26, 2009, effective July 1, 2010), P.R.C. LAWS 21 (China), http://www.npc.gov.cn/zgrdw/englishnpc/Law/2011-02/16/content_1620761.htm [hereinafter 2009 Tort Liability Law].

36 The General Provisions of Civil Law was adopted by the NPC on March 15, 2017, effective October 1, 2017. Minfa Zongze (民法总则) [General Provisions of the Civil Law] (promulgated by the Nat'l People's Cong., Mar. 15, 2017, effective Oct. 1, 2017) (China), http://www.npc.gov.cn/zgrdw/npc/xinwen/2017-03/15/content_2018907.htm [hereinafter 2017 GPCL].

37 Under Article 1260 of the 2020 Civil Code, at the time when the civil code takes effect on January 1, 2021, the following laws are repealed: the Marriage Law, the Succession Law, the General Principle of Civil Law, the Adoption Law, the Guarantee Law, the Contract Law, the Property Law, the Tort Liabilities Law and the General Provisions of Civil Law. *See* 2020 Civil Code, *supra* note 1.

38 Part IV of the 2020 Civil Code is entitled: Right of Personality. *See* 2020 Civil Code, *supra* note 1.

39 For a general discussion of the socialist market economy, see Siegfried Karsten, *China's Approach to Socialist Market Economy: The Chinese Variant of Market Socialism Seeks to Escape from the Difficulties of Central Command Planning*, 47 AM. J. ECON. & SOCIO. 129 (1988).

the provision of quasi-contract, obligations of the parties in preparing to make a contract, formation of contract via actual performance, effect of non-effective contract, third party interest, green performance requirements, and electronic contracts.[40] In addition, the Civil Code expands the specific contracts from fifteen types in the Contract Law to nineteen types.[41]

There are two other changes to Chinese contract law that are considered significant. The first is the formal adoption of the *Rebus Sic Stantibus* approach (changes in circumstances) in respect to the contract performance.[42] For many years, even before the Contract Law was adopted, there had been a widespread call in China to allow a contracting party to be excused from performing the contract if the circumstances surrounding its execution had changed so dramatically that injustice would occur if performance continues.[43] Not until the adoption of the Civil Code did this approach become a statutory ground for discharging the duty of performance without incurring liability for breach of contract.[44]

The other change is the rule of compulsory contracting under the state purchase order or mandatory task.[45] Both the state purchase order and the mandatory task were provided in the Contract Law as devices to implement state plans through the means of contract.[46] The Civil

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40 *See* 2020 Civil Code, *supra* note 1.

41 The new types of specific contracts added in the 2020 Civil Code are guarantee contract, partnership contract, factoring contract, and property management contract. 2020 Civil Code, *supra* note 1, III(2), ch. XIII, XVI, XXIV, XXVII.

42 *Id.* art. 533.

43 *See* HAN SHIYUAN, THE LAW OF CONTRACT 382–83 (3d ed. 2011).

44 According to Professor Wang Liming of Renmin University, a key drafter of the 2020 Civil Code, there were as many as 10 major aspects in which the 2020 Civil Code differs from the 1999 Contract Law. The 10 issues include: (a) relationship between contract law and the law of *obligatio*, (b) the rules of contract formation, (c) a promise made during the contract negotiation (whether it may be deemed as a contractual clause), (d) effect of contract, (e) performance of contract, (f) preservation of contract, (g) modification and assignment of contract, (h) unrest defense and anticipatory repudiation, (i) dissolution of contract, and liabilities for breach of contract. *See* Wang Liming, *An Analysis of Ten Major Issues in the Drafting of the Civil Code*, 1 YUNNAN SOC. SCI. 77 (2020).

45 The state purchase order and mandatory task are the order or task assigned by the state to particular entity or entities for the need of the state. Both the order and task are compulsory in nature.

46 Under Article 38 of the 1999 Contract Law, if the State, according to the needs, gives mandatory orders or State purchase orders, the legal persons and other organizations concerned shall conclude contracts in accordance with the rights and obligations provided for by the relevant laws and administrative regulations. *See* 1999 Contract Law, *supra* note 33.

Code makes it an obligation for the parties to enter into a contract necessitated by the state purchase order, the mandatory task, or under the operation of law.[47] In addition, the Civil Code defines the grounds for issuing the state purchase order or mandatory task to include rescue and disaster relief, epidemic prevention and control, and other needs.[48] Moreover, in contrast to the Contract Law, the Civil Code expands those who are subject to a state purchase order or mandatory task to range from "relevant legal person or other organization" to all "relevant civil subjects," including individuals.[49]

A change in the scope of contract law is also seen here. Under Article 2 of the Contract Law, a contract is defined as an agreement made by and between natural persons, legal persons, or other organizations with equal status to establish, modify, and terminate the civil right and obligation relationship.[50] An agreement that involves a personal status relationship such as marriage, adoption, and guardianship, however, is not covered by the Contract Law.[51] The Civil Code replaces the phrase "between natural persons, legal persons, or other organizations with equal status" with a simple term: "civil subjects."[52] More notably, it makes the contract law provisions applicable referentially to the relationship of personal status.[53]

With all the changes, the Civil Code integrates the existing contract legislation, judicial practice, and new development into a refined legal framework that governs contracts in the Country. This article intends to take a closer look at the Civil Code on contracts and to analyze the changes made to the Contract Law. The analysis purports to take a deep dive into the relevant issues, with a focus on the rules, underlying doctrines, and possible impacts. This article suggests that enactment of the Civil Code demonstrated China's development in upholding civil rights and private interests, but it

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47 *See* 2020 Civil Code, *supra* note 1, art. 494.

48 *See id.* art. 494.

49 *See id.*

50 1999 Contract Law, *supra* note 33, art. 2.

51 *Id.*

52 2020 Civil Code, *supra* note 1, art. 464.

53 According to Article 464 of the 2020 Civil Code, contract is an agreement entered into by and between civil subjects to establish, modify and terminate civil legal relationship. The agreement involving personal status relationship such as marriage, adoption or succession is governed by the law regulating thus status. The contract provisions in the Civil Code may apply to this agreement by way of reference absent relevant provisions in the personal status laws. *See* 2020 Civil Code, *supra* note 1, art. 264.

remains questionable how such rights and interests are effectively protected, especially when government power is involved.[54]

Part I of this article begins with the civil law concept of *obligatio* and discusses how contracts interplay with *obligatio* under the Civil Code. The discussion concentrates on the determination of *obligatio* in the newly provided quasi-contract, non-contractual obligations, and preliminary contract (i.e., agreement to enter into a contract or agreement to agree). Part II examines freedom of principle as applied in the Civil Code under the rule of priority of agreement. It analyzes the expansion of freedom of contract as desired and the limitations newly imposed. Part III looks into the contracting process and provides an analytical review of the issues involving formation, effect, and performance of contract, as well as third party rights and obligations as provided in the Civil Code.

Part IV of this article turns on the relationship between contractual obligation and creditor's rights. It analyzes the new rules affecting contract modification and assignment. The focal point of discussion is on the protection of creditor's rights and measures to preserve contract in terms of validity and enforcement. Part V examines the rules of interest balance between the parties in connection with liability imposition, including rescission, breach of contract, and remedies. Part VI explores remaining issues that require further clarification or judicial interpretation so as to avoid confusion and to help achieve the goal of the law of contract under the Civil Code. It argues that the unleashed government power would pose great challenges to the effective protection of private rights and interests.

The article concludes that the contract legislation in China bears strong marks of Chinese legal culture and reflects both social and political realities of the Country. Although the restructured legal regime of contracts under the Civil Code lays the ground for an improved contract system, the Country remains struggling with a much-wanted shift from an obligation-based society to a rights-based one. In addition, in order to have the Civil Code implemented as intended and expected, the further effort from NPC and Supreme

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54 Ever since the economic reform was initiated in late 1970s, there have been debates in China pertaining to the rule of law. Many in China believe that a fundamental goal of the rule of law is to provide maximum safeguard of the private right by restricting the government power, and that such fundamental goal should form the core value of the civil code. During the drafting of the 2020 Civil Code, efforts have been made by a vast number of scholars to structure the Civil Code as much "civil" as possible so as to make it center on civil rights. *See* Liming, *supra* note 3.

People's Court ("SPC") would be needed in terms of interpretation of law and interpretation of application of law.

II. *OBLIGATIO* AND CONTRACT

A major difference between the Civil Code and the Contract Law is that the Civil Code incorporates the concept of *obligatio* into contract and equips the law of contract with the function of *obligatio* so as to establish primary rules that govern the legal relationship arising from *obligatio*. The rules so provided not only govern contractual relationships but also apply through reference clause to non-contractual relationships.[55] The idea is to maintain the entirety of *obligatio* while making the law of contract the center of *obligatio*.[56] Note that unlike civil legislation in other countries,[57] the Civil Code is not structured so as to place both contractual and non-contractual obligations under the umbrella of *obligatio*.

Obligatio as a legal concept was first introduced to China in the late 19th century.[58] As noted, it formed part of the 1907 Qing draft civil code.[59] Since then, *obligatio* has been widely accepted in China and has become an important system regulating civil rights and obligations in the Country.[60] *Obligatio* also serves as the legal basis that separates creditor's rights from property rights, and determines the cause of action as to whether a particular claim is a matter of obligation or an issue of the right to thing.[61]

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55 For example, the *obligatio* as provided in the Civil Code applies to both contract and torts.

56 *Id.*

57 In Germany, for example, both contracts (except for capacity to contract, intent and formation) and torts (including other non-contractual obligations) are provided under the law of obligations of the civil code. *See* Bürgerliches Gesetzbuch [BGB] [Civil Code], as amended 2002, Book II: Law of Obligations (Ger.), https://www.gesetze-im-internet.de/englisch_bgb/. In the French Civil Code, *obligatio* includes contract or conventional obligations and undertakings formed without agreement, which are provided under the title of the various ways to acquire ownership. *See* Code civil [C. civ.] [Civil code], art. 1101-1369-11, 1371-1370 (Fr.), http://www.fd.ulisboa.pt/wp-content/uploads/2014/12/Codigo-Civil-Frances-French-Civil-Code-english-version.pdf.

58 *See* HAN SHIYUAN, *supra* note 43, at 26.

59 *See* CHANG, *supra* note 7, at 19.

60 *See* JIAFU, *supra* note 7, at 16–18.

61 *See* JIANYUAN, *supra* note 13, at 1.

A. Concept of Obligatio and Contractual Obligations

In the civil law system, the term "*obligatio*" (*obligationes*) is commonly used to refer to both rights and obligations in civil aspects.[62] A Roman law concept alien to many common law lawyers, "*obligatio*" in the Institutes of Justinian, the sixth-century codification of Roman law ordered by the Byzantine emperor Justinian I, was characterized as "a bond of law by which we are under a necessity of releasing (*solvendae*) something according to the laws of our state."[63] Roman jurist Gaius divided "*obligationes"* into three major categories as to their origin, including obligations *ex contractu* (obligations arising out of contracts), *ex delicto* (obligations incurred in torts), and *ex variis causarum figuris* (obligations by other causes or an unclassifiable miscellaneous group).[64] The *ex variis causarum figuris* was understood to contain *obligationes quasi ex contractu* (quasi-contractual obligations) and *quasi ex delicto* (quasi-delictual obligations)."[65]

Today, in the countries with a civil law tradition, the civil obligations are generally classified into contractual obligations and non-contractual obligations.[66] The former deals with consensual obligations while the latter covers non-consensual obligations.[67] Conceptually, non-contractual obligations are further classified into obligations that arise out of tort and non-tort obligations.[68] Non-tort obligations refer to, particularly, unjust enrichment and *negotiorum gestio* (agency without due authority).[69] In addition, there also developed a doctrine of *culpa in contrahendo* (faulty in contract negotiating) to impose a liability arising out of contract negotiations.[70]

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62 *See* Ibbetson, *supra* note 12.

63 *See* THOMAS COLLETT SANDERS, THE INSTITUTES OF JUSTINIAN 319 (7th ed. 1917); *see also* WILLIAM SMITH, A DICTIONARY OF GREEK AND ROMAN ANTIQUITIES 817–21 (1875).

64 *See* SMITH, *supra* note 63, at 818; *see also* Max Radin, *The Roman Law of Quasi-Contract*, 23 VA. L. REV. 241, 242 (1937).

65 *See* SMITH, *supra* note 63, at 818.

66 *See generally* REINHARD ZIMMERMANN, THE LAW OF OBLIGATIONS: ROMAN FOUNDATIONS OF THE CIVILIAN TRADITION (1996).

67 *See id.* at 1–3.

68 For example, under Article 2 of the 2007 EU Regulation on the Law Applicable to Non-Contractual Obligations (known as Rome II), non-contractual obligations cover damages "arising out of tort/delict, unjust enrichment, *negotiorum gestio* or *culpa in contrahendo*." *See* Commission Regulation 864/2007, O.J. (L 119) (EC), https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=celex%3A32007R0864.

69 *See id.*

70 *See id.*

In China, the 1986 General Principles of Civil Law defined *obligatio* as "a relationship of specific rights and duties between parties, arising either from terms of a contract or by the operation of law."[71] Under that definition, the party who enjoys a right is the obligee while the party who bears the duty is the obligor.[72] In the relationship arising out of *obligatio*, the obligee has the right to demand that the obligor perform his duty according to the terms of the contract or the provision of law.[73] Thus, the *obligatio,* as defined in the 1986 General Principles of Civil law, includes both creditor's rights and debtor's obligations.[74]

According to Chinese scholars, in contrast to the property right, which is the right against anyone, the *obligato* mainly refers to the relationship between the specific parties; the term "specific" is used to describe the *obligatio* relationship that focuses primarily on the debtor or obligor.[75] In other words, in order to realize the creditor's right, the debtor must be specific. The underlying theory is that the *obligatio* creates a right to make a claim against a specific person. Therefore, the satisfaction of a creditor's right depends on fulfillment of the obligation that requires the obligor's action.[76]

The Civil Code contains no definition of *obligatio* but it structures the law of both contractual and non-contractual obligations under the concept of *obligatio.*[77] Under Article 118 of the Civil Code, a civil subject (i.e., person conducting civil activities) shall enjoy creditors' rights in accordance with law.[78] It is further provided in Article 118 that a creditor's right is the right of an obligee to request a specific obligor to or not to engage in certain performance, as arising from a contract, a tortious act, *negotiorum gestio*, unjust enrichment, or other provision of the law.[79]

Article 118 of the Civil Code is actually a replica of Article 118 of the 2017 General Provisions of Civil Law ("GPCL"), where the

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71 *See* Gray & Zheng, *supra* note 32, art. 84.

72 *Id.*

73 *Id.*

74 *Id.*

75 *See* JIANYUAN, *supra* note 13, at 1–4.

76 *See id.* at 3.

77 During the process of drafting the 2020 Civil Code, there were heated debates on whether the law of *obligatio* should be singled out to become a separate part of the code. In the early drafts of the code, there was a part called general provisions of *obligatio.* Due to resistance from some key legislators, however, that part of the code was deleted and incorporated into the provisions of contract instead.

78 2020 Civil Code, *supra* note 1, art. 118.

79 *Id.*

obligatio was provided primarily from the perspective of the creditor's right for the first time.[80] Also, similar to the 1986 General Principles of Civil Law, the Civil Code makes the agreement and the operation of law two legal sources of *obligatio*.[81] One refers to contracts while the other includes torts, unjust enrichment, and *negotiorum gestio*. Note, however, that under the Civil Code, both unjust enrichment and *negotiorum gestio* are provided under quasi-contracts, which are covered by the law of contracts.[82]

What is unclear, however, is whether under Article 118 of the Civil Code, an *obligatio* may arise from a unilateral civil act. In China, the unilateral civil act is an act that would take effect upon the expression of intent of only one party.[83] The common examples are reward and donation because both are considered as the civil act of one party that creates certain rights and obligations between the party taking that act and the other party involved.[84] The relationship so created results in an *obligatio*.

B. Obligatio and Allocation of Contractual Liabilities

Again, *obligatio* is a legal relationship where one party has the right to make a claim against the other for payment or fulfilment of

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80 *See* 2017 GPCL, *supra* note 36, art. 118.

81 *See* Gray & Zheng, *supra* note 32, art. 84; *see also* 2020 Civil Code, *supra* note 1, art. 118.

82 *See* 2020 Civil Code, *supra* note 1, art. 979–88.

83 The concepts of unilateral and bilateral contracts are understood differently in China than they are in common law countries such as the United States. In China the difference between a bilateral contract and a unilateral contract lies in whether there are mutual obligations between the parties. If the contractual parties owe each other an obligation to perform, such an agreement constitutes a bilateral contract. If, on the other hand, only one party to the contract has a duty to perform for the benefit of the other party, such an agreement constitutes a unilateral contract. A contract to make a gift or a donation is a unilateral contract. Because of the mutuality of obligations it creates, bilateral contracts are often referred to by Chinese scholars as "reciprocal contracts."

84 In its 2009 Interpretation of the Application of the Contract Law, the SPC explicitly recognized the legal effect of rewards made to the public, although a reward is categorized as a unilateral act. According to the SPC, when the offeror of a reward publicly announces an offer to pay to a person who has performed certain acts, and then that person requests the payment, the court shall grant the request, unless fraud, coercion, or other illegality is involved. *See* Zhang Zhiqiang, *Interpretation of the Supreme People's Court on Several Issues Concerning the Application of the Contract Law of the People's Republic of China* art. 3, FINDLAW, https://china.findlaw.cn/hetongfa/hetongfagui/hetongfa/htfsfjs/5713.html (last visited Sept. 16, 2021).

other obligations.[85] Thus, as far as the parties are concerned, *obligatio* creates the right of claim between them. In contracts, the mutual agreement of the parties determines the nature and contents of the *obligatio*, and the substance of the right of claim.[86] More importantly, because it is based on agreement, the *obligatio* arising from a contract is mostly subject only to non-mandatory rules.[87]

On that ground, the Civil Code defines contract as an agreement by and between civil subjects to create, modify, and terminate civil legal relations.[88] It is also provided that a contract, once legally formed, is protected by law, and is binding only to the parties involved unless otherwise provided by law.[89] Similar to the 1999 Contract Law, the Civil Code required that the parties perform their obligation thoroughly according to the terms of their agreement and abide by the principle of good faith.[90]

But, unlike the Contract Law, the law of contract under the Civil Code is intended not only to establish a legal framework governing the *obligatio* based on agreements, but also serves the basic function of the general law of *obligatio*. As noted, the early legislation on *obligatio* was the 1986 General Principles of Civil Law. In addition to the definition of *obligatio*, the 1986 General Principle of Civil Law divides *obligatio* into joint *obligatio* and joint and several *obligatio*.[91] The Civil Code expands *obligatio* to include selective *obligatio*, joint *obligatio*, and in the meantime provides the rules on how the contractual rights or obligations are allocated when two or more obligees (i.e, creditors) or obligors (i.e., debtors) are involved.

The selective *obligatio* refers to the *obligatio* in which there are two or more subject matters of obligation, and the obligor may choose

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85 *See* TONG ROU & WANG LIMING, CIVIL LAW OF CHINA 299 (1990).

86 *See* WANG HONGLIANG, THE GENERAL THEORY OF OBLIGATION LAW 42–46 (2016).

87 *See* JIANYUAN, *supra* note 13, at 42.

88 *See* 2020 Civil Code, *supra* note 1, art. 464.

89 *See id.* art. 465.

90 *See id.* art. 509.

91 Under Article 86 of the 1986 General Principles of Civil law, when there are two or more creditors, each creditor shall be entitled to rights in proportion to his proper share of the credit; if there are two or more debtors, each debtor shall assume obligations in proportion to his proper share of the debt. Pursuant to Article 87, when there are two or more creditors or debtors, each of the joint and several creditors shall be entitled to demand that the debtor fulfil his obligations under the provision of law or the agreement between the parties; each of the joint debtors shall be obliged to perform the entire debt, and the debtor who performs the entire debt shall be entitled to ask the other joint debtors to reimburse him for their shares of the debt. *See* Gray & Zheng, *supra* note 32.

to perform any of them to satisfy the creditor's rights.[92] In certain cases, the choice is in the hands of the creditor. For example, under Article 582 of the Civil Code, if performance does not conform to the terms of contract, the obligee may reasonably request the obligor to bear such obligation as repair, re-work, replace, return, or reduction of price or remuneration.[93] Thus, as long as the obligor performs any of the listed obligations, the creditor's right to the obligee is and should be satisfied.

The Civil Code contains two articles that governs selective *obligatio*. The first provision concerns the right to choose.[94] In accordance with Article 515 of the Civil Code, when an obligation has multiple subject matters and the debtor only needs to perform one of them, the debtor has the right to choose which to perform unless otherwise provided by the law, agreed upon by the parties, or specified by transaction practices.[95] If, however, the party who has the right to choose does not make a choice within the agreed time limit or before the expiry of the performance time period and fails to choose within a reasonable time limit after being urged, the right to choose is transferred to the other party.[96]

The second provision is about notice and restriction.[97] Article 516 of the Civil Code requires that when a party exercises its right to choose, a timely notice should be provided to the other party.[98] Only if the notification reaches the other party, will the subject matter to be performed be ascertained. Once ascertained, the targeted subject matter for performance should not be changed unless agreed to by the other party.[99] A restriction imposed by Article 516 is that if any of subject matters available for choice could not be fulfilled due to the occurrence of a certain event, the party with the right to choose shall not choose the unfulfillable subject matter unless the unfulfillable situation is caused by the other party.[100]

The provisions on the joint *obligatio* and joint and several *obligatio* in the Civil Code are similar to, but more specific than, those in the 1986 General Principles of the Civil Law. Under the Civil Code,

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92 *See* 2020 Civil Code, *supra* note 1, art. 515.
93 *See id.* art. 582.
94 *Id.* art. 515.
95 *See id.*
96 *See id.*
97 *Id.* art. 516.
98 *See id.*
99 *See id.*
100 *See id.*

the joint *obligatio* may refer to either joint creditors' rights or joint debtors' liability.[101] In cases where there are more than two creditors and the subject matter involved can be divided, the creditors' right will be the joint creditors' right if the right of each of the creditors is based on the portion to which the creditor is entitled.[102] On the other hand, if there are two or more debtors, and each of the debtors is liable for a part of the debts, the debtors will be joint debtors or debtors with joint liability.[103] For both joint creditors and joint debtors, if the portions of credits or debts among the creditors or debtors are difficult to identify, they each will be deemed to have equal portion.[104]

Joint and several *obligatio* covers the "one for all" situation. As provided in Article 518 of the Civil Code, if there are two or more creditors, and some or all of the creditors can request the debtor to perform the debt, the creditors' right will be considered joint and several.[105] Likewise, if there are two or more debtors, and the creditor can request some or all of the debtors to perform the entire debt, the debtors bear joint and several debt liability.[106] Under Article 518, the joint and several creditors' right or debtors' liability may only be created by operation of law or by agreement of the parties.[107]

The complexity in joint and several *obligatio* lies with the determination of indemnity between or among joint and several creditors or debtors.[108] Pursuant to Article 519 of the Civil Code, a joint and several debtor who assumes more than their own share of debt shall have the right to recover the excess portion from the other joint and several debtors within their unfulfilled share and enjoy the rights of the creditor accordingly.[109] But the joint and several debtors' exercise of that right shall not harm the interests of the creditor. The defense available to other joint and several debtors against the creditor may be claimed against the joint and several debtor who sues to recover the excess portion. If, however, a joint and several debtor against whom the indemnity is sought is unable to perform its portion

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101 *See id.* art. 517.
102 *See id.*
103 *See id.*
104 *See id.*
105 *See id.* art. 518.
106 *See id.*
107 *See id.*
108 *See id.* art. 519.
109 *See id.*

of debt, the other joint and several debtors shall share it proportionally.[110]

Article 519 is quite abstract on its face. It essentially deals with the relationship among debtors who are jointly and severally liable for certain debt. Such a relationship implicates two basic rights: the right to recover (i.e., indemnification) and the right to subrogate (i.e., assume the creditor's rights). The precondition for application of Article 519 is that a joint and several debtor has paid an amount exceeding its own liability.[111] In this case, the joint and several debtor has the right to recover the excess portion from other joint and several debtors and obtain the corresponding creditor's right against the joint and several debtors at issue.[112]

With regard to joint and several debtors, the Civil Code also contains the rules that govern the allocation of liability in different situations. First, if some of the joint and several debtors perform so as to offset the debts or deposit the subject matter of debts, the debts of other debtors to the creditor shall be extinguished correspondingly and those joint and several debtors may recover from other debtors.[113] Second, if the debts of some joint and several debtors are forgiven by the creditors, the debts of other debtors to the creditors shall be eliminated within the scope of the liability shares that such joint and several debtors should bear.[114] Third, when the debts of certain joint and several debtors and the creditor's rights are combined and belong to the same person, after deducting the debtor's share the creditor's rights to other debtors continue to exist.[115]

In addition, the Civil Code requires that a joint and several creditor who actually receives payment based on the creditor's rights shall repay other joint and several creditors in proportion to their

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110 *See id.*

111 *Id.*

112 A similar provision can be seen from German Civil Code. Under Section 426 of German Civil Code, (1) The joint and several debtors are obliged in equal proportions in relation to one another unless otherwise determined. If the contribution attributable to a joint and several debtor cannot be obtained from him, the shortfall is to be borne by the other obligors obliged to adjust advancements. (2) To the extent that a joint and several debtor satisfies the obligee and may demand adjustment of advancements from the other obligors, the claim of the obligee against the other obligors passes to him. The passing of ownership may not be asserted to the disadvantage of the creditor. *See* Bürgerliches Gesetzbuch [BGB] [Civil Code], *supra* note 57, § 426.

113 *See* 2020 Civil Code, *supra* note 1, art. 520.

114 *See id.*

115 *See id.*

creditors' rights.[116] If the actual shares of creditors' rights are difficult to ascertain, the joint and several creditors shall be deemed to have equal shares.[117] The same rule also applies to joint and several debtors.[118] The portion of the debts among the joint and several debtors will be considered equal if the actual portion for each debtor is unable to be determined.

Also, under Article 520 of the Civil Code, if the creditor's acceptance of the payment made by some of the joint and several debtors is delayed, the legal effect of such delay shall be applicable to other joint and several debtors.[119] The idea is that when the debtor is fulfilling the obligation to pay, the creditor's delay in acceptance may cause losses to the debtor. It then would be unfair to have the debtor bear the loss resulting from the delay by the creditor.

Since the purpose of establishing joint and several debts is to realize the creditor's right, when the creditor accepts the full performance from a joint and several debtor, the debt liability of all joint and several debtors will be discharged.[120] If, however, the creditor delays in accepting performance, it will affect not only the performing debtor but also other debtors who are jointly and severally liable for the debt. Therefore, in its delay in accepting performance, the creditor should be responsible for possible loss of both the joint and several debtor fulfilling the obligation and other joint and several debtors involved.

C. Quasi-Contract and Non-Contractual Obligations

Quasi-contract is a new system in the law of contract under the Civil Code. As a legal concept, quasi-contract is not a native product of China. Historically, as noted, quasi-contract originated from the Roman concept of *obligationes quasi ex contractu* (quasi-contractual obligations).[121] Due to the fact that it was not a mutually agreed-to obligation, quasi-contract was considered a statutory obligation not

116 *See id.* art. 521.

117 *Id.*

118 *See id.*

119 *See id.*

120 *See id.* art. 520 ("where one of the debtors assuming joint and several liabilities has performed his obligation . . . the obligation of the other debtors owed to the creditor is extinguished to the corresponding extent . . . ").

121 *See* SMITH, *supra* note 63, at 819.

resting upon the consent of the parties.[122] Now, in American contract law theory, quasi-contract is used as a synonym of contract implied in law, meaning that it is not really a contract at all but a legal fiction.[123]

The Civil Code provides no definition to quasi-contract. Instead, it divides quasi-contract into two categories: *negotiorum gestio* and unjust enrichment.[124] In many other countries, both *negotiorum gestio* and unjust enrichment are considered non-contractual obligations, and each of them is an independent source of *obligatio* by the operation of law.[125] In China, however, they are grouped together under quasi-contract, which constitutes part of the law of contract, although many believe that they are not obligations arising from contract.[126]

Under Article 979 of the Civil Code, *negotiorum gestio* occurs where a person without statutory or consensual obligations manages the affairs of others in order to avoid loss in the interests of others.[127] In the case of *negotiorum gestio*, the managing person may request that the beneficiary repay the necessary expenses incurred in the management of affairs, and if the managing person suffers losses due to the affair management, he may request that the beneficiary make appropriate compensation.[128]

Article 979 also contains certain requirements for the managing person in order to make *negotiorum gestio* actionable for compensation.[129] First, the management of affairs must conform to the real intention of the beneficiary, unless the real intention of the

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122 *See* William Keener, *Quasi Contract, its Nature and Scope*, 7 HARV. L. REV. 57, 68 (1893).

123 *See* EDWARD A. FARNSWORTH, CONTRACT 101 (3d ed., 1999); JEFFREY FERRIELL, UNDERSTANDING CONTRACTS 4 (2d ed., 2009); DAVID EPSTEIN, BRUCE A. MARKELL & LAWRENCE PONOROFF
, MAKING AND DOING DEALS: CONTRACTS IN CONTEXT 955 (2d ed. 2006). For general discussion of quasi contract as used in the common law system, see Timothy Sullivan, *The Concept of Benefit in the Law of Quasi Contract*, 64 GEO. L.J. 1 (1975).

124 In the 2020 Civil Code, Part III of Contracts is entitled "Quasi Contract," which includes two chapters: *negotiorum gestio* and unjust enrichment.

125 Under 2007 EU Regulation on the Law Applicable to Non-Contractual Obligations, for example, *negotiorum gestio* and unjust enrichment, together with torts and *culpa-in-contrahendo* (pre contractual liability) are categorized as non-contractual obligations. *See* Commission Regulation (EC) 864/2007, 2007 O.J. (L 199/40).

126 *See* SHEN WEIXING, CIVIL LAW 500, 508 (2013) (where *negotiorum gestio* and unjust enrichment are termed as statutory *obligatio* in contrast to the contractual *obligatio*). *See also* JIANYUAN, *supra* note 10, at 283, 315.

127 *See* 2020 Civil Code, *supra* note 1, art. 979.

128 *See id.*

129 *See id.* art. 979.

beneficiary violates the law or public order and good morals.[130] Second, the methods used to manage the affairs of others shall be beneficial to the beneficiary, and the managing work may not be interrupted if that interruption is detrimental to the beneficiary.[131] Third, if possible, the beneficiary shall be promptly notified of the managed affairs. If the managed affairs need not be dealt with urgently, the managing person shall wait for the instruction from the beneficiary.[132] And fourth, after the managing work is complete, the managing person shall report to the beneficiary on the status of the managed affairs, and any property acquired during the affair management shall be timely transferred to the beneficiary.[133]

Unjust enrichment involves benefits obtained without legal justification so that a restitution would be prompted as a matter of fairness.[134] In the United States, unjust enrichment is viewed as an equitable principle under which restitution is sought to prevent a person from being enriched at the expense of another.[135] Although the debates on how unjust enrichment should be defined and applied never rested throughout the development of the concept, the most recent contract law literature has interpreted unjust enrichment as an "enrichment that lacks adequate legal basis."[136] The legal basis in this context is understood to refer to such legal sources as contracts, trusts, gifts, and so on.[137] In many cases, the discussion of unjust enrichment is closely related to quasi-contract.[138]

In China, like many other civil law countries, unjust enrichment is a statutory claim. Under Article 92 of the 1986 General Principles of Civil Law, unjust enrichment refers to the benefits that are acquired improperly and without a legal basis.[139] In the case of unjust enrichment, restitution shall be made if the enrichment results in loss to the other party.[140] The Civil Code follows the provision of Article

130 *See id.*
131 *See id.* art. 981.
132 *See id.* art. 982.
133 *See id.* art. 983.
134 *See Unjust Enrichment,* BLACK'S LAW DICTIONARY (11th ed. 2019).
135 *See* FARNSWORTH, *supra* note 123, at 103.
136 *See The Intellectual History of Unjust Enrichment*, 133 HARV. L. REV. 2077, 2099 (2020).
137 *See id.*
138 *See* EPSTEIN, MARKELL & PONOROFF, *supra* note 123, at 956–98.
139 Grey & Zheng, *supra* note 32, art. 92.
140 *See id.*

92 of the 1986 General Principles of Civil Law but makes certain exceptions to the restitution.

In accordance with Article 985 of the Civil Code, no restitution shall be granted if (a) a payment is made to fulfill moral obligations; (b) repayment of debts is made before maturity; and (c) a debt repayment is made with the knowledge that there is no obligation to pay.[141] The rationale underlying Article 985 is that in any of those three situations, no unjust enrichment occurs. Article 985 then constitutes a legal basis on which the receipt of payments is justified. In the first situation, for example, if a payment is made to support elder relatives, no restitution is allowed on the basis of unjust enrichment due to moral obligations.

In addition, the Civil Code sets forth three particular rules on restitution in case of unjust enrichment. The first one is the non-return rule. Pursuant to Article 986, if a recipient does not know and should not know that the benefits obtained have no legal basis, and the benefits obtained no longer exist, the recipient has no obligation to return the benefits.[142] The second rule is the rule of compensation. In accordance with Article 987, if a recipient knows or should know that the benefits obtained have no legal basis, the person who has suffered losses may request the recipient to return the benefits obtained and to compensate for the losses under the law.[143] The third rule is the rule of claim against third parties. It is provided in Article 988 that if the recipient has transferred the benefits obtained to a third party gratis, the person who has suffered losses may request the third party to bear the obligation of return to the corresponding extent.[144]

D. Preliminary Contract and Liability

A highlighted feature of contract law under the Civil Code is the concept of preliminary contract that makes the parties' agreement to enter into a contract a contractual obligation. Under Article 495 of the Civil Code, the agreement by the parties to execute a contract within a certain period of time in the future—including letter of subscription, letter of orders, letter of reservation, and the like—constitutes a preliminary contract,[145] meaning an agreement to enter into a contract or an agreement to agree. The legal effect of the agreement as such

141 *See* 2020 Civil Code, *supra* note 1, art. 985.
142 *See id.* art. 986.
143 *See id.* art. 987.
144 *See id.* art. 988.
145 *See id.* art. 495.

creates an obligation to make a contract between the parties. Therefore, as Article 495 provides, if one of the parties fails to perform the obligation to make the contract as promised, the other party may hold him liable for breach of that preliminary agreement.[146]

Previously, the obligation arising from a preliminary agreement to contract was handled under pre-contractual liability. The legal provision of pre-contractual liability in current Chinese law is Article 42 of the Contract Law. Pursuant to Article 42, a party shall be liable for losses caused to the other party if, during the formation of contract, it (a) disguises and pretends to conclude a contract and negotiates in bad faith; (b) conceals deliberately the important facts relating to the conclusion of the contract or purposefully provides false information; or (c) engages in other acts in violation of the principle of good faith.[147]

In its 2012 Interpretation on the Issues Involving Application of Law in Adjudicating Disputes over Sales Contracts, the SPC for the first time used the term "preliminary contract" to describe pre-contractual obligations arising during contract negotiation.[148] According the SPC, when the parties sign a preliminary contract—such as a letter to prescribe, letter of order, letter of booking, letter of intent, or memorandum— under which they agree to conclude a contract of sales at a specified time in the future, and one party fails to fulfill the obligation to enter into the contract, the other party may bring a suit against him for breach of preliminary contract or for rescission of preliminary contract and seek compensation for damages.[149]

Compared with the SPC's interpretation, Article 495 of the Civil Code more directly defines the preliminary contract and emphasizes the liability for the breach of such a contract.[150] But in substance, both the SPC's interpretation and Article 495 of the Civil Code are premised on the view that the preliminary contract is a mutually independent contract from the main contract, and that the liability for breach of the preliminary contract is not based on negligence but rather an independent contractual obligation.

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146 *See id.*

147 *See* 1999 Contract Law, *supra* note 33, art. 42.

148 *See* Fa Shi 2012 [Interpretation of Supreme People's Court on Applicable Legal Issues in Trial of Cases of Sale and Purchase Contract Disputes] (adopted March 31, 2012, issued May 10, 2012), https://www.chinacourt.org/law/detail/2012/05/id/145832.shtml.

149 *Id.*

150 2020 Civil Code, *supra* note 1, art. 495.

Article 495 is significant because it extends the preliminary contract obligation to all contracts and creates a statutory claim by which a party may be held liable for failure to perform.[151] As a practical matter, when making a promise to enter into a written contract in a certain written form during negotiations, the parties may subject themselves to contractual liability if they fail to reach the final deal. Put differently, Article 495 of the Civil Code provides a legal ground on which a party may make a claim against the other party for breach of preliminary contract under this circumstance.

III. PRINCIPLE OF VOLUNTARINESS AND FREEDOM OF CONTRACT

In many Western countries, contracting parties are given broad power to decide their bargains under the notion of freedom of contract. Labeled as a slogan for laissez-faire capitalism, the concept of freedom of contract, however, was not recognized in China until after the Country opened up to the outside world in the late 1970s.[152] Among the attributes of the denial of freedom of contract was the fear of Western influence. Such a fear has been a dominant force in China for the past several decades, during China's endeavors to join the mainstream world economy, and the fear remains discernable in Chinese legislation.

Many in China believe that the domestic statutory acceptance of freedom of contract began with the adoption of the Contract Law in 1999.[153] Note, however, that the Contract Law did not use the term "freedom of contract," but instead emphasized "voluntariness." Under Article 4 of the Contract Law, the parties shall have the right to enter into a contract voluntarily in accordance with the law and no unit or individual may unlawfully interfere.[154] Article 4 was hailed among Chinese contract scholars as having addressed two essential elements of the freedom of contract: voluntariness and freedom from any external interference,[155] although the word "unlawful" appeared to be quite vague and confusing.

In the Civil Code, freedom of contract is, once again, provided under terms of voluntariness. Article 5 of the Civil Code makes it a general principle that civil parties shall abide by the principle of

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151 *See id.*

152 WANG LIMING, STUDIES IN CONTRACT LAW 151–52 (2002).

153 *See* WANG LIMING, CONTRACT LAW OF CHINA 14 (2016).

154 *See* 1999 Contract Law, *supra* note 33, art. 4.

155 *See* SUN LIHAI ET AL., A PRACTICAL EXPLANATION TO THE CONTRACT LAW 22–24 (1999).

voluntariness in conducting civil activities and shall, according to their own will, create, modify, or terminate civil legal relationships.[156] Article 5 applies to all civil legal relationships, including contracts.[157] Further, Article 130 provides that persons of civil law shall enjoy their civil rights according to law under their own will free from any interference; this is interpreted as the provision to protect individual freedom in civil affairs.[158]

Compared with the Contract Law, the Civil Code is viewed in China as further strengthening the concept of freedom of contract, even though the term "freedom of contract" does not appear in the provisions of the Civil Code.[159] This is true for several reasons. First, with regard to the process of contracting, the Civil Code reinforces the notion that a party has the right to decide whether to enter into a contract, how to conclude the contract, with whom the contract is to be made, and what the contents of the contract are to be.[160] Second, during performance, the parties may, by agreement, decide to make a supplement to or alter the contract.[161] Third, in the event of a dispute over the contract, the parties may voluntarily negotiate a dispute settlement method, and may also consult with each other on liquidated damages.[162]

More broadly, most of the provisions in Book III (Contracts) of the Civil Code are nonmandatory in nature,[163] which means that the parties can choose whether or not to apply them. The notion underlying the nonmandatory provisions is that, as imbedded in the concept of freedom of contract, the parties are the master of their own

156 *See* 2020 Civil Code, *supra* note 1, art. 5.

157 *See id.* Also, under Article 464 of the 2020 Civil Code, contract is defined as "an agreement to creates, modify, or terminate a civil legal relationship between civil subjects."

158 *See* YANG LIXIN & LI YIWEN, KEY POINT OF THE NEW RULES IN THE CIVIL CODE OF CHINA 116 (2020) ("The civil parties have the right to control the civil rights and rights that they enjoy according to their own wishes, exercise them according to their own desire, and fulfill their own needs and realize their own values through control and exercise of their rights.").

159 *See* SPC CIVIL CODE IMPLEMENTATION LEADING GROUP, UNDERSTANDING AND APPLICATION OF THE CIVIL CODE – GENERAL PROVISIONS 53–54 (2020) [hereinafter SPS CIVIL CODE IMPLEMENTATION LEADING GROUP]. The book covers five subjects in corresponding to the five books of the Civil Code, including General Parts, Property, Contracts, Torts, and Marriage and Family Relations.

160 *See id.* at 54.

161 *See id.* at 53.

162 *See* LIMING, *supra* note 153, at 14.

163 For most contract provisions provided in the Civil Code, the word "may" rather than "shall" is used to prescribe the obligations of the parties.

civil affairs in dealing with each other. Under this notion, the nonmandatory provisions simply serve as default rules and apply unless the parties have agreed differently. As reflected in the Civil Code, the adoption of nonmandatory provisions implicates an "agreement first" rule, representing the freedom of contract in a more specific way.[164]

A. Rule of "Agreement First"

For the purpose of the Civil Code, the rule of "agreement first" gives priority to the agreement reached by the parties in case there is a conflict between the parties' agreement and a legal provision.[165] For example, under Article 483, a contract is concluded when acceptance takes effect unless the parties agree otherwise.[166] It is held in China that a provision like Article 483 has the effect of prioritizing the parties' agreement; that is, if the parties have agreed on how a contract is to be concluded, the parties' agreement will trump the legal provision and take control if the legal provision is not mandatory.[167]

The rule of "agreement first" is premised on the belief that an agreement representing the true intent of the parties must be honored and enforced. Such an agreement, if not in violation of a mandatory provision of law, possesses a legal effect over that of a default provision. Where both an agreed provision and a legal provision coexist, the court or arbitration body is required to render its decision according to the provision as agreed by the parties rather than the legal provision. In a general sense, the rule of "agreement first" represents the principle of freedom of contract, which aims to provide the parties engaging in civil activities with the power of autonomy to create by agreement their own rights and obligations. Thus, an agreement, once made, is valid and enforceable as long as it does not violate any mandatory provision of law or regulation.

Many in China believe that "agreement first" was already a rule implicated in the Contract Law.[168] Under Article 60 of the Contract Law, the parties shall perform their obligations thoroughly according

164 *See* Shi Hong, Significant Development and Innovation of Contract Law Provisions in the Civil Code, 15 CHINA PEOPLE'S CONG. J., 1 (2020), http://www.npc.gov.cn/npc/c30834/202009/13d3ce4424044d4ab7766ba20cdb94b2.shtml.

165 *See id.*

166 *See* 2020 Civil Code, *supra* note 1, art. 483.

167 *See* LIMING, *supra* note 153, at 14.

168 *See* Hong, *supra* note 164.

to the terms of the contract.[169] The Civil Code expands the application of "agreement first," particularly to the matters involving the conclusion, effectiveness, performance, and allocation of liabilities of the contract.[170] Under Article 44 of the Contract Law, for example, the contract becomes effective when formed.[171] Article 502 of the Civil Code revises Article 44 of the Contract Law and provides that a contract is effective upon formation except when otherwise agreed upon by the parties.[172]

In its interpretation of the application of the Civil Code, the SPC opined that the Civil Code applied retroactively to contracts formed before the Civil Code took effect.[173] According to the SPC, for contracts concluded prior to the effectiveness of the Civil Code, if application of then effective law or judicial interpretation would render the contract invalid while the application of the Civil Code would make it valid, the relevant provisions of the Civil Code shall apply.[174] This interpretation exemplifies the SPC's position in favor of the parties' agreement.

B. Limitations on Contract-Making Power

Freedom of contract, or whatever it is termed, is not an unbounded principle. Rather, the autonomy of the parties to make a contract is subject to certain restrictions. In China, under the Contract Law, the parties must abide by the law and regulations,[175] must not violate any of the principles governing contracts,[176] must follow the state plan mandate and administrative supervision,[177] and must obtain government approval if required for the contract to become effective.[178] The Civil Code reiterates these restrictions so as to make them applicable to civil activities in general, while also revising the

169 *See* 1999 Contract Law, *supra* note 33, art. 60.

170 *See* Hong, *supra* note 164.

171 1999 Contract Law, *supra* note 33, art. 44.

172 *See* 2020 Civil Code, *supra* note 1, art. 502.

173 *See* SPC, *Several Provisions on the Statute of Limitations of the Application of the Civil Code of the People's Republic of China*, art. 9 (Dec. 29, 2020), http://www.hncourt.gov.cn/public/detail.php?id=183587.

174 *See id.*

175 *See* 1999 Contract Law, *supra* note 33, art. 7.

176 *See id.* art. 2–8. The principles governing contracts include equality and voluntariness, fairness and good faith, legality and public interests, and observance of contract.

177 *See id.* art. 38, 127.

178 *See id.* art. 44.

state plan mandate and good faith restrictions as applied to contracts.[179] In addition, the Civil Code makes it a duty for the parties to protect the environment under what is referred to as the "green" rule.[180]

1. Compulsory Contracting

In China, as noted, the parties have the right, under the principle of voluntariness, to determine whether to enter into a contract. The right, however, is limited where government mandatory tasks or purchase orders are involved.[181] According to Article 38 of the Contract Law, when the State issues a mandatory task or purchase order on the basis of necessity, the relevant legal persons or other organizations shall enter into contracts accordingly.[182] Article 38 serves two purposes: on the one hand, the parties involved are required to enter into a contract to implement the State mandatory task or fulfill the State purchase order; on the other hand, a contract would be considered invalid if it fails to follow such mandatory task or purchase order.

The State mandatory tasks derive from the State plan and are issued by the State for the need of the national economy and social development.[183] The issuance of mandatory tasks is a device by which the State directly manages such products or projects as those considered essential to the national security, public interest, and social welfare.[184] State purchase orders are the form of government procurement under the State plan to be fulfilled by particular business entities or enterprises. Both the State mandatory task and the State purchase order are aimed at maintaining State control over the production and distribution of certain products. Given its administrative nature, Article 38 is widely viewed as a residual of the planned economy that used to dominate the Country.[185]

The Civil Code revises Article 38 of the Contract Law and creates a rule of compulsory contracting. Under Article 494 of the Civil Code,

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179 *See* 2020 Civil Code, *supra* note 1, art. 4–8.

180 *See id.* art. 9.

181 *See id.* art. 494.

182 *See id.* art. 38.

183 *See* JIANG PING ET AL., PRECISE EXPLANATIONS OF CHINESE CONTRACT LAW 29 (1999).

184 *See id.*

185 *See* LIU WENHUA ET AL., NEW CONTRACT LAW: DETAILED EXPLANATIONS AND TYPICAL CASES 38 (1999).

where the State issues mandatory tasks or purchase orders, the civil subjects (i.e., persons) concerned shall conclude the contracts in accordance with the rights and obligations provided by the relevant laws or administrative regulations.[186] In contrast to Article 38 of the Contract Law, Article 494 of the Civil Code is distinctive in several aspects.

First, Article 494 expands the coverage of State mandatory tasks and purchase orders from "legal persons" or "other organizations" to "civil subjects"—a general term referring to all persons participating in civil activities.[187] Second, Article 494 defines the term "necessity" and limits the application of the mandatory contracting to such events as "emergency and disaster relief, pandemic prevention and control, or the like."[188] What is unclear, however, is whether "the like" would also include the needs for national defense, state key construction, as well as national strategic reserves.

The third and more striking aspect is that in Article 494, there is a new provision of mandatory offer and acceptance, which constitutes the core of compulsory contracting.[189] Pursuant to Article 494, the party that has an obligation to make an offer in accordance with the provisions of laws and administrative regulations shall make a reasonable offer in a timely manner, and likewise, the party that has an obligation to make an acceptance shall not reject the reasonable request of the other party to conclude a contract.[190] Thus, in light of Article 494, compulsory contracting is a process in which a contract is made where a party is required to make an offer to the other party, or a party is obligated to enter into a contract with the other party.[191] In either case, it is an obligation for a party to enter into a contract with the other.

Note, however, the compulsory offer and acceptance situation does not seem to be limited to circumstances where the state mandatory task or state purchase order is at stake. For example, under Article 648 of the Civil Code, a supplier providing electricity to the public shall not refuse a reasonable request of a consumer to conclude a contract for the use of electricity.[192] Similarly, it is provided in

186 *See* 2020 Civil Code, *supra* note 1, art. 494.
187 *See id*. *See also* 1999 Contract Law, *supra* note 33, art. 38.
188 *See* 2020 Civil Code, *supra* note 1, art. 494.
189 *See id.*
190 *See id.*
191 *See id.*
192 *Id.* art. 648.

Article 810 of the Civil Code that a carrier engaging in public transportation shall not reject an ordinary and reasonable transport request from a passenger or consignor.[193] In both situations, an acceptance is mandatory. But a question is raised about whether such a contract falls within the dimension of compulsory contracting.

2. Good Faith Mandate

Good faith is one of the principles that governs contracts in China and is purported to help maintain good business ethics and sound transaction order. The first time that the good faith legal principle was seen was in the 1986 General Principles of Civil Law, where it was phrased as "honesty and credibility."[194] Under Article 6 of the Contract Law, the parties to a contract were required to observe honesty and credibility in exercising their rights and fulfilling their obligations under the contract.[195] The 2017 GPCL specifically made good faith a civil law principle.[196] With the enactment of the Civil Code, Article 6 of the 2017 GPCL became Article 7 of the Civil Code.[197]

Under Article 7 of the Civil Code, a person conducting civil affairs should observe the principle of good faith, adhere to honesty, and commit to promise.[198] But like all previous civil law legislation, the Civil Code contains no definition of good faith. Nevertheless, the principle of good faith is commonly held in China to require that when conducting civil activities—including exercising civil rights, fulfilling civil obligations, and assuming civil liabilities—all persons or entities should uphold such ethical standards as honesty, good faith, credibility, and faithfulness to their promise.[199]

According to the SPC, good faith requires the parties conducting civil activities to (a) provide truthful information to each other and commit no misrepresentation or fraud; (b) exercise their own rights in sound and lawful means; and (c) deal reasonably and fairly with the

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193 *Id.* art. 810.

194 *See* Gray & Zheng, *supra* note 32, art. 4 (stating that in civil activities, the principles of voluntariness, fairness, making compensation for equal value, honesty, and credibility shall be observed).

195 *See* 1999 Contract Law, *supra* note 33, art. 6.

196 *See* 2017 GPCL, *supra* note 36, art. 6.

197 *See* 2020 Civil Code, *supra* note 1, art.7.

198 *See id.*

199 *See* SPC CIVIL CODE IMPLEMENTATION LEADING GROUP, *supra* note 159, at 63–65.

situation not clearly addressed between them or the circumstances that have changed so significantly as to affect their rights or obligations.[200] In the SPC's view, the good faith principle makes it imperative that the parties perform the contract fully as agreed upon, and, in the meantime, preserve such duties as notice, assistance, and confidentiality.[201] In addition, good faith as provided in the Civil Code imposes on the parties the duty to avoid waste of natural resources, environmental pollution, and destruction of ecological balance.[202]

As a practical matter, the good faith principle functions to fill gaps both in law and in contracts. Where certain provisions of a law are not clear or contain loopholes as to a particular issue or matter, the court or arbitration body may rely on the principle of good faith to construe the provisions and implement the law as intended.[203] As far as contracts are concerned, good faith analysis is a useful tool for the court or arbitration body to use in interpreting the terms in disputes and to help balance the rights and obligations of the parties.[204]

3. Duty to Maintain "Green"

A highly notable provision in the Civil Code is the "green" rule. Under Article 9 of the Civil Code, when conducting civil activities, any person shall act in a manner that facilitates conservation of resources and protection of the ecological environment.[205] It is the first time in the Country that the "green" rule appears in civil legislation and becomes a civil law principle.[206] Unlike other principles provided in the Civil Code, however, the "green" rule is more of a guidance than a mandate; meaning that it is a legal norm advocating, promoting, and guiding all civil actors to adopt specific behavior patterns.[207]

According to the SPC, the "green" rule, though not mandatory, plays a unique role in different aspects. First, it guides future civil legislation and helps formulate relevant laws and regulations in the civil area to achieve the "green" goal. Second, it sets standards for civil behavior in environmental protection and establishes basic compliance for people in their civil engagements. Third and more

200 *See id.* at 64.
201 *See id.*
202 *See id.*
203 *See id.*
204 *See* HAN SHIYUAN, *supra* note 43, at 41–42 (2011).
205 *See* 2020 Civil Code, *supra* note 1, art. 9.
206 SPC CIVIL CODE IMPLEMENTATION LEADING GROUP, s*upra* note 159, at 78.
207 *See id*. at 79.

practically, it provides certain standards for case adjudication. In other words, under the "green" rule, the conservation of resources and eco-environment protection become important factors the court should consider when adjudicating relevant cases.[208]

As applied to contracts, the "green" rule operates as a directive that imposes certain obligations on the parties in different aspects of the contract.[209] In one aspect, the "green" rule may create additional obligations for the contractual parties because, in making a contract, a duty to protect the environment could arise.[210] In another aspect, the "green" rule may affect the performance of the contract since the obligee could refuse to accept the performance if such performance is considered inconsistent with environmental protection.[211] Furthermore, the "green" rule may also influence the validity of a contract because a contract could be held void if the contract or the performance of it is deemed harmful to the environment.[212]

For example, under Article 509 of the Civil Code, the parties shall avoid wasting resources, polluting the environment, or damaging ecology during performance of the contract.[213] With regard to sales contracts, Article 619 further provides that absent an agreement between the parties on the packaging method or if the agreement is unclear, if the packing method cannot be determined and if there is no generally accepted method for the packaging, a manner that is sufficient to protect the item and is also conducive to preserving resources and protecting the ecological environment shall be used.[214]

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208 *See id.* at 80.

209 *See* He Jian, *Green Principle and Law & Economics*, 2 CHINESE JURIS. 110, 115–16 (2019).

210 *See id.*

211 *See id.*

212 *See id.*

213 *See* 2020 Civil Code, *supra* note 1, art. 509.

214 *See id.* art. 619. Other examples include article 558 ("After the parties' claims and obligations are terminated, the parties shall, in compliance with the principle of good faith and the like, perform such obligations as…recycling the used items according to the course of dealing"); article 625 ("Where, in accordance with the provisions of laws and administrative regulations or as agreed by the parties, the item shall be taken back for recycle after expiration of its service life. the seller has the obligation to have it recycled by himself or by an authorized third person"); and article 655 ("A consumer shall use the electricity in a safe, economical and planned manner in accordance with the relevant regulations of the State and the agreement between the parties.").

IV. CONTRACT PROCESS AND PARTY-ORIENTED RULES

The Civil Code modifies the Contract Law quite intensively, aiming to improve the contract system in the Country in both process and substance. By comparison, there are more than 300 changes made in the Civil Code to the Contract Law and over 150 of them are either newly added provisions or substantive amendments to the existing rules. Some notable changes in the general provisions are related to the formation and performance of contracts. Those changes are considered significant in the sense that they are purposed to cement the party autonomy in contracts.

A. Contract Formation

Under the Contract Law, to form a contract, mutual assent between parties is required, and that mutual assent is manifested and materialized through offer and acceptance.[215] Note, however, like in many other civil systems, consideration is not needed for the formation of a contract in China.[216] Therefore, for the purpose of the Contract Law, the process of contract formation is simply a matter of offer and acceptance. The Civil Code expands the contract formation to include "other means" in addition to offer and acceptance.[217] In the meantime, the Civil Code adds, as a new contract form, the electronic contract and refines the provisions governing the standard contracts.

1. Formation by the Means Other than Offer and Acceptance

Under Article 471 of the Civil Code, a contract may be formed between the parties by an offer and acceptance, or by other means.[218] Although generally a contract is formed via an offer and acceptance, the formation could be made without the offer and acceptance, or in a situation where the offer and acceptance cannot be ascertained.

The Civil Code does not specify what constitutes "other means." In one scholarly interpretation, "other means" refers to a process in which a contract is formed but there is no obvious expression of offer and acceptance by the parties.[219] In China, many consider the standard contract, reward contract, auction contract, and online shopping

215 *See* 1999 Contract Law, *supra* note 33, art. 13, 14.

216 *See id.* art. 13 ("The parties shall conclude a contract in the form of an offer and acceptance.").

217 *See* 2020 Civil Code, *supra* note 1, art. 471.

218 *See* 2020 Civil Code, *supra* note 1, art. 471.

219 LIXIN & YIWEN, *supra* note 157, at 270–71.

agreement as contracts that are formed by "other means" because such contracts either lack a clear external form of offer and acceptance or contain no identifiable process of offer and acceptance.[220] Others believe that the compulsory contract is a typical example of the contract formed by "other means."[221]

It seems hard to understand how a contract could be made without offer and acceptance because, as noted, offer and acceptance manifest the mutual assent of the parties. But the Civil Code appears to avoid unwanted debates or disputes over the finding of offer and acceptance in certain contracts and attempts to provide a more practical way than the conventional offer-acceptance scheme to ascertain the existence of a contract. The concept is that the "other means" could serve as a catch-all device to help prescribe and maintain a contractual relationship that would otherwise be uncertain between the parties. But confusion may arise when a determination of mutual assent becomes an issue if offer and acceptance, the common indicators of such assent, are missing.

2. Electronic Contract

The electronic contract involves the formality of contract. Under Article 10 of the Contract Law, the parties may conclude a contract in written, oral, or other forms.[222] Article 11 of the Contract Law further provides that a written form refers to any form that can tangibly show the described contents such as a contractual document, letter, or data-message (including telegram, telex, fax, Electronic Data Interchange, and email).[223] In contrast to the Contract Law, the Civil Code, while reaffirming the flexible rule concerning the formality of contracts, is more specific on the written forms. More noticeably, the Civil Code contains a number of provisions that govern electronic contracts.

First, Article 469 of the Civil Code provides that the written form refers to such forms that can tangibly carry the contents such as a contractual document, letter, telegram, telex, or fax.[224] It further provides that a data message in any form, such as electronic data exchange and e-mail that can show the contents contained in a tangible way and is accessible for reference and use at any time, shall be

220 *See id.*

221 *See* SPC CIVIL CODE IMPLEMENTATION LEADING GROUP, s*upra* note 159, at 60–61.

222 *See* 1999 Contract Law, *supra* note 33, art. 10.

223 *See id.* art. 11.

224 2020 Civil Code, *supra* note 1, art. 469.

deemed a written form.[225] The importance of Article 469 is that it codifies the written nature of electronic contracts and renders data messages a recognizable written form for the contract.[226]

Second, pursuant to Article 16 of the Contract Law, if an offer is made through data message, it will become effective at the time the data enters into the specified system if the offeree has designated such system to receive a data message, or at the time the data message first enters into the offeree's systems if no specific system is designated.[227] Article 137 of the Civil Code modifies Article 16 with regard to the situation where no specific data system is designated. Under Article 137, if no data system is specified, the offer will take effect at the time the other party knows or should have known that the data message has entered into its system.[228] The change is made in reference to the provision of the 2005 United Nations Convention on the Use of Electronic Communications in International Contracts, to which China is a member.[229]

Third, the Civil Code contains a provision that specifically governs the time of delivery for online contracts. In accordance with Article 512 of the Civil Code, unless otherwise agreed by the parties, the time of delivery for a contract made electronically is determined in three different ways, depending on the subject matter of the contract and the method of delivery: (a) if the subject matter involves goods, and the goods are to be delivered by express delivery services, the time of delivery is the time of the recipient's acknowledgment of receipt of the goods; (b) if the subject matter of the said contract relates to

225 *See id.*

226 *See id.*

227 *See* 1999 Contract Law, *supra* note 33, art. 16.

228 *See* 2020 Civil Code, *supra* note 1, art. 137.

229 The United Nations Convention on the Use of Electronic Communications in International Contracts was adopted on November 23, 2005 and went into effect March 1, 2013. China joined the Convention on June 7, 2006. Under Article 10(2) of the Convention, the time of receipt of an electronic communication is the time when it becomes capable of being retrieved by the addressee at an electronic address designated by the addressee. The time of receipt of an electronic communication at another electronic address of the addressee is the time when it becomes capable of being retrieved by the addressee at that address and the addressee becomes aware that the electronic communication has been sent to that address. An electronic communication is presumed to be capable of being retrieved by the addressee when it reaches the addressee's electronic address. U.N. COMM'N ON INT'L TRADE L., U.N. CONVENTION ON THE USE OF ELECTRONIC COMMUNICATIONS IN INTERNATIONAL CONTRACTS, U.N. Sales No. E.07.V.2 (2007), https://uncitral.un.org/sites/uncitral.un.org/files/media-documents/uncitral/en/06-57452_ebook.pdf.

services, the time for delivery is the time stated in the automatically generated electronic certificate or physical certificate, or the actual time of the delivery if there is no time stated in such a certificate or if the time stated therein is inconsistent with the actual time for the service to be provided; or (c) if the subject matter is to be delivered through online transmission, the time of delivery is the time when the subject matter enters the specific system that is designated by the other party and can be tracked and identified.[230]

The Civil Code stipulates, for the first time in the law of contracts, the formation and delivery time of the "electronic contract" executed through the internet and other information networks.[231] It intends to handle disputes that occur in judicial practice due to the lack of a provision in the Contract Law on matters involving online shopping.[232] It is believed that delivery is essential to the performance of electronic contracts and the determination of the delivery time would affect such matters as the allocation of risks, transfer of ownership, distribution of interests accrued, as well as price ascertainment.[233]

Thus, given the relevance of delivery to the respective rights and obligations of the parties of an electronic contract, and the significance of delivery to the contract performance and dispute settlement,[234] the Civil Code takes a further step and lays out a specific legal framework for the matter of delivery. More generally, premised on the notion that electronic contracts have become a major form in modern commercial transactions, the electronic contract provisions in the Civil Code constitute a regulatory basis to ensure the reliability of the online business dealings.[235]

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230 *See* 2020 Civil Code, *supra* note 1, art. 512.

231 In fact, much of the provisions concerning electronic contracts in the 2020 Civil Code incorporate the provisions of the E-Commerce Law of China. More specifically, art. 512 of the 2020 Civil Code is actually taken from art. 51 of the 2018 E-Commerce Law. The E-Commerce Law of China was adopted by the Standing Committee of the NPC on August 31, 2018. P.R.C. E-Commerce Law (2018), CHINA L. TRANS., https://www.chinalawtranslate.com/en/p-r-c-e-commerce-law-2018.

232 *See* SPC CIVIL CODE IMPLEMENTATION LEADING GROUP, *supra* note 159, at 363.

233 *See id.* at 359.

234 *See id.*

235 *See id.*

3. Standard Terms

Standard terms are defined in Chinese law as the terms that are prepared by one party in advance for repeated use and are not negotiated with the other party in concluding a contract.[236] In many cases, standard terms also refer to standard contracts. Both the Contract Law and the Civil Code recognize the legal effect of the standard terms but impose certain conditions. Under Article 39 of the Contract Law, for example, the party who supplies the standard terms is required to abide by the principle of fairness in defining the rights and obligations between the parties, and to provide notice to the other party in a reasonable manner with regard to a liability exclusion or alleviation clause.[237]

In contrast to the Contract Law, the Civil Code imposes more stringent conditions on the standard terms. The purpose is to ensure that the standard terms will not be abused, and rights and obligations between the parties will be balanced. To that end, the Civil Code altered the Contract Law in several aspects. First, under Article 496 of the Civil Code, the standard terms of which the other party must be made aware are expanded from the liability exclusion or alleviation clause to include clauses involving significant interests or concerns of the other party.[238] Article 496 provides the courts with a discretionary power to determine whether the interests and concerns of the other party are significant on a case-by-case basis.[239] As a practical matter, however, the main terms of a contract, or other terms that are related to the purpose of the contract or may affect the balance of rights and obligations of the parties are normally considered significant to the interests of the other party.[240]

Second, the Civil Code specifies the legal consequences of the standard terms provider's failure to fulfill its obligation to provide prompt notice. Unlike the Contract Law that is silent about what happens when the party providing the standard terms violates its notice duty, the Civil Code gives the other party an option to reject the standard terms if the required notice was not given.[241] Pursuit to Article 496, where the party providing the standard terms fails to make

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236 2020 Civil Code, *supra* note 1, art. 496.

237 *See* 1999 Contract Law, *supra* note 33, art. 39.

238 *See* 2020 Civil Code, *supra* note 1, art. 496.

239 *See id.*

240 *See* SPC CIVIL CODE IMPLEMENTATION LEADING GROUP, *supra* note 159, at 246–47.

241 *See* 2020 Civil Code, *supra* note 1, art. 496.

the other party aware of the terms that involve its significant interests and concerns, the other party may claim to exclude the terms from the contract.[242] According to the SPC, when such a claim is made, the People's Courts shall rule in favor of the claimant.[243]

Third, the Civil Code strengthens the review of reasonableness of the standard terms and invalidates the terms that restrict the main rights of the other party in a more specific way than the Contract Law. Under Article 497 of the Civil Code, in addition to the situation where a civil act is considered invalid, a standard term will become void if the term (a) unreasonably exempts or alleviates that party from liability, imposes a heavier liability on the other party, or restricts the major rights of the other party; or (b) deprives the other party of its main rights.[244] These two invalidation situations are also seen as the legal consequences of the standard terms provider's violation of the principle of fairness in determining the rights and obligations between the parties.[245]

Lastly, the Civil Code provides an interpretation rule for the standard terms. According to Article 498 of the Civil Code, where a dispute arises over the understanding of a standard clause, the clause shall be interpreted under its commonly understood meaning.[246] In addition, if there are two or more interpretations of a standard clause, the clause shall be interpreted against the party providing the standard clause.[247] Furthermore, when a standard clause is inconsistent with a non-standard clause, the non-standard clause shall prevail.[248]

B. Effect of Contract

A contract, once made, shall be binding to the parties unless the effect of the contract is called into question.[249] Put differently, a contract will take effect at the time it is concluded if its effectiveness is not impacted by internal or external factors. An internal factor refers to a condition imposed by the parties in the contract, while an external

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242 *See id.*

243 *See* SPC CIVIL CODE IMPLEMENTATION LEADING GROUP, *supra* note 159, at 243.

244 *See* 2020 Civil Code, *supra* note 1, art. 497.

245 *See* SPC CIVIL CODE IMPLEMENTATION LEADING GROUP, *supra* note 159, at 250.

246 *See* 2020 Civil Code, *supra* note 1, art. 498.

247 *See id.*

248 *See id.*

249 *See* LIMING, *supra* note 152, at 81–82.

factor is the requirement provided in the law. Under Article 502 of the Civil Code, a contract formed in accordance with the law becomes effective upon its formation unless otherwise provided by law or agreed upon by the parties.[250]

Compared with the Contract Law, the Civil Code contains more specific rules in ascertaining the effect of a contract. The Civil Code not only emphasizes the legal effect of the contract, but also includes provisions that deal particularly with the effect-to-be-determined contracts. In Chinese contract law, effect-to-be-determined contracts include those which: (a) are made by a party lacking contractual capacity, (b) require government approval, or (c) are concluded by a party who had no authority to make it.[251] The Civil Code revises the Contract Law mainly in the situation where government approval or due authorization is at issue.[252]

1. Presumption of Effectiveness

Contract in China is legally characterized as a civil act. Under Article 143 of the Civil Code, a civil act is valid and effective as a matter of law if (a) the person performing the act has the corresponding civil capacity, (b) there is a genuine expression of intent, and (c) it does not violate mandatory provisions of law or administrative regulation nor offend public order or social morals.[253] As noted, according to Article 502 of the Civil Code, a lawfully formed contract is effective upon its formation absent any obstacle to its effectiveness under the law or agreement.[254] The implication of Article 502 is that a contract will be presumed to become effective when concluded.

The notion underlying this presumption is that a court shall uphold the effectiveness of a contract, unless otherwise proven to be

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250 *See* 2020 Civil Code, *supra* note 1, art. 502.

251 *See* LIMING, *supra* note 152, at 96–97.

252 Note that under Contract Law, the effect-to-be-determined contracts also include unauthorized disposition contracts, or the contracts that are made by a party who has no right to disposal of the other's property. The Civil Code drops those provisions because a contract as such is considered to be more related to the property rights (property law issue) other than contractual obligation (a matter of contract law). For a general discussion, see Sun Xianzhong, *Comments on the Repeal of Article 51 of the Contract Law in the Draft Civil Code Concerning "No Right to Disposition,"* CHINA LEGAL NETWORK (Dec. 23, 2019), https://www.sohu.com/a/362788809_694573.

253 *See* 2020 Civil Code, *supra* note 1, art. 143.

254 *Id.* art. 502.

ineffective. The burden of proving ineffectiveness is on the complaining party, and the determination must be made either on the basis of the parties' agreement or under the provisions of the law.[255] It should be noted that the effectiveness of a contract is viewed differently from the validity of a contract in China, although an invalid contract has no effect. The former concerns primarily the time when the contract becomes binding, while the latter mainly involves enforceability of the contract.[256]

2. Contract Requiring Government Approval

Under Chinese laws, there are certain contracts that need government approval before taking effect. For these contracts, effectiveness is separate from formation, which means that such a contract, when formed, will not take effect until approved by the government.[257] Currently, there are four areas in which government approval is required for a contract to become effective, including finance and insurance,[258] transfer of the state owed property,[259] foreign investment,[260] and transfer of prospecting and mining rights.[261] Foreign investment mainly involves joint ventures.

Under the Contract Law, if a contract is subject to approval or registration as provided for by the laws or administrative regulations, the provisions of such laws or regulations shall be followed.[262] The Civil Code scraps the registration requirement and provides a number of rules concerning approval. The first rule is about the effect of contract. According to Article 502 of the Civil Code, if a party fails to

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255 *Id.*

256 *See* SPC CIVIL CODE IMPLEMENTATION LEADING GROUP, *supra* note 159, at 293.

257 2020 Civil Code, *supra* note 1, art. 502.

258 *See* [Law of the People's Republic of China on Commercial Banks] (promulgated by Nat'l People's Cong., May 10, 1995, adopted Dec. 27, 2003) (China) (stating that contract to purchase more than 5% of total equity stocks of a bank shall be subject to prior approval by the People's Bank of China).

259 *See* [Law of the People's Republic of China on State-Owned Assets in Enterprises] (promulgated by Nat'l People's Cong., Oct. 28,2008, effective May 1, 2009), art. 24 (China).

260 Prior to adoption of the Foreign Investment law in 2019, contracts to form a Sino-foreign joint ventures require government approval before taking effect after formation. After 2019, approval is required only for contracts to form foreign investment enterprises that falls within the negative list for foreign investment.

261 *See* [Mineral Resources Law] (promulgated by Nat'l People's Cong., Oct. 28, 2008, effective May 1, 2009), art. 24 (China).

262 *See* 1999 Contract Law, *supra* note 33, art. 44.

obtain approval so that the effectiveness of a contract is impacted, the effectiveness of the clauses concerning the obligation to file for approval, as well as other relevant clauses, shall not be affected.[263] This rule establishes an independence principle that separates the obligation to file an approval from the effectiveness of the contract itself. The implication of this rule is that absent government approval, the contract for which the approval is required will not be deemed invalid but ineffective.

The other rule deals with the right to make a claim. Pursuant to Article 502 of the Civil Code, if the party obligated to file application for approval or undertake other procedures fails to do so, the other party may request the former to bear the liability for breach of such obligation.[264] The practical significance of this rule is that if an approval is required for a contract, a failure to obtain the approval, although the contract would not take effect, creates a right for the other party to make a claim. In general, upon a request, the court will direct the obligated party to fulfill the obligation of filing. If the obligated party takes no action, the other party may ask for damages stemming from breach of contract.[265]

The third rule involves approval for modification, assignment, or dissolution of the contract. It is provided in Article 502 of the Civil Code that if under the provisions of the laws or administrative regulations, modification, assignment, or rescission of a contract is subject to approval or other procedures, such provisions shall be followed.[266] Thus, Article 502 of the Civil Code not only applies to a contract itself, but it also governs modification, assignment, or dissolution of the contract if government approval is required by the law or administrative regulations. The purpose is to help maximize the effectiveness of a contract freely entered into by the parties.[267]

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263 *See* 2020 Civil Code, *supra* note 1, art. 502.

264 *Id.*

265 *See* SPC CIVIL CODE IMPLEMENTATION LEADING GROUP, *supra* note 159, at 306–07.

266 *See* 2020 Civil Code, *supra* note 1, art. 502.

267 *See* SUP. PEOPLE'S CT., *Judicial Interpretation of Several Issues Concerning Application of Foreign Investment Law* art. 2, http://www.npc.gov.cn/npc/c30834/201912/c1cbc5a2b7c44e68bd9eb7829cf71af5.shtml. For example, in its Judicial Interpretation of Several Issues Concerning Application of Foreign Investment Law, the SPC makes it clear that in the case of an investment contract formed in a field outside the negative list of foreign investment access referred to in Article 4 of the Foreign Investment Law, where the parties claim that the contract is invalid or has not entered into force on the grounds

3. Contract by Agent Without Due Authorization

Under Chinese law, a contract made by an agent, if duly authorized to act on behalf of the principal, will bind the principal.[268] In many cases, however, authorization becomes problematic. The situations in which an agent is considered to lack due authorization include: (a) there is no authorization, (b) authorization has been revoked or held ineffective, (c) the scope of authorization has been exceeded, or (d) the authorization has expired or terminated.[269] The issue then is whether a contract entered into by an agent in any of these situations would have a binding effect on the principal.[270]

Under the Contract Law, a contract made by an agent without due authorization will not bind the principal unless and until the principal ratifies it or the other party has reason to believe that the agent has been duly authorized.[271] The former refers to actual authority of the agent, while the latter implicates the apparent authority of the agent.[272] The Contract Law, however, is silent on how the ratification should be made, particularly in a case where the principal has performed under the contract entered into by the unauthorized agent.

The Civil Law fills this gap by providing a rule of implied ratification. According to Article 503 of the Civil Law, if a person without authority concludes a contract in the name of a principal, and the principal has already started performing the contractual obligations or accepted the performance of the other party, the contract is deemed ratified.[273] Article 503 is premised on the notion that to maintain the free will and equal status of the parties, it is important for the parties to recognize their own performing acts in the process of contract performance, as well as the performance of the other party. Thus, under Article 503, the principal's ratification could be made either expressly or implicitly.

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that the contract has not been approved or registered by the relevant administrative department, the People's Court shall not grant the claim.

268 As provided in Article 162 of the Civil Code, a civil legal act performed by an agent in the principal's name within the scope of authority in binding on the principal. *See* 2020 Civil Code, *supra* note 1, art. 162.

269 *See* SPC CIVIL CODE IMPLEMENTATION LEADING GROUP, *supra* note 159, at 854–855.

270 *See id.* at 809.

271 *See* 1999 Contract Law, *supra* note 33, art. 48.

272 *See* SHIYUAN, *supra* note 43, at 213.

273 *See* 2020 Civil Code, *supra* note 1, art. 503.

C. Fulfillment of Contractual Obligations

As noted, under both the Contract Law and the Civil Code, the parties are required to fully perform their respective obligations as agreed upon in the contract. Believing that fulfillment of contractual obligation is essential to the achievement of the purpose of contract, many Chinese scholars view performance as the core of the contractual relationship.[274] But there are certain situations, either by operation of law or by agreement, in which the obligation to perform the contract can be excused or the contractual relationship can be terminated.[275] The Contract Law provides a number of statutory grounds for dissolving or terminating a contract.[276] The Civil Code embraces the provisions of the Contract Law together with new provisions that are drawn from the actual practices of Chinese courts. The most notable provisions include the rule of obligation offset by the parties and the rule dealing with circumstantial changes during contractual performance.[277]

1. Obligation Offset

Obligation offset is the rule that allows the parties mutually obligated to each other to discharge contractual obligation to the equal amount. It is provided in Article 99 of the Contract Law that where the parties to a contract have debts due mutually and the category and character of the debts are the same, any party may offset his debt against the other's unless prohibited by the law or not suitable according to the character of the contract.[278] Article 100 of the Contract Law further provides that the parties may, by agreement, offset the debts due to each other even though the category and character of the debts are different.[279]

The key element of the statutory offset is the mutual maturity of debts, meaning that the debts, to be offset, must both be due. The Civil Code also recognizes the rule of obligation offset.[280] But unlike the Contract Law, the Civil Code does not require mutual maturity in the

274 *See* LIMING, *supra* note 153, at 127.
275 *See id.* at 183–84.
276 *See* 1999 Contract Law, *supra* note 33, art. 91–94.
277 See 2020 Civil Code, *supra* note 1, art. 533, 586.
278 *See* 1999 Contract Law, *supra* note 33, art. 99.
279 *See id.* art. 100.
280 *See* 2020 Civil Code, *supra* note 1, art. 586.

statutory offset.[281] According to Article 568 of the Civil Code, when the parties mutually owe obligations to each other and the subject matter of the obligations are of the same category and character, any party may offset his obligation against the due obligation of the other party, unless the obligation cannot be offset by the nature of the obligations or by the agreements of the parties or the provisions of law.[282]

Note also that with regard to the exceptions to the statutory offset, there are two aspects in which Article 568 of the Civil Code differs from Article 99 of the Contract Law. First, the Civil Code changes "the nature of contract" as provided in the Contract Law to "the nature of obligations."[283] The change as such is considered necessary because the term "obligations" more accurately reflects the purpose of offset than the term "contract" does.[284] Second, in addition to "the provisions of law" and "the nature of obligations," the Civil Code allows the parties by agreement to prohibit certain obligation offset, giving the parties the power to determine their own dealings as they wish.[285]

2. Change of Circumstances

Change of circumstances refers to the situation when, during the performance of contract, the basic presumption on which the contract is formed has changed so significantly as to make the continuing performance of the contract as originally agreed upon obviously unfair and unreasonable.[286] Thus, the circumstance so changed prompts a need to modify or rescind the contract. The theoretical basis justifying the modification or rescission as such is the doctrine of *rebus sic stantibus* (thing thus standing).[287]

Borrowed from international law of treaties, the doctrine of *rebus sic stantibus* as applied in contracts provides the parties with a legal ground not to perform the original terms and conditions of contracts given a fundamental change of circumstances.[288] This doctrine,

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281 *See id.*

282 *See id.*

283 *See id.*

284 *See id.*

285 *See id.*

286 *See* SPC CIVIL CODE IMPLEMENTATION LEADING GROUP, *supra* note 159, at 477–78.

287 *See id.*

288 For a general discussion of the *Rebus Sic Stantibus* doctrine, see John P. Bullington, *International Treaties and the Clause "Rebus Sic Stantibus*," 76 UNIV. PENN. L. REV. 153 (1927).

however, was not legislatively accepted in China until the adoption of the Civil Code, although it had been recognized by Chinese courts in their judicial practices for many years. The delay was due to the difficulty of defining the term "changed circumstances."[289] The Civil Code, for the first time in Chinese contract legislation, adopts the doctrine of *rebus sic stantibus* and makes it a statutory excuse for non-performance of a contract.[290]

In accordance with Article 533 of the Civil Code, the application of *rebus sic stantibus* must meet certain conditions. First, the change at issue must involve the basic condition upon which the contract was made; second, the change must be objective and unforeseeable at the time of contract; third, the change must not fall within any of the commercial risks; and fourth, continuing performance of the contract must result in obvious unfairness to one of the parties.[291] Under those circumstances, the parties may negotiate for a solution. If the parties are unable to reach an agreement, any of the parties may file a claim either with a court or with an arbitration body for modification or rescission of the contract. It is required under Article 533 that upon the request by the parties, a People's Court or an arbitration body shall modify or rescind the contract in compliance with the principle of fairness, taking into account the actual circumstances of the case.[292]

Article 533 of the Civil Code sets forth the rule for modification or rescission of a contract under the doctrine of *rebus sic stantibus*. There are, however, at least three questions left unanswered. One question is about the differences between "change of basic condition" and "*force majeure*." More specifically the question is whether the two are mutually exclusive or are overlapping. The other question is how to differentiate between "change of basic condition" and "commercial risk." This question is concerned with how the commercial risk should be defined and determined. The third question involves the obvious unfairness. As a practical matter, the question is to what extent an unfairness may be considered obvious.

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289 *See* MO ZHANG, CHINESE CONTRACT: THEORY AND PRACTICE 276 (2d ed. 2020).

290 *See* SPC, CIVIL CODE IMPLEMENTATION LEADING GROUP (CONTRACTS), *supra* note 159, at 478.

291 *Id.*

292 *See id.*

D. Third Party

In Chinese contract law, there is no particular section that primarily deals with third party interests. Rather, the issues concerning the third-party interests are addressed in scattered provisions. Under the Contract Law, the third party generally is implicated in three situations: (a) where a third party receives the benefit of performance, (b) where a third party is assigned a duty to perform, and (c) where a third party has caused a breach of contract.[293] Thus, for the purpose of the Contract Law, the third party in China is understood to include any person, other than the parties, who may affect or has a relation to the performance of the contract.[294]

The third-party provisions of the Contract Law are now merged into the Civil Code. While recognizing the third-party interests set forth in the Contract Law, the Civil Code rectifies the Contract Law to more effectively handle third-party interests. The most notable changes include the third party's right to make a claim, third-party performance, and the third-party accession to the debts. Under the theory of privity, a contract has the effect of binding parties only and may not externally affect others. The changes the Civil Code makes to the Contract Law break the privity to the extent that the third party's interests become an issue.

1. Third Party Claim on the Basis of Contract

Pursuant to Article 64 of the Contract Law, where the parties agree that the obligor shall perform contractual obligations to a third party, but failed to perform or the performance made does not meet the terms of the contract, the obligor shall be liable to the obligee for the breach of the contract.[295] This provision imposes an obligation on the obligee but does not address how the interests of the third party involved are to be protected, particularly in a case where the third party is a person who will benefit from the performance of the contract.

Under the Contract Law, a third party receiving performance may either be the person upon whom the benefit of contract will be conveyed through performance or the person who only received the performance on behalf of an obligee for the benefit of the obligee. The third party in the latter case is actually an agent rather than a beneficiary. In the former case, however, since the third party is a

293 *See* ZHANG, *supra* note 288, at 381–92.

294 *See id.*

295 *See* 1999 Contract Law, *supra* note 33, art. 64.

beneficiary of the performance of the contract, a question then is whether the third party may make a claim if no performance is made or the performance contains defects. This question was left unresolved in the Contract Law.

The Civil Code contains a new provision that intends to grant the third-party beneficiary a right to make a claim against the obligor. According to Article 522 of the Civil Code, where it is provided by law or agreed upon by the parties that a third person may directly request the debtor to perform the obligation to him, and the third person does not explicitly reject it within a reasonable period of time, the third person may request the debtor to bear default liability if the debtor fails to perform the obligation to the third person or the performance does not conform to the agreement.[296]

Based on Article 522 of the Civil Code, the third-party beneficiary's right to directly make a claim has two sources: the law and the parties' agreement. But the prerequisite to the exercise of such right is that the third party must make no objection. In accordance with Article 522, a third party need not make an acceptance of the benefit to be conveyed by the parties in order to make his right vested, but will acquire the right if no objection is expressly made within a reasonable period of time. On the other hand, however, under Article 522, a defense that the debtor has against the creditor may be asserted against the third party.[297]

2. Third Party Performance for its Own Benefit

As noted, third party performance in the Contract Law occurs when the parties agree that the third party performs the obligation to the obligee.[298] In other words, under the Contract Law, the parties' agreement constitutes the basis on which the performance is to be made by a third party. The Civil Code creates a new ground for the performance by a third party, and the performance as such can be made without the parties' agreement. According to the SPC, the new provision in the Civil Code is intended to serve the purposes of improving transaction efficiency, facilitating the realization of creditor's rights, and reducing civil disputes.[299]

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296 *See* 2020 Civil Code, *supra* note 1, art. 522.

297 *See id.*

298 1999 Contract Law, *supra* note 33, art. 65.

299 *See* SPC CIVIL CODE IMPLEMENTATION LEADING GROUP, *supra* note 159, at 421.

It is provided in Article 524 of the Civil Code that where a debtor fails to perform an obligation, and a third person has a lawful interest in the performance of the obligation, the third person is entitled to perform it to the creditor on behalf of the debtor unless the obligation may only be performed by the debtor based on the nature of the obligation, as agreed by the parties, or as provided by law.[300] Article 524 further provides that after the creditor accepts the performance of such obligation by the third person, his claim against the debtor shall be assigned to the third person unless otherwise agreed by the debtor and the third person.[301]

As interpreted by the SPC, the application of Article 524 of the Civil Code shall meet certain requirements. First, there is no agreement between the parties for the third party to perform the contract; second, the obligor does not, or is unable to, perform the contract; third, the third party has a legitimate interest in the performance of the contract; and fourth, the third party is not excluded from performing based on the nature of the contract, by the agreement of the parties, or under a provision of the law.[302]

3. A Third Party's Joining of the Debts

In a contract, once a creditor-debtor relationship is created, the relationship exists only between the parties, and thus the debtor is normally a party to the contract. In certain cases, however, a third party may voluntarily make accession to the debts that incur between the parties under the contract.[303] The accession may also be called debt assumption, which can be made independently by the third party or jointly with the existing debtor.[304] The former is often seen in the case of novation while the latter normally implicates delegation.[305]

The assumption of debts by a third party under the provisions of the Civil Code refers to the situation in which a third party voluntarily joins the debts and performs the contract along with the original debtor.[306] With the third party joining the debts, the creditor is further secured to realize his rights and interests through the contract

300 *See* 2020 Civil Code, *supra* note 1, art. 524.

301 *See id.*

302 *See id*.

303 For a general discussion on the assumption of debts by a third party, see John Tsai, *Assumption of Obligations: Third Party No More*, 45 LA. L.R. 819 (1985).

304 *See id.* at 820–21.

305 *See* E. ALLEN FARNSWORTH, CONTRACTS 747 (3d ed. 1999).

306 2020 Civil Code, *supra* note 1, art. 552.

performance. In this case, the original debtor remains liable for the contractual obligation.[307] The difference between the debt joining and delegation is that, unlike the delegation, the debt joining does not require the consent of the creditor.[308]

Under Article 552 of the Civil Code, where a third person agrees with the debtor (i.e., obligor) to join in the obligation and notifies the creditor (i.e., obligee) of it, or a third person indicates to the creditor his willingness to join in the obligation, if the creditor fails to explicitly make a rejection within a reasonable period of time, the creditor may request the third person to assume the joint and several obligation with the debtor to the extent of the obligation the third person is willing to assume.

The SPC construes Article 552 as consisting of four elements: (a) there exists an original credit-debt relationship under the contract; (b) a third party agrees to join the debt as a new debtor; (c) the debt owed by the original obligor is not reduced or exempted; and (d) consent of the creditor is not needed as long as the creditor is notified or the creditor does not expressly object within a reasonable period of time.[309] A key feature of the debt joining is that upon the third party's joining the debt, the third party and the debtor are jointly and severally liable for the contractual obligations.[310] In other words, the creditor may sue the third party for the entire debt if non-performance or non-conforming performance occurs.

V. CONTRACTUAL OBLIGATION AND CREDITORS' RIGHTS

A contractual obligation refers to the duties the parties are bound to fulfill under the contract they have entered into. A failure of either party to perform under the terms of the contract will constitute a breach of contract for which legal remedy could be sought. Therefore, a proper performance of the contract is purported to achieve what the parties have bargained for and what they have expected. More importantly, the performance is to realize the creditor's rights so that the obligation of the debtor will be discharged. A proper performance under Chinese law is a performance that is complete and adequate.

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307 *See* SPC CIVIL CODE IMPLEMENTATION LEADING GROUP, *supra* note 159, at 581–82

308 *See id.*

309 *See id.* at 582.

310 *See id.* at 583.

Both the Contract Law and Civil Code require that the parties fulfill their respective obligations they have agreed upon.[311] The Civil Code, however, emphasizes realization of the creditor's right. Premised on the notion that contract is a commitment of the parties and thus the reasonable expectation of the parties must be honored and protected in order to maintain the good order of business transactions, the Civil Code prescribes several new rules that are aimed at optimizing the rights created under the contract.

A. Principal and Secondary Rights

It is held in China that contractual rights consist of both a principal right and secondary right.[312] A principal right is the right independent of all other rights, and a secondary right, also called a collateral right, is the right attached to the principal right.[313] A security, for example, is the right secondary to the right secured. Since the secondary right is derived from the principal right, the secondary right cannot exist separately from the principal right.[314] Thus, if a principal right is invalid, the secondary right attached to it is also invalid. On the same ground, a secondary right would be eliminated with the elimination of the principal right.[315]

The Contract Law establishes a rule of secondary right subordinate to the principal right. Under Article 81, when an obligee (i.e., assignor) assigns its rights, the assignee shall acquire the secondary rights attached to the principal rights, except that the secondary rights exclusively belong to the obligee.[316] The implication of Article 81 of the Contract Law is that if the principal right is assigned, the rights collateral to the principal right will automatically be transferred to the assignee as well. Put differently, the holder of the principal right is also the holder of the rights subordinate to the principal right.[317]

The Civil Code follows the provision of Article 81 of the Contract Law.[318] But in addition to the rule of collateral right subordinate to the

311 *See* 1999 Contract Law, *supra* note 33, art. 60; 2020 Civil Code, *supra* note 1, art. 509.

312 *See* LIXIN & YIWEN, *supra* note 158, at 312.

313 *See id.* at 313.

314 *See* WANG LIMING, CONTRACT LAW RESEARCH (VOL. II) 245 (2003).

315 *See id.*

316 *See* 1999 Contract Law, *supra* note 33, art. 81.

317 *See* LIXIN & YIWEN, *supra* note 158, at 313.

318 *See* 2020 Civil Code. *supra* note 1, art. 547.

principal right set forth in Article 81, the Civil Code adds a provision signifying the effect of the collateral rights when the principal right is legally assigned.[319] Under Article 547 of the Civil Code, failure to register the assignment of the collateral right or failure to change the possession thereof shall not affect the acquisition of the collateral right by the assignee.[320]

Article 547 signifies the notion that transfer of a secondary right is a natural transfer resulting from assignment of the creditor's right, and thus is not affected by registration or possession even though the registration or possession is required for the effective assignment of the creditor's right.[321] More specifically, in accordance with Article 547, after a contractual right is assigned, the rights collateral to it will be transferred to the assignee regardless of whether the secondary rights are registered or the possession of such rights is transferred.[322]

B. Modification and Assignment

In Chinese contract law, assignment is related to, if not a part of, modification.[323] It is typical in China that assignment and modification are not only provided together in the law, but also addressed jointly in contract law textbooks.[324] A common view among Chinese contract scholars is that modification can be defined both narrowly and broadly: a narrow definition involves only changes in the contents of a contract, while the broad definition includes changes in the parties or assignment.[325]

Both the Contract Law and the Civil Code provide that a contract may be modified upon agreement by the parties.[326] But, under the Contract Law, a government approval or registration must be obtained in order for the modification to be effective if such approval or registration is required by the law or administrative regulations.[327] The Civil Code, however, does not require registration and provides only

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319 *See id.*

320 *See id.*

321 *See* SPC CIVIL CODE IMPLEMENTATION LEADING GROUP, *supra* note 159, at 569.

322 *See* LIXIN & YIWEN, *supra* note 158, at 313.

323 *See* LIMING, *supra* note 153, at 161–62.

324 *See id*. ch. 7; 1999 Contract Law*, supra* note 33, ch. 5; 2020 Civil Code, *supra* note 1, Book III, ch. 7.

325 *See id.* at 161.

326 *See* 1999 Contact Law, *supra* note 33, art. 77; 2020 Civil Code, *supra* note 1, art. 543.

327 *See* 1999 Contract Law, *supra* note 33, art. 77.

that the modification shall be made on the basis of an agreement between the parties.[328] If an approval is needed, the rules of approval set forth, as noted, in Article 502 shall apply.

In addition, the Civil Code amends the Contract Law with regard to the assignment of a contract by providing a rule that stipulates the effect of a non-assignment agreement on the third party.[329] Developed from Article 79 of the Contract Law, Article 545 of the Civil Code provides three situations where a contractual right may not be assigned: (a) the right is not assignable by virtue of its nature; (b) the right is not assignable by agreement of the parties; or (c) the right is not assignable by operation of law.[330]

An issue arising from Article 79 of the Contract Law involves the interests of the third-party assignee, particularly in a case where the assignee is a *bona fide* third party. To deal with this issue, Article 545 of the Civil Code provides a third-party rule.[331] Under this rule, the effect of a non-assignment clause on an assignee depends on the nature of the right involved. If a pecuniary right is assigned, the non-assignment clause shall not be asserted against a third person.[332] If, however, the right assigned is non-pecuniary, the third party against whom the non-assignment agreement is asserted must be a *bona fide* third party.[333]

C. Preservation of Contract

Contract preservation is understood in China as a protective mechanism under which the creditor may take certain actions to ensure the realization of their right in a situation where the debtor purposefully reduces its property, increases its liability, or neglects to exercise its own creditor's right in order to evade its debt liability.[334] Under the Contract Law, the preservation of contract consists of two rights: the right of subrogation and the right of cancellation.[335] The

328 *See* 2020 Civil Code, *supra* note 1, art. 543.

329 *See* SPC CIVIL CODE IMPLEMENTATION LEADING GROUP, *supra* note 159, at 561–62.

330 *See* 2020 Civil Code, *supra* note 1, art. 545.

331 *See id.*

332 *See id.*

333 *See id.*

334 *See* LIMING, *supra* note 153, at 141.

335 1999 Contract Law, *supra* note 33, art. 73, 74.

Civil Code consolidates those two rights under the preservation of contract.[336]

1. Right of Subrogation

The right of subrogation is a civil right aimed at protecting the creditor right of the obligee. It allows the obligee, in his own name, to exercise the obligor's credit right against a third party who is a debtor of the obligor.[337] As provided in Article 73 of the Contract Law, if the obligor is indolent in exercising its due creditor right so as to damage the interest of the obligee, the obligee may ask the court for subrogation to exercise in its own name the obligor's creditor right, except that the credit right exclusively belongs to the obligor.[338]

The Civil Code formulates the right of subrogation in a new way. First, it expands the subrogation right to also apply to rights collateral to the obligor's creditor right.[339] According to Article 535 of the Civil Code, the right of subrogation may be exercised upon the obligee's request when a debtor is indolent in exercising its creditor right or a collateral right related thereto so that the realization of the obligee's due creditor right would be adversely affected.[340] Article 535 limits the scope of the right of subrogation to the obligee's creditor right that has become due.

Second, despite the limited scope prescribed in Article 535, the Civil Code further provides a protective rule that expands the application of subrogation to the obligor's creditor right not yet due.[341] Under Article 536 of the Civil Code, prior to the due date of the obligee's creditor right, where there exists a circumstance under which the statute of limitations for the debtor's principal right or a collateral right related thereto is to expire, or the debtor fails to timely declare his right in a bankruptcy proceeding, and the enforcement of the obligee's creditor right is thus adversely affected, the creditor may, by subrogation, request the debtor of the obligor to perform his obligation to the obligor, declare the debtor's right to the bankruptcy administrator, or take other necessary action.[342]

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336 2020 Civil Code, *supra* note 1, art. 535.
337 *See* ZHANG, *supra* note 289, at 259.
338 *See* 1999 Contract Law, *supra* note 33, art. 73.
339 *See* 2020 Civil Code, *supra* note 1, art. 535.
340 *See id.*
341 *See id.* art. 536.
342 *See id.*

Third, the Civil Code signifies the legal effect of the right of subrogation. Article 537 of the Civil Code provides that where the People's Court determines that the right of subrogation is granted, the debtor of the obligor shall perform the obligation to the obligee.[343] Article 537 further provides that, after performance is accepted by the obligee, the corresponding rights and obligations between the obligee and the obligor, and between the obligor and the obligor's debtor, are terminated.[344] In addition, when the debtor's creditor right or a collateral right related thereto against its debtor is subject to preservation or enforcement measures, or when the debtor becomes bankrupt, it shall be dealt with in accordance with the provisions of the relevant laws.[345]

2. Right of Cancellation

Similar to the right of subrogation, the right of cancellation is also purposed to protect the obligee's creditor right and to ensure that the contract will be fully performed. Unlike the right of subrogation, the right of cancellation applies when the obligor's gratuitous disposition or unreasonably priced transaction leads to a reduction in his property rights or improperly aggravated liability burden so that the realization of the obligee's creditor rights would be impaired. In this situation, the obligee, as the creditor of the obligor, may request the People's Court to cancel the obligor's transaction at issue or revoke the obligor's actions.[346]

The right of cancellation, as a statutory right, was first provided in Article 74 of the Contract Law.[347] The Civil Code differs from the Contract Law in that it separately provides more detailed rules for the gratuitous transfer of property and transactions at unreasonable prices. Under Article 538 of the Civil Code, if an obligor gratuitously disposes of his proprietary rights and interests by renouncing his creditor's right, disclaims the security for such right, or transfers his properties gratis, and the like, or if the obligor maliciously extends the

343 *See id.* art 537.

344 *Id.*

345 *See id.*

346 *See* LIMING, *supra* note 153, at 151–52.

347 If the obligor disclaims its due creditor's rights or transfers gratis its property and thus causes losses to the obligee, the obligee may apply to a People's Court to revoke the obligor's action. The obligee may also apply to a People's Court to cancel the debtor's action if the obligor causes losses to the obligee by transferring its property at a low price evidently unreasonable and with awareness of the transferee. *See* 1999 Contract Law, *supra* note 30, art. 74.

period of performance of due obligations, so that the enforcement of the obligee's creditor right is adversely affected, the obligee may request the People's Court to revoke the obligor's transactions involved.[348]

According to Article 538 of the Civil Code, to exercise the right of cancellation, three conditions must be met. First, the creditor's right of the obligee must be valid and effective against the obligor; second, the obligor must have done something resulting in a gratuitous transfer of property or related rights; third, the transactions involved must be harmful to the realization of the obligee's creditor rights.[349] In addition, in the situation where the obligor extends the period of performance of the debts owed to him, malice is a prerequisite.[350] Note that in the Contract Law, the renounced creditor right must be the right that is due already, while the Civil Code simply requires "creditor right" regardless of whether the right is due or not.

Article 539 of the Civil Code deals with the obligor's transfer of property at an unreasonable price, and it also includes a situation in which the obligor provides a guarantee for others.[351] Pursuant to Article 539 of the Civil Code, when the obligor transfers his property at an obviously unreasonably low price, takes another's property, or provides security for another's obligation at an obviously unreasonably high price so as to adversely affect the realization of the obligee's creditor right, the obligee may request the People's Court to revoke the obligor's act if the other knows or should have known such circumstance.[352]

To determine whether the price in the involved transaction is reasonable or not, the SPC develops a "transaction time and place" rule. According to the SPC, the reasonableness of the transaction price shall be determined on the basis of price prevalent at the time and location of the transaction.[353] In addition, the SPC sets forth a thirty percent standard to help judge reasonableness.[354] More specifically, if a transaction price is thirty percent lower than the local fair price at the time of the transaction, the transaction price will generally be

348 *See* 2020 Civil Code, *supra* note 1, art. 538.

349 *See id*. art. 538.

350 *See id.*

351 *See id.* art. 539.

352 *See id.*

353 *See* SUP. PEOPLE'S CT., *Interpretation of Application of the Contract Law (II),* art. 19, http://www.court.gov.cn/fabu-xiangqing-64.html.

354 *See id*.

considered "unreasonably low."[355] On the other hand, if a transaction price is thirty percent higher than the fair price, the transaction price will be deemed "unreasonably high."[356] For the purpose of price determination, the fair price could be either the guided price or market price.[357]

Article 542 of the Civil Code further provides that when an act of an obligor adversely affecting the creditor's right to the obligee is cancelled, the act shall have no effect *ab initio*.[358] This provision is premised on Article 155 of the Civil Code, which states a general rule that a void or revoked civil act does not have any legal effect from the very beginning.[359] Also, under the Civil Code, the right of cancellation must be exercised within one year of the time when the oblige knows or should have known the cause for cancellation.[360] The maximum period for the exercise of the creditor's right of the obligee is limited to five years from the date on which the act of the obligor takes place.[361]

VI. LIABILITY AND BALANCE OF INTERESTS

Again, on the basis of the Contract Law, the Civil Code not only enhances the regulatory scheme of contracts through codifying the SPC-endorsed practices, but it also strives to balance the rights and obligations of the parties by either revising the existing provisions of the Contract Law or by creating new rules implementing the fruits resulting from the reforms.[362] As far as the contractual relationship is concerned, the Civil Code is intended to build a legal environment in which a contract, once formed, will be maintained and the performance of the contract will be undertaken in the way that helps

355 *Id.*

356 *Id.*

357 *See* SPC CIVIL CODE IMPLEMENTATION LEADING GROUP, *supra* note 159, at 539.

358 *See* 2020 Civil Code, *supra* note 1, art. 542.

359 *See id*. art. 155.

360 *See id*. art. 541.

361 *See id.*

362 *See* Wang Chen, *Explanations on the "Civil Code of the People's Republic of China (Draft)"*, NAT'L PEOPLE'S CONG. OF PEOPLE'S REPUBLIC CHINA (May 22, 2020), http://www.npc.gov.cn/npc/c30834/202005/50c0b507ad32464aba87c2ea65bea00d.shtml.

promote equal exchange, fair competition, and the free flow of commodities and products.[363]

A general notion underscoring the contract provisions of the Civil Code is that a legally formed contract is valid and must be performed unless otherwise excused by agreement of the parties or by operation of law.[364] As noted, contractual performance is considered in China to be the core of the entire system of contracts.[365] While focusing on performance, the Civil Code appears to be more concerned about the balanced rights and obligations of the parties than the Contract Law. Those concerns are clearly discernible in the provisions of the Civil Code pertaining to rescission, breach, and remedies.

A. Rescission

Rescission is a mechanism to dissolve the contractual or creditor-debtor relationship between the parties. Under the Contract Law and the Civil Code, rescission can be made either by agreement of the parties or by provisions of the law, commonly called contractual rescission or statutory rescission. Contractual rescission takes place when the parties agree to bring a contract to an end before the contract is performed or the performance is complete, or in a situation where a certain event provided for in the contract to dissolve the contract occurs.[366]

Statutory rescission is rescission by operation of law. Both the Contract Law and the Civil Code allow a contract to be rescinded in the case of (a) *force majeure* by which the purpose of the contract cannot be realized; (b) anticipatory repudiation by a party; (c) failure of a party to perform the principal obligations of the contract; (d) non-performance or other act of a party in breach of the contract so as to frustrate the purpose of the contract; or (e) other situations as provided by the law.[367] In addition, under the Civil Code, for a contract that requires continuous performance for an indefinite period of time, the parties thereto may rescind the contract at any time.[368]

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363 *See id.*

364 *See* SPC CIVIL CODE IMPLEMENTATION LEADING GROUP, *supra* note 159, at 338–39.

365 *See id*. at 338.

366 *See* 2020 Civil Code, *supra* note 1, art. 562 ("The parties may rescind the contract upon agreement through negotiation. The parties may agree on the causes for rescission of the contract by a party. When a cause as such arises, the party with the right to rescission may rescind the contract.").

367 *See id*. art. 563; 1999 Contract Law, *supra* note 33, art. 94.

368 *See* 2020 Civil Code, *supra* note 1, art. 562.

1. Unilateral Rescission

In many cases, rescission is a unilateral act of one party either due to the occurrence of the stipulated event or by a provision of law. For the purpose of rescission, the Contract Law provided a "Notice Rule" under which rescission will take effect upon receipt of the notice by the other party.[369] If rejected, the party rejecting the rescission may ask a court or arbitration body to determine the effectiveness of the rescission made.[370] The Civil Code adopts the "Notice Rule" but provides the parties with more options than allowed by the Contract Law.

First, the Civil Code adds a cushion to the Notice Rule. Under Article 565 of the Civil Code, the rescission of a contract shall take effect at the time the notice reaches the other party.[371] But, when the notice of rescission states that the contract shall be automatically rescinded if the other party fails to perform his obligation within a specified period of time, the rescission shall become effective when the other party fails to perform upon expiration of the specified period of time.[372] An implication of Article 565 is that the obligor may get another chance to fulfill his operation if the obligee chooses to do so.

Second, the Civil Code gives both of the parties an option to request the People's Court or arbitration body to decide the validity of rescission if disputed.[373] As noted, the Contract Law only allows the party who objects to the rescission to make such a request. The Civil Code expands the coverage of the provision of the Contract Law from one party to either of the parties. Under Article 565 of the Civil Code, where the rescission of the contract is disputed, either party may request the People's Court or an arbitration body to make a determination on the validity of the rescission.[374]

The expansion is rested on the rationale that if a party neglects to make a timely request to the court or arbitration body when disputing the rescission, the effect of the contract will remain unstable and uncertain, and the lawful rights and interests of the person seeking rescission will be damaged. By allowing either party to make the request, the Civil Code intends to balance the rights and interests of

369 *See* 1999 Contract Law, *supra* note 33, art. 96.
370 *See id.*
371 *See* 2020 Civil Code, *supra* note 1, art. 565.
372 *See id.*
373 *See id.*
374 *See id.*

the two parties and to maintain the safety and stability of contractual transactions.

The expansion under Article 565 of the Civil Code is intended to serve a two-fold function: on the one hand, it helps prevent a party from abuse of the right to rescind the contract, and on the other hand, it prevents the other party who protests rescission from purposefully lagging behind to make a request for the determination of the effect of rescission so as to harm the interests of its counterpart.[375] The ultimate goal, once again, is to protect the rights of both parties so that their bargained for interests will be realized.

Third, the Civil Code provides an alternative to the Notice Rule. Pursuant to Article 565 of the Civil Code, where one of the parties requests rescission of the contract without notifying the other party by directly filing a lawsuit or applying for arbitration, and the People's Court or arbitration body grants such request, the contract shall be rescinded when a duplicated copy of the complaint or the application letter for arbitration is served on the other party.[376] Unlike the Contract Law, under Article 565 of the Civil Code, when seeking a rescission, the party may either send a notice to the other party or make a request to the court or arbitration body in order for the rescission to become effective.[377]

2. Post-Rescission Remedies

When a contract is rescinded, the contractual relationship between the parties ends. But an issue arising is the legal effect of part of the contract that has already been performed. In other words, given the possible conveyance of benefits between parties as a result of partial performance, certain remedial measures would have to be taken in order to avoid unjust enrichment or other unfair results. Questions involved include (a) retroactive effect of rescission and (b) compensation after rescission.

Under Article 97 of the Contract Law, after the rescission of a contract, if the contract has not been performed, the performance is terminated.[378] On the other hand, if the contract has been performed, the party concerned may, in accordance with the situation of performance and the nature of the contract, demand a restoration to

375 *See* SPC CIVIL CODE IMPLEMENTATION LEADING GROUP, *supra* note 159, at 656.

376 *See* 2020 Civil Code, *supra* note 1, art. 565.

377 *Id.*

378 1999 Contract Law, *supra* note 33, art. 97.

the original status or take other remedial measures, and the party also has the right to claim compensation.[379] Restoration means restitution. Other remedial measures, according to the SPC, include repair, replacement, reworking, and reduction of price.[380]

The Civil Code amends Article 97 of the Contract Law with two additional provisions. One provision concerns liability for breach and the other provision is about guarantee liability. According to Article 566 of the Civil Code, where a contract is rescinded due to a breach of contract, the party rescinding the contract may request that the breaching party bear the liability for breach unless otherwise agreed by the parties.[381] Article 566 further provides that after the principal contract is rescinded, a guarantor shall still be obligated to secure the debtor's liability unless otherwise provided by the guarantee agreement.[382]

There have been debates among Chinese scholars on whether a liability for breach should be included in the breach-based rescission. One view is that when a contract is rescinded because of breach, liability for that breach should be excluded.[383] A second view holds that liability for breach shall be excluded from the rescission, but if there are any damages associated with the rescission, compensation should be sought.[384] The third view takes the position that the breach-based rescission and liability for breach are not mutually exclusive.[385] The third view has been endorsed by the SPC and has become general practice in the courts. It is the belief of the courts that excluding liability for breach from rescission would result in an imbalance of the rights and obligations of the parties.[386] In recognition of the SPC's view and court practice, the Civil Code provides the non-breaching party seeking rescission with the right to make a claim against the

379 *See id.*

380 *See* SPC CIVIL CODE IMPLEMENTATION LEADING GROUP, *supra* note 159, at 660.

381 *See* 2020 Civil Code, *supra* note 1, art. 566. Also under Article 566, after a contract is rescinded, where the obligations have not yet been performed, the performance shall cease; where the obligations have already been performed, the parties may, taking into account the performance status and the nature of the contract, request restoration to the original status or other remedial measures taken, and have the right to request for compensation for losses. *Id.*

382 *See id.*

383 *See* SPC CIVIL CODE IMPLEMENTATION LEADING GROUP, *supra* note 159, at 662.

384 *See id.*

385 *See id.*

386 *See id.*

breaching party for breach of contract. Thus, if a contract is rescinded on the basis of breach, no matter whether the rescission is made unilaterally or by agreement of the parties, the liability clause shall remain effective unless the parties have agreed otherwise.

Guarantee is a liability auxiliary to the main contract because its purpose is to ensure that the contract will be performed as expected. A general principle provided in the Guarantee Law is that if the principal contract is invalid, the guarantee agreement shall also be invalid unless it stipulates otherwise.[387] This principle, however, is held inapplicable in the situation where the contact is rescinded. A simple reason is that rescinding a contract does not necessarily mean that the contract is invalid.[388] Therefore, either in the statutory rescission or in the agreed rescission, the validity or effectiveness of the guarantee agreement shall not be affected. Put differently, except for a provision to the contrary in the guarantee agreement, the guarantor shall remain liable when the contract is rescinded.

B. Liability for Breach of Contract

It is a settled rule in the Contract Law and the Civil Code that a civil liability arises upon the breach of a contract. A common understanding in China is that any failure to perform the contract without justification constitutes a breach, which includes (a) refusal to perform, (b) inability to perform, (c) delay in performance, and (d) incomplete performance.[389] Under the Contract Law and the Civil Code, a breach may take the form of actual breach or anticipatory repudiation. In either case, liability for breach will be assessed, followed by corresponding remedies.

1. Liability Basis

The ground on which liability for breach of a contract is imposed has long been a contested issue in China. The center of the issue is whether the liability for breach of contract is imputed on a basis of

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387 *See* Daibiao Fa (担保法) [Guarantee Law] (promulgated by Standing Comm. of the Nat'l People's Cong., June 30, 1995, effective Oct. 1, 1995), art. 8 (China), *translated in* http://www.china.org.cn/china/LegislationsForm2001-2010/2011-02/12/content_21908185.htm. The law was repealed on the day the Civil Code took effect. But the principle governing the validity of the guarantee agreement remains effective.

388 *See* SPC CIVIL CODE IMPLEMENTATION LEADING GROUP, *supra* note 159, at 665.

389 *See id.* at 716–17.

fault or non-fault. Fault-based liability means that a breach may not necessarily result in liability unless the breaching party is found at fault. In other words, the liability imposition is contingent upon the presence of fault of the breaching party rather than the fact of breach. The non-fault-based liability focuses on whether there is a proved breach regardless of underlying fault of the party in breach.[390]

According to Article 107 of the Contract Law, where a party fails to perform his contractual obligation or his performance does not conform to the agreement, the party shall bear such liability as continuing to perform, taking remedial measures, or compensating for losses.[391] Article 107 is held by many in China as a non-fault-based liability provision that governs liability imputation in contracts. The Civil Code makes no change to Article 107 of the Contract Law. Under Article 577 of the Civil Code, a party shall bear liability for breach when a failure to perform or a non-conforming performance occurs.[392]

Similar to Article 107 of the Contract Law, Article 577 of the Civil Code does not require a finding of fault on the breaching party in order to impose liability on him.[393] Based on Article 107 of the Contract Law and Article 577 of the Civil Code, non-fault liability forms a general foundation for the liability imputation in contracts. It is believed that in contrast to fault-based liability, the strictness of contractual liability will better help protect the legitimate rights and interests of the parties and more effectively regulate the behavior of the parties.[394] This belief is premised on the notion that liability for breach of contract is essentially transformed from contractual obligations deriving from an agreement between the parties; thus, to impose liability for breach is in fact to fulfill the wishes and bargains of the parties.[395]

While adopting non-fault as the basic rule of liability imputation, the Civil Code, like the Contact Law, also recognizes certain exceptions where the fault of a party is a required element for the liability imposition. For example, under Article 257 of the Contract Law and Article 776 of the Civil Code, in a work contract, a contractor shall promptly notify the ordering party if the contractor finds that the

390 For more discussion on the contractual liability imputation in China, see ZHANG, *supra* note 288, at 347–51.

391 *See* 1999 Contract Law, *supra* note 33, art. 107.

392 *See* 2020 Civil Code, *supra* note 1, art. 577.

393 *Id.*

394 *See* LIMING, *supra* note 153, at 217.

395 *See id.*

drawings or technical requirements provided by the ordering party are unreasonable.[396] But if losses to the contractor are due to indolence in reply by the ordering party, the ordering party shall be liable for making compensation. In this case, the ordering party's fault (failure to timely reply) is required for the imposition of liability.[397]

The obligor's failure to perform is often the obligee's fault. The question then is whether the obligor shall still be held liable for breach in this situation. Based on fairness considerations, the Civil Code imputes liability onto the obligee, rather than the obligor, when the obligee is found at fault. A notable provision to this effect is Article 832 of the Civil Code. Under Article 832, a carrier shall not bear the liability for compensation for any destruction, damage, or loss of the goods occurring in the course of transport, if said destruction, damage, or loss is caused by the negligence of the consignor or the consignee.[398]

2. Anticipatory Repudiation

Borrowed from the common law system, anticipatory repudiation was first provided in the Contract Law.[399] The Civil Code adopts it from the Contract Law with certain textual modification. Under the Civil Code, anticipatory repudiation occurs when a party explicitly expresses or indicates by his actions that he will not perform his contractual obligation before expiration of the time period for performance.[400] In its external form, an anticipatory repudiation may either be expressed by language or implied from conduct.[401] Repudiation must be unequivocal.

There are two options provided in the Contract Law and the Civil Code in case of anticipatory repudiation. One option is to rescind the contract and the other one is to claim breach of contract. Note, however, that in order for a contract to be rescinded, an anticipatory repudiation must involve a principal obligation; whereas in seeking liability for breach of contract, involvement of a principal obligation

396 1999 Contract Law, *supra* note 33, art. 257; 2020 Civil Code, *supra* note 1, art. 776.

397 *See* 1999 Contract Law, *supra* note 33, art. 257; 2020 Civil Code, *supra* note 1, art. 776.

398 *See* 1999 Contract Law, *supra* note 33, art. 257; 2020 Civil Code, *supra* note 1, art. 832.

399 1999 Contract Law, *supra* note 33, art. 94(2).

400 *See* 1999 Contract Law, *supra* note 33, art. 94(2); 2020 Civil Code, *supra* note 1, art. 563(2), 578.

401 2020 Civil Code, *supra* note 1, art. 563(2).

is not a prerequisite.[402] Note also that under the Contract Law, where an anticipatory repudiation by a party occurs, the other party may demand the former to bear liability for breach before the expiry of the time period for performance.[403] When adopting this provision, the Civil Code changes the word "demand" to "request," intending to better reflect the nature of the creditor-debtor relationship.[404]

3. Breaching Party's Right to Terminate the Contract

A well-established rule governing performance under Chinese law is that a legally formed contract is binding and shall be fully performed.[405] Under the Contract Law and the Civil Code, a party who fails to perform or whose performance does not meet the terms of the contract shall bear liability for breach of contract.[406] The breach may involve both monetary and non-monetary obligations. The liability for breach includes continuing performance, taking remedial measures, and making compensation for losses.[407]

According to Article 110 of the Contract Law, if performance involves a non-monetary obligation, continuing performance will not be an option under any of the following circumstances: (a) performance cannot be made in law or in fact; (b) the subject matter of the obligation is unfit for a compulsory performance, or the performance expenses are excessively high; or (c) the creditor fails to request the performance within a reasonable period of time.[408] In these situations, a request for continuing performance on the ground of breach of contract will not be granted.[409]

A loophole of Article 110 of the Contract Law, however, is that although the breaching party may rely on Article 110 to defend against the performance request, the contract still exists unless terminated by

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402 *See* 1999 Contract Law, *supra* note 33, art. 94(2); 2020 Civil Code, *supra* note 1, art. 563(2).

403 S*ee* 1999 Contract Law, *supra* note 33, art. 108.

404 *See* 2020 Civil Code, *supra* note 1, art. 578.

405 *See* SPC CIVIL CODE IMPLEMENTATION LEADING GROUP, *supra* note 159, at 338–39.

406 *See* 1999 Contract Law, *supra* note 33, art. 107; 2020 Civil Code, *supra* note 1, art. 577.

407 *See* 2020 Civil Code, *supra* note 1, art. 577; 1999 Contract Law, *supra* note 33, art. 107.

408 *See* 2020 Civil Code, *supra* note 1, art. 577; 1999 Contract Law, *supra* note 33, art. 110.

409 *See* 1999 Contract Law, *supra* note 33, art. 110.

the other party.[410] The problem is that if the other party does not, or refuses to, terminate the contract, the breaching party would face an awkward situation in which his obligation to perform was discharged by the operation of law on the one hand, and his obligation to perform under the contract stays intact on the other hand (because the contract is, at least literally, still in effect).[411]

To solve this problem and, more importantly, maintain fairness to both of the parties, the Civil Code provides the breaching party with a right to terminate the contract under certain conditions. In accordance with Article 580 of the Civil Code, if one of the exceptions to the continuing performance with regard to non-monetary obligations exists to the extent that the purpose of the contract cannot be achieved, the People's Court or an arbitration institution may, upon request by a party, terminate the contractual relationship of rights and obligations without affecting the liability for the breach of contract.[412]

For the purpose of Article 580 of the Contract Law, "a party" would include both the breaching party and non-breaching party. However, to exercise the Article 580 right to terminate a contract, certain conditions must be met: (a) the performance is non-monetary, (b) continuing performance is excused on any of the statutory grounds, (c) the contract's purpose cannot be realized, (d) the termination must be made by a court or an arbitration body upon request, and (e) the breaching party's liability for breach of contract shall remain.[413]

Proponents of Article 580 argue that under narrowly defined circumstances, allowing the breaching party to terminate the contract would help break the deadlock in the contract performance and achieve substantive justice and fairness.[414] The reason is that if an obligation cannot be performed on the grounds prescribed by the law, to permit a party to sue for termination of the contract would encourage business transactions because by doing so, the contractual relationship will not be left uncertain and unstable.[415]

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410 *See id*.

411 *See* SPC CIVIL CODE IMPLEMENTATION LEADING GROUP, *supra* note 159, at 740–41.

412 *See* 2020 Civil Code, *supra* note 1, art. 580.

413 *See id*.

414 S*ee* LIXIN & YEWEN, *supra* note 158, at 329–30.

415 *See* SPC CIVIL CODE IMPLEMENTATION LEADING GROUP, *supra* note 159, at 740–41.

C. Remedies

As noted, when breach of contract occurs, the non-breaching party may seek continuing performance, remedial measures, or compensation, depending on the nature and scale of the breach.[416] Like specific performance, continuing performance possesses the character of compulsory performance, but the difference is that continuing performance is available no matter whether the legal or monetary remedy is adequate. Remedial measures generally mean the measures taken to help cure the defects in the performance.[417] Compensation means a monetary remedy to offset the damages resulting from the breach.[418]

1. Monetary and Non-Monetary Obligations

Monetary obligations are obligations that are based on the payment of a certain amount of money, while non-monetary obligations refer to any obligations other than the payment of money.[419] Unlike the Contract Law, the Civil Code expands monetary obligations to include rent, interests, or other pecuniary obligations in addition to price and remuneration.[420] In accordance with Article 579 of the Civil Code, where a party fails to pay the price, remuneration, rent, or interests, or fails to perform another pecuniary obligation, the other party may request such payment or performance.[421]

In China, Article 579 is viewed as a provision that makes continuing performance applicable to monetary obligations.[422] It should be noted, however, that the continuing performance for monetary obligations does not have to be specific, as is the case of specific performance given the fungibility of money. In addition, the performance of monetary obligations in general may not be excused on the ground of *force majeure* because it is believed that there is hardly any obstacle to the payment of money that is "unforeseeable,

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416 *See* 1999 Contract Law, *supra* note 33, art. 107.

417 *See id*. art. 112; 2020 Civil Code, *supra* note 1, art. 582 (explaining that the remedial measures include repairing, replacement, reworking, return of the goods, reduction of price or remuneration, etc.).

418 *See* 2020 Civil Code, *supra* note 1, art. 584.

419 *See* SPC CIVIL CODE IMPLEMENTATION LEADING GROUP, *supra* note 159, at 386.

420 2020 Civil Code, *supra* note 1, art. 579.

421 *See id.*

422 *See* SPC CIVIL CODE IMPLEMENTATION LEADING GROUP, *supra* note 159, at 734.

unavoidable, and insurmountable"— the three key elements for the application of *force majeure*.[423]

A non-monetary obligation is a frequent subject for continuing performance.[424] As discussed, a party may request for the other party to continue to perform if the other party fails to perform or the performance does not meet the terms of the contract, with certain exceptions. Different from the Contract Law, the Civil Code contains a provision for substitute performance. Under Article 581 of the Civil Code, if the continuing performance is not available due to the nature of the obligation, the non-breaching party may seek a substitute performance by the third party and ask the breaching party to bear the expenses that incur in this regard.[425]

2. Stipulated Damage and Earnest Money

In China, in order to provide assurance for the performance of a contract, the parties may, by agreement, provide in the contract both stipulated damage and earnest money.[426] The former refers to a negotiated monetary amount paid to the non-breaching party in case of breach of contract, while the latter is an advanced payment representing a certain percentage of the contract price. A notable feature of earnest money is that it may not be used to substitute damages.

The Civil Code revises the earnest money provision of the Contract Law by imposing a ceiling on the amount of earnest money. Article 586 of the Civil Code explicitly provides that the amount of earnest money agreed to by the parties shall not exceed twenty percent of the value of the subject matter of the principal contract, and any excess amount does not have effect as earnest money.[427] In addition, according to Article 586, if the amount of earnest money actually delivered is more or less than the agreed amount, the agreed amount of the earnest money shall be deemed to have been changed.[428]

Under the Contract Law and the Civil Code, where a contract contains stipulated damages and earnest money, if a party breaches the

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423 1999 Contract Law, *supra* note 33, art. 117; 2020 Civil Code, *supra* note 1, art. 180 (defining *Force majeure* as "objective conditions which are unforeseeable, unavoidable, and insurmountable.").

424 *See* LIMING, *supra* note 153, at 231–32.

425 2020 Civil Code, *supra* note 1, art. 581.

426 *Id.* art. 585, 586.

427 *Id.* art. 586.

428 *See id.*

contact, the other party may choose either of them, but not both, as a remedy.[429] As a modification to the Contract Law, the Civil Code further provides that if the earnest money is not sufficient to compensate for the losses caused by one party's breach, the other party may request compensation for the losses in excess of the amount of the earnest money.[430]

With regard to the stipulated damage, the Civil Code follows the Contract Law and provides three basic rules. First, the parties may, by agreement, stipulate a certain amount of damages to be paid according to the circumstance of the breach or agree on a method for calculating the compensation for losses arising from the breach.[431] Second, if the agreed upon damages are lower or excessively higher than the loss caused, the People's Court or an arbitration institution may make an adjustment to the amount upon the request of a party.[432] Third, if a stipulated damage is provided for delayed performance, the breaching party shall continue to perform the contractual obligation after paying the stipulated damages.[433]

3. Compensation

In contracts, once breach occurs, compensation will follow. The purpose of compensation is to restore the party affected to the position it should have been in if the contract was fully performed as agreed upon by the parties. According to Article 584 of the Civil Code, when a contract is breached, the damages to be compensated shall be equivalent to the loss caused by the breach of contract.[434] Damages include the benefits expected to be obtained if the contract had been performed. But it shall not exceed the loss that may be caused by the breach that the breaching party foresees or should have foreseen at the time of formation of the contract.[435]

Article 584 inherits Article 113 of the Contract Law, which set forth a rule of full compensation.[436] Under the full compensation rule, all losses suffered by a party as a result of the other party's breach of

429 *See id.* art. 588; 1999 Contract Law, *supra* note 33, art. 116.
430 *See* 2020 Civil Code, *supra* note 1, art. 588.
431 *See id.* art. 585.
432 *See id.*
433 *See id.*
434 *Id.* art. 584.
435 *See id.*
436 1999 Contract Law, *supra* note 33, art. 113.

contract shall be compensated by the other party.[437] Bound by the rule of full compensation, the breaching party should not only compensate the non-breaching party for actual losses but should also be liable for the expected interests. But the expected interests are subject to the foreseeability requirement.[438]

The Civil Code provides two new rules that govern compensation. The first rule is the liability deduction rule. Under Article 592 of the Civil Code, where a party's breach of contract causes loss to the other party, if the other party's fault contributes to the occurrence of such loss, the amount of compensation may be reduced accordingly.[439] Related to the liability deduction rule is the liability split rule. Premised on Article 120 of the Contract Law, Article 592 of the Civil Code also provides that if both parties are at default, each shall bear corresponding liabilities.[440] Since the liability split rule deals only with the liability in a mutual breach case, it prompts the need for the liability deduction rule that would help allocate the loss fairly.

The second rule is the rule of the obligee's liability for refusal. This is the rule that applies to a situation where the obligee refuses to accept the obligor's performance. Under Article 589 of the Civil Code, when an obligor performs his obligation in accordance with the agreement and the obligee refuses to accept the performance without just cause, the obligor may request the obligee compensate for any additional expenses.[441] Article 589 imposes liability on the obligee and gives the obligor the right to make a request for compensation.[442] The only condition that triggers the application of Article 589 is the obligee's refusal without justification.[443]

In certain cases, however, the obligee does not necessarily refuse to accept the performance but delays in making acceptance when the obligor performs. Under those circumstances, unless the delay makes it impossible to achieve the purpose of the contract, the obligor remains liable for performance. But in order to protect the obligor, Article 589 of the Civil Code provides a safety valve under which the debtor may not only be able to claim additional expenses but also does

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437 *Id.*

438 *See* 2020 Civil Code, *supra* note 1, art. 584; 1999 Contract Law, *supra* note 33, art. 116.

439 *See* 1999 Contract Law, supra note 33, art. 116.

440 *See id*. art. 592.

441 *See id.* art. 589.

442 *Id.*

443 *Id.*

not need to pay interests for the period of delay.[444] The very purpose is to ensure that in case of breach, the interests of either party will not be unfairly impaired.

VII. REMAINING ISSUES

It is commonly held in China that the legislative purpose of contract law under the Civil Code is to promote transaction convenience.[445] Thus, all articles or provisions concerning contracts in the Civil Code are believed to center on encouraging transactions.[446] To that end, the rules that govern contracts are designed to serve such functions as (a) to facilitate the formation of the contractual relationship as effectively as possible, (b) to render the legally formed contract as effective as possible, and (c) to help realize the creditor's right under the contract as fully as possible.[447]

Despite the improvements the Civil Code makes to contract law, there are several issues that remain unsolved and deserve further discussion. Some of the issues touch the very ideologic foundation on which the Civil Code is purposed to stand, and other issues involve the substances of the contract provisions. Given the complexity of the civil and commercial activities, the broad coverage of contract law under the Civil Code requires significant efforts to be made in both legislative and judicial interpretations. Furthermore, implementation and enforcement in the way that would best serve the intended goal of the Civil Code pose great challenges to the judiciary, both as a matter of law and as a matter of practice.

A key issue concerning the ideologic foundation is the legislative theme of the Civil Code. From a legislative standpoint, adoption of the Civil Code is an important measure to promote development of the

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444 *Id.*

445 *See* SPC CIVIL CODE IMPLEMENTATION LEADING GROUP, *supra* note 159, at 4.

446 *See* SUP. PEOPLE'S CT., *Minutes of National Courts' Working Conference on Implementation of the Civil Code* (Mar. 15, 2021), https://m.thepaper.cn/baijiahao_12384274 (stating that if the parties have disputes over whether the contract is established, the People's Court should deal with it in accordance with the law in the spirit of respecting contract freedom and encouraging and promoting transactions. Where the name of the parties, subject matter and quantity of the contract can be determined, the People's Court shall generally consider that the contract is formed, unless otherwise provided by law or agreed upon by the parties).

447 *See* Wang Yi, *Key Issues in the Understanding and Application of the Contract Law in "Civil Code,"* CIV. & COM. L. (Sept. 17, 2020), https://www.civillaw.com.cn/zt/t/?id=37208#.

rule of law and the advancement of state governance.[448] Scholars in China view the Civil Code as a statutory safeguard for the private rights of individuals and a legal mechanism for enhancing the role and status of civil law in state governance.[449] Under Article 1 of the Civil Code, the purpose of the Civil Code is to protect the lawful rights and interests of persons, regulating civil-law relations, maintaining social and economic order, meeting the needs for developing socialism with Chinese characteristics, and carrying forward the core socialist values.[450]

Behind the legislative theme of the Civil Code is a question about state power *vis a vis* private rights. Put differently, the question concerns the very function of the Civil Code in upholding private rights and restricting state power, particularly when state power is abused to the extent that private rights are infringed upon. Historically, China is known as a country where obligations are weighted significantly over rights. In past decades, the development of a market economy and the rebuilding of the legal system under the notion of the rule of law have generated a drive to reverse the order of the rights and obligations and to turn the country from an obligation-based society to a rights-based one.[451] Associated with this drive is an effort to promote a notion that law should function differently pertaining to private rights and government power.

In his speech at the State Council's meeting on anti-corruption in 2014, Chinese premier Li Keqiang addressed a basic rule that is aimed at protecting private rights and preventing the government from being corrupted. According to Li, to govern the County under the rule of law, it is important to "ensure that market entities can do anything not prohibited by the law, while government must not do anything unless authorized by the law."[452] The former refers to the private rights that are within the realm of the civil or private law, while the latter deals with the government power which is part of the public law.

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448 *See* Chen, *supra* note 2.

449 *See* Wang Liming, *Significance of the Civil Code*, 15 PEOPLE'S PROCURATORATES (2020), https://news.sina.com.cn/gov/2020-08-17/doc-iivhuipn9150477.shtml.

450 2020 Civil Code, *supra* note 1, art. 1.

451 For a general discussion of rights versus obligations in China, see Mo Zhang, *The Socialist Legal System with Chinese Characteristics: China's Discourse for the Rule of Law and Bitter Experience*, 24 TEMP. INT'L & COMP. L. J., 1, 55–58 (2010).

452 *See* Li Keqiang, *Speech at the Press Conference with Media in the End of Second Annual Assembly Session of the 12th National People's Congress* (Mar. 13, 2014), http://lianghui.people.com.cn/2014npc/n/2014/0313/c382531-24626203.html.

A well-received notion in the western world is that for individuals, everything not forbidden by the law is permitted, and for government, anything not authorized by law is prohibited.[453] This notion does not imply that the government has no role to play in the matters of private law. On the contrary, the government's power affects individual rights. But the role of government in private law should primarily be "facilitative of horizontal dealings among private parties."[454]As far as contract law is concerned, its function would ideally be centered on providing the means of enforcing whatever bargained-for agreement the competent individual contractors had freely entered into without government interference.[455]

Despite the progress made in the Civil Code toward the development of a rights-based society, the reality in China is that the supremacy of the Communist Party's leadership makes it difficult, if not impossible, to secure private rights, particularly in a case where the Party's interest is considered to be at stake. As is often the case, the protection of private rights and interests is always quite vulnerable to the unleashed party-led government power. Since the Civil Code is labeled as a legislative expression of "the will of the party,"[456] the dominance of the Party in every aspect of the country may significantly undercut the intended goal of the Civil Code to help build a civil society in which the private rights and interests are the center of concern.

The issues involving the substance of the contract provisions in the Civil Code mainly include those that appear ambiguous and those

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453 For example, when addressing the natural liberty, Adam Smith, attempting to maximize individual freedom, explicitly stated: "Every man, as long as he does not violate the laws of justice, is left perfectly free to pursue his own interest his own way, and to bring both his industry and capital into competition with those of any other man." *See* ADAM SMITH, THE WEALTH OF NATIONS, BOOK IV 209 (Univ. of Chicago Press, 1976). Also under John Locke's rule of limited government, "For all the power the Government has, being only for the good of the society, as it ought not to be *Arbitrary* and under Pleasure, so it ought to be exercised by *established and promulgated laws*…" and "The power of the legislative, being derived from the people by a positive voluntary grant and institution, can be no other than what that positive grant conveyed, which being only to make laws, and not to make legislators, the legislative can have no power to transfer their authority of making laws, and place it in other hands." *See* JOHN LOCKE, TWO TREATISES OF GOVERNMENT 360, 363 (Cambridge Univ. Press, 2002).

454 *Id.*

455 *See id.*

456 *See* Zhou Qiang, *Under the Guidance of Xi Jinping Thought on Socialism with Chinese Characteristics for a New Era, Ensure the Correct Implementation of the Civil Code through Fully Exercising the Function of Trials*, "Qiu Shi" (Seeking Truth) (2020), http://www.court.gov.cn/zixun-xiangqing-236451.html.

for which additional provisions are needed. The former is a matter of interpretation, but the latter requires further legislative or judicial action. The interpretation deals with the meanings and scope of particular provisions while the further action concerns the measures taken by way of amendment or implementation to fix the flaws or missing pieces in the existing provisions.

It is important to bear in mind that the interpretation of law in China is divided into legislative interpretation and judicial interpretation. The legislative interpretation of law is the interpretation made by the country's top legislature, namely the National People's Congress and its Standing Committee. Its function is to tell what the law is. By contrast, the judicial interpretation is the one made by the judiciary, mainly the SPC, and the interpretation as such is to explain how the law is to be applied. Since the line between interpretation of law and interpretation of application of law blurs in many cases, the SPC's interpretation often seems to cross the line and to have the effect of legislative interpretation.[457]

As noted, the Civil Code revises quite a number of provisions of the Contract Law and adopts many new provisions in order to improve the regulatory scheme that governs contracts. However, there are a great deal of concepts in the contract provisions that are either ill-defined or uncertain in their contents. A highly notable example is Article 471—it allows a contract to be formed by offer and acceptance or other means.[458] As discussed, since the "other means" is not defined nor specified in the Civil Code, confusion inevitably arises when parties dispute whether an effective offer or acceptance ever exists. A quite debatable issue is whether a contract could be made without an offer and acceptance. Essentially, the issue is how mutual assent could be found absent offer and acceptance.

Another example involves the terms of a contract. Under Article 470 of the Civil Code, a contract shall generally include such terms as: (a) name or designation and domicile of each party; (b) subject matter; (c) quantity; (d) quality; (e) price or remuneration; (f) time period, place, and manner of performance; (g) default liability; and (h) dispute resolution.[459] Article 470 is a replica of Article 12 of the Contract

457 For general discussion of legislative and judiciary interpretations in China, see Mo Zhang, *Pushing the Envelope: Application of Guiding Cases in Chinese Courts and Development of Case Law in China,* 26 WASH. INT'L L.J. 269, 274–82 (2017).

458 *See* 2020 Civil Code, *supra* note 1, art. 471.

459 *Id.* art. 470.

Law.[460] What remains unclear, however, is what would be the required terms without which a contract could be held to have not been formed. Although like the Contract Law, the Civil Code contains certain provisions that help determine or clarify the terms of a contract, it is still questionable under the Civil Code whether a contract can be found to be formed if it only contains some of the terms listed in Article 470.[461]

A third example is the provision of a preliminary agreement. According to Article 495 of the Civil Code, a failure to fulfill the obligation to form a contract under the preliminary agreement will result in a liability for breach of the preliminary agreement.[462] The question then is what liability the breaching party should bear under Article 495. The liability type provided in the Civil Code, as noted, includes continuing performance, remedial measures, and compensation.[463] But in the case of breach of preliminary agreement, it is uncertain whether the continuing performance refers to continuity of contract negotiation or actual conclusion of the contract. If the continuing performance is to mean continuing negotiation, it may not necessarily lead to the formation of contract. Otherwise, the contract would have to be formed no matter how the negotiation goes.

The provisions that require further legislative or judicial action are the provisions in which certain matters are left unprovided. For instance, pursuant to Article 483 of the Civil Code, a contract is formed at the time when an acceptance becomes effective, unless otherwise provided by law or agreed by the parties.[464] The inference of Article 483 is that a contract may not necessarily be formed upon effectiveness of the acceptance. An issue, however, is whether a remedy may be sought when a contract cannot be formed despite a valid acceptance. The Civil Code provides a remedy in a situation where a contract is invalidated or rescinded, including restitution or compensation for damages, but is silent about any remedy that might be available when the formation of a contract fails.

A related question is whether a contract that has been formed but has not yet taken effect may be rescinded. Under Article 502 of the

460 *See id.*

461 According to the SPC, a general practice is that for the sale of goods, a contract would not be formed without the following three terms: (a) name or designation and domicile of each party, (b) subject matter of the contract, and (c) quantity. *See* SPC CIVIL CODE IMPLEMENTATION LEADING GROUP, *supra* note 158, at 56–58.

462 *See* 2020 Civil Code, *supra* note 1, art. 495.

463 *See id*. art. 577.

464 *See id*. art. 483.

Civil Code, if a contract is subject to government approval, the contract, though formed, will not become effective unless and until the approval is obtained.[465] Also, according to Article 502, if a party responsible for submitting an application for approval fails to do so, the party may, upon request by the other party, be held liable for breach of such obligation.[466] Since one of the remedies in a breach of a contractual obligation is to rescind the contract, it becomes questionable whether Article 502 remedies would also include rescission.[467]

In addition, under Article 500 of the Civil Code, during the course of a contract formation, a party shall be held liable for compensation if the party causes loss to the other party in any of the following situations: (a) under the guise of concluding a contract, engaging in consultation with malicious intention; (b) intentionally concealing material facts or providing false information concerning the conclusion of the contract; or (c) committing any other acts contrary to the principle of good faith.[468] Article 500 provides fault liability in the formation of a contract, but what is left unanswered is whether a party may still be held liable for the fault committed in the process of making a contract after the contract is actually formed or takes effect.[469]

Another provision that invites debate is Article 575 of the Civil Code. On the basis of Article 105 of the Contract Law, Article 575 of the Civil Code provides a rule of debt forgiveness.[470] Under Article 105 of the Contract Law, the whole or part of the rights and obligations of a contract would be terminated if the obligee exempts the obligor from the debt obligation wholly or partially.[471] A criticism is that Article 105 failed to address the mutuality in terms of contractual rights and obligations between the parties since it made debt forgiveness a unilateral act of the obligee without considering the obligor's interests.[472]

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465 *See id*. art. 502.

466 *Id.*

467 The remedies for breach of contract under the Civil Code include rescission, restitution, continuing performance, remedial measures, and compensation.

468 *See* 2020 Civil Code, *supra* note 1, art. 500.

469 *Id.*

470 *See id.* art. 575.

471 1999 Contract Law, *supra* note 33, art. 105.

472 *See* SPC CIVIL CODE IMPLEMENTATION LEADING GROUP, *supra* note 159, at 700.

As a response, Article 575 of the Civil Code provides the obligor with a right to refuse to accept exemption while recognizing the rule of debt forgiveness.[473] Under Article 575 of the Civil Code, where an obligee exempts part or all of the obligor's obligations, the obligations shall be terminated in part or in whole, unless the obligor objects within a reasonable period of time.[474] The intended purpose of Article 575 is to ensure that the obligor's right will be duly respected. An underlying concern is that when debt forgiveness is offered by the obligee, the obligor may not be willing to accept it.[475]

However, there is serious doubt about the practical meaningfulness of the change Article 575 of the Civil Code makes to Article 105 of the Contract Law.[476] First, there can hardly be a case where the obligor does not want to accept the debt forgiveness.[477] Second, although Article 575 of the Civil Code turns the debt forgiveness from a unilateral act to a bilateral one, a question remains as to what would be the consequence when the obligee offers to cancel the debt but the obligor rejects.[478] Third, the reasonable period of time during which the obligor's rejection must be made would also need further clarification.[479]

Also, the "green" rule is quite debatable. As noted, the Civil Code intends to make the "green" rule a general principle that governs civil activities, including contracts. A criticism is that the imposition of the "green" rule on civil matters is actually a mess-up of the restriction under the public law (environmental protection law) and the obligations created by the civil law.[480] On the other hand, it is argued that unlike the fairness and good faith rules, the "green" rule applies only to specified areas and thus can hardly become a general principle.[481] In addition, there is a concern that since the provisions in the Civil Code that relate to the "green" rule are basically advisory in nature, it is highly questionable as to how it can be effectively applied, especially from a practical viewpoint.[482]

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473 2020 Civil Code, *supra* note 1, art. 575.

474 *Id.*

475 *See* SPC CIVIL CODE IMPLEMENTATION LEADING GROUP, *supra* note 159, at 703.

476 *See* YANG LIXIN & LI YIWEN, *supra* note 158, at 327.

477 *See id.*

478 *See id.*

479 *See id.*

480 *See* HE JIAN, *supra* note 193, at 113.

481 *See id.*

482 *See id.* at 116–18.

The Civil Code's implementation and enforcement involves several issues. The thorniest issue is perhaps the potential ideological conflict between the party-led government power and individual private rights. As discussed, China is traditionally an obligation-based society in which individual rights are always overshadowed by government power. The Civil Code is intended to change this course with a focus on civil rights. On that ground, the Civil Code is acclaimed among Chinese scholars as a law of rights.[483] But whether civil rights can be respected and protected without government interference remains an open question. The lack of a mechanism to effectively prevent government power from being abused, especially at the local levels, has been, and continues to be, a challenge facing the Chinese legal system.

Another issue concerns the balance that the contract provisions are intended to achieve among rights and obligations of parties. As previously mentioned, there are many new provisions in the Civil Code that are designed to maintain the rights of the obligee and protect the interests of the obligor. The equilibrium between the rights and obligations of the parties to a contract, however, is not always readily attainable because, on one hand, certain provisions are not clearly defined, and, on the other hand, some new rules in favor of the obligor provide only lip service and thus may have little practical significance.[484]

There is also an issue related to the institutional structure of the Chinese judiciary. China does not have, nor does it intend to practice, separation of powers in its government. The judiciary is subject to the People's Congress and ultimately to the leadership of the Communist Party.[485] Within the court system, all trials are under the supervision

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483 *See* Liu Guixiang, *Several Major Issues in the Application of the Civil Code*, 1 PEOPLE'S JUST. (2021), http://www.ebra.org.cn/news/detail/6220_1.html.

484 For example, the provision allowing the obligor to refuse debt exemption offered by the obligee. Another example is compensation in the case of rescission by agreement. The question is whether the expected interest should also be included in the compensation as provided in Article 584, especially when the breach of contract does not constitute a fundamental breach of the contract so as to frustrate the purpose of the contract, but the parties voluntarily cease to perform the contract whereby the contract is rescinded.

485 Under Article 9 of the Organic Law of People's Courts (as amended 2018), the Supreme People's Court is responsible to, and reports on its work to, the National People's Congress and its Standing Committee. Local people's courts are responsible to, and report on their work to, the local people's congresses at corresponding levels and their standing committees. *Organic Law of the People's Courts of the P.R.C.* (2018 Revision), CHINA L. TRANS.,

of the adjudication committee,[486] and individual judges can hardly decide the cases independently, especially the cases considered to have local or national impacts. Therefore, the implementation of the Civil Code very likely is affected by both the state policies and local interests. In addition, since the power of judicial interpretation rests only with the SPC,[487] all other courts may only do as they are told. Thus, given the complex nature of civil and commercial matters, the implementation of the Civil Code may often be hindered by the hysteresis of judicial interpretation.

VIII. CONCLUSION

Enactment of the Civil Code is hailed in China as a milestone in the Country's civil legislation.[488] Although its impact on the development of civil society, which China endeavored to build since the Country adopted the open-door policy in the late 1970s, is yet to be seen,[489] the Civil Code is considered significant not only in regulating civil and commercial matters but also in protecting individuals' rights and interests.[490] With regard to contract law in

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https://www.chinalawtranslate.com/en/organic-law-of-the-peoples-courts-of-the-p-r-c-2018-revision/#_Toc528417340 (last visited Sept. 16, 2021).

486 It is required under the Organic Law of People's Courts that all levels of People's Court establish adjudication committees (art. 36). Consisting of the court president, vice-presidents, and several senior judges, the adjudication committee performs such functions as (1) Summarizing trial work experience; (2) Discussing and deciding upon the application of law in major, difficult or complicated cases; (3) Discussing and deciding whether there should be a retrial on already effective judgments, rulings, and mediation certificates; and (4) Discussing and deciding upon other major issues related to trial work (art. 37). *See id*.

487 It is provided in Article 18 of the Organic Law of People's Courts that the Supreme People's Court may conduct interpretation of specific issues on the application of law in the course of trials. *See id*. art. 18.

488 *See* Qiao Xinsheng, *Civil Code a Milestone in Legal System,* Op Ed, CHINA DAILY (May 27, 2020), https://global.chinadaily.com.cn/a/202005/27/WS5ecda3eda310a8b241158a88.html.

489 *See* Wang Liming, *The Role of Civil Code in Promoting the Modernization of State Governance,* GUANGMIN DAILY (Jan. 16, 2020), http://www.npc.gov.cn/npc/c30834/202001/106b6a0c0d1d4a0588e092ca4f2be674.shtml (explaining that the Civil Code is the basic law of civil society, and the basic law for the protection of private rights in China). For a general discussion about the development of civil society in China, see Jenna Nicholas, *the Development of Civil Society in China*, https://ssir.org/pdf/Jenna_Nicholas_Civil_Society_in_China.pdf.

490 *See* Wang Liming, *Civil Code: Assurance of the Modernization of State Governance,* SINO-FOREIGN JURIS. (2020), http://fzyjs.chinalaw.org.cn/portal/article/index/id/844.html.

particular, the Civil Code reformulates the contract landscape by strengthening the legal framework which further turns the Nation's economic driving force from government planning to contracts.[491]

It is commonly held in China that the Civil Code will have significant impacts on many aspects of the lives of individuals, and also on the Country's political, economic, cultural, and social spheres. More specifically, the Civil Code is expected to help lay a foundation for the building of a rights-based society because a general belief is that the Civil Code is not only about civil rights, but also about the Nation's governance system and state governance capabilities. Many in China even regard the Civil Code as a declaration of civil rights.[492]

But there are many obstacles lying ahead; some are inherent in the existing system of state governance, some are by-products of the traditional orthodoxy, and some are associated with the application of law. It is fair to say that the Civil Code significantly improves the Contract Law and makes contract legislation a vital part of the civil law system under which civil and commercial activities are regulated. It is also true that, although many of the contract provisions have a foreign or international origin, Chinese characteristics remain strong. In addition, there is hope that the NPC, and especially the SPC, will further issue interpretations so that the Civil Code will be implemented and applied as intended both as a matter of law and as a matter of application of law.

491 *See id*. (explaining that the Civil Code grants full freedom to contractual parties, stimulates the vitality and creativity of market entities, and gives full play to the role of market entities in national and social governance).

492 *See* Wang Liming, *Civil Code: Assurance of the Modernization of State Governance, supra* note 490.