generated many hypotheses drawing on different empirical support. This book does not attempt to contribute a new perspective to this debate. Instead, what we can draw from the debate is the importance of context. It is hard to deny the influence of culture and tradition on how contracts operate in a given society and the norms, principles, and rules that govern contractual relationships. At the same time, appreciating the historical, political, and economic contexts of the contemporary regime of contract law in the PRC directs our attention to its multifaceted role in the country's transition to a modern 'socialist market economy' with Chinese characteristics.

[1-3] This introductory chapter aims to provide an overview of the background, basic concepts, and fundamental principles of Chinese contract law. To develop a better understanding of contract law and practice in the PRC today, we start with a brief overview of its historical evolution, particularly the period from 1979 until present. Following on, we explore the sources of Chinese contract law. This book focuses on the general rules contained in the principal legislation, the Contract Law of the PRC ('CL').[5] We then examine the basic definition of a contract and highlight some of its main characteristics. Finally, the last section explicates the fundamental principles of the CL.

1.2 A Brief Historical Overview

[1-4] The legal system in imperial China had a range of philosophical influences including Confucianism, Daoism, and Legalism.[6] Overall, Confucianism dominated much of Chinese legal tradition and legal thinking. Law was seen as inferior to morality, which could make 'possible an order [in society] which would be self-sustaining without outside enforcement or coercion'.[7] As Professor Valerie Hansen puts it, the Confucian 'prejudice against law in favour of ritual and custom … expressed itself in the conviction that gentlemen should fulfil their obligations simply because they were gentlemen'.[8]

[1-5] Scholars have engaged in considerable debate over the existence of 'civil' or 'private' laws that regulated the rights and obligations arising between non-state actors in imperial China. Much of the laws in China's imperial history belonged to the realms of administrative and criminal law. 'Law' as a concept was inherently penal. In this context, a system of civil law governing private transactions was 'comparatively underdeveloped' in imperial China, and moral standards were used to resolve a range of civil affairs between private citizens.[9]

5 Contract Law of the People's Republic of China《中华人民共和国合同法》adopted at the 2nd Session of the Ninth National People's Congress on 15 March 1999, effective 1 October 1999.

6 Albert Chen, *An Introduction to the Legal System of the People's Republic of China* (4th edn, Lexis Nexis 2011) ch 2.

7 Chaibong Hahm, 'Confucianism and the Concept of Liberty' (2006) 4 Asia Europe Journal 477, 481.

8 Valerie Hansen, *Negotiating Daily Life in Traditional China: How Ordinary People Used Contracts 600-1400* (Yale University Press 1995) 5.

9 Junwei Fu, *Modern European and Chinese Contract Law: A Comparative Study of Party Autonomy* (Wolters Kluwer 2011) 12–13.

[1-6] Some scholars have dated the concept and usage of contracts as far back as the Zhou dynasty (1100 to 770BC).[10] Written agreements, which had various terms (such as *hetong, quan, qi, qi yue*), were used by individuals to buy, sell, rent, or borrow goods, animals, land, or money in traditional China.[11] According to Professor Mo Zhang, rules that governed the substance, making, and enforcement of agreements throughout different dynasties shared certain characteristics: these rules were primarily accepted norms emerging from customs or common usage, they were patriarchal in nature and emphasised obligations rather than rights, and the punishment for breach of an agreement tended to be harsh.[12]

[1-7] The above observations are reflected in Professor Hansen's study of contracts during China's medieval period (600 to 1400AD). For example, the very few miscellaneous provisions related to contracts in the Tang Code, the 'legal crown jewel' of the Tang Dynasty (681 to 907AD), 'captured the state's unwillingness to intervene in private transactions'.[13] Moreover, such provisions in the Tang Code (and subsequently in the Song Code) were of a penal nature. The growing use of contracts during the Song Dynasty corresponded with a period of commercial growth. Bureaucrats struggled to collect stamp taxes on contracts during the Song Dynasty as the population sought to avoid such taxes by not registering their contracts,[14] an undertaking which the Mongols (Yuan Dynasty) were much more successful compared to their predecessors.[15]

[1-8] Overall, a set of uniform rules governing contracts did not exist in imperial China.[16] As Professor Albert Chen puts it, 'the jurisprudential distinction between criminal law and civil law did not exist in traditional China, and penal sanctions were sometimes attached to acts which would have been governed by civil law in a modern legal system'.[17]

[1-9] The influence of Western civil law traditions began to take effect in the late Qing dynasty. At the turn of the 20th century, Emperor Guang Xu ordered the reform of China's legal system and commissioned a team to draft a civil code modelled after continental European civil law traditions. The drafting process of the first civil code in China took place between 1908 and 1910. As the Qing Dynasty collapsed shortly after, the draft Civil Code (*Da Qing Min Lü Cao An*) was never enacted. During the Republican era, legislators of the Nanjing Government promulgated the first Civil Code in China on 26 December 1930.

10 Hansen (n 8) 8.

11 ibid, 10.

12 Mo Zhang, *Chinese Contract Law: Theory and Practice* (Brill 2006) 27.

13 Hansen (n 8) 17.

14 ibid, ch 4.

15 ibid, ch 5.

16 Lei Chen and Larry A DiMatteo, 'History of Chinese Contract Law' in Larry A DiMatteo and Lei Chen, *Chinese Contract Law: Civil and Common Law Perspectives* (Cambridge University Press 2017) 3–26.

17 Chen (n 6) 18.

This Code contained several provisions regarding contract law. The German Civil Code had a significant influence on the structure and concepts of this code.[18]

[1-10] Shortly after the Communist Party of China's victory in 1949, a new government under Mao Zedong abolished all existing laws and institutions. A legal framework emerged by the mid-1950s that included the first Constitution of the PRC and various organic laws and institutions influenced by the Soviet legal system. Under a centrally planned economy, the state embarked on a process of mass collectivisation and nationalisation of private enterprises. The Central People's Government Administration Council issued some administrative rules on the use of contracts for carrying out economic planning, such as the Provisional Measures for the Conclusion of Contracts by Official Organs, State-Owned Enterprises and Collectives.[19] At the same time, the Trade Ministry also issued the Decision Concerning the Careful Signing and Strict Fulfilment of Contracts.[20]

[1-11] The drafting of a new civil code in the PRC commenced in 1954 and was completed in 1956. The Soviet model of socialist law substantially influenced this draft code. However, the draft was never promulgated due to the virtual abolition of legal institutions during the Anti-Rightist movement in the late 1950s. Meanwhile, the deteriorating Sino-Soviet relationship gave rise to criticism of Soviet influence on the PRC legal system.

[1-12] There were some attempts at preparing the second draft of the civil code in 1962. The central government issued a small handful of regulations that governed limited forms of contractual activities, such as the Circular Regarding the Strict Implementation of Basic Construction Procedures and Economic Contracts[21] and the Interim Regulation on Basic Provisions in Contracts for Ordering Industrial and Mineral Products.[22] However, from the mid-1960s onwards, all legislative attempts were abandoned as Mao Zedong launched the Cultural Revolution.[23] The ensuing decade of political turmoil witnessed the dismantling of the entire legal system.

[1-13] In 1978, the opening up of the Chinese economy by Deng Xiaoping was a turning point in the development of a modern legal system in the PRC. To address the immediate needs of reforming a centrally planned economy into a 'socialist

18 Xianchu Zhuang, 'The New Round of Civil Law Codification in China' (2016) 1 University of Bologna Law Review 106, 110; Shiyuan Han, 'A Snapshot of Chinese Contract Law from an Historical and Comparative Perspective' in Lei Chen and CH van Rhee (eds) *Towards a Chinese Civil Code: Comparative and Historical Perspectives* (Martinus Nijhoff Publishers 2012) 235–256, 236–237.

19 《机关国营企业、合作社签订合同契约暂行办法》promulgated by the Central People's Government Administration Council Economy and Finance Committee on 3 October 1950.

20 《关于认真订立与严格执行合同的决定》promulgated by the Central People's Government Administration Council Trade Ministry on 3 October 1950.

21 《关于严格执行基本建设程序、严格执行经济合同的通知》promulgated by the State Council on 10 December 1962.

22 《关于工矿产品订货合同基本条款暂行规定》promulgated by the State Economic Commission on 30 August 1963.

23 Jianhua Zhong, and Guanghua Yu, 'China's Uniform Contract Law: Progress and Problems' (1999) 17 UCLA Pacific Basin Law Journal 1, 4.

market economy', the State Administration for Industry and Commerce ('SAIC') was established in 1979 and had the role of overseeing the implementation of economic contracts. The National People's Congress ('NPC') enacted the first major piece of national contract legislation in 1981, the Economic Contract Law ('ECL').[24] The ECL and related regulations governed ten types of domestic contracts, namely sales contracts, construction project contracts, material processing contracts, freight transportation contracts, supply of electricity contracts, warehouse storage contract, leases, loans, property insurance contracts, and scientific cooperation contracts.

[1-14] Shortly after the ECL, the NPC enacted the Foreign Economic Contract Law ('FECL') in 1985, which regulated contracts between Chinese enterprises or economic organisations and foreign entities.[25] The FECL was based on the regulatory experiences gained from the development and implementation of local laws on foreign economic contracts in special economic zones (such as Shenzhen[26]). The Standing Committee of the NPC ('NPCSC') further enacted the Technology Contract Law ('TCL') in 1987 that applied to domestic contracts in technology development, transfer, consulting, and services.[27] When the United Nations Convention on Contracts for the International Sale of Goods ('CISG') came into effect in 1988, China adopted the instrument as its international sales law.[28]

[1-15] Together with related administrative regulations and rules, the ECL, FECL, and TCL formed the three pillars of Chinese contract law before 1999. While they provided a regulatory framework for new and diverse types of private economic activities involving contracts, these laws were primarily seen as instruments for pursuing the state's economic planning and market reform goals.[29] The predominant view of these laws as 'economic law' — as opposed to civil law that governed the rights and obligations of parties to a civil act — was reflected in the exclusion

24 Economic Contract Law of the People's Republic of China 《中华人民共和国经济合同法 [失效] 》adopted at the 4th session of the Fifth National People's Congress on 13 December 1981, effective 1 July 1982 [repealed].

25 Foreign Economic Contract Law of the People's Republic of China 《中华人民共和国涉外经济合同法 [失效] 》 adopted at the 10th session of the Standing Committee of the Sixth National People's Congress on 21 March 1985, effective 1 July 1985 [repealed].

26 Provisions of the Shenzhen Special Economic Zone for Foreign Economic Contracts 《深圳经济特区涉外经济合同规定[失效]》 adopted by the Standing Committee of the Sixth People's Congress of Guangdong Province on 11 January 1984, effective 2 February 1984 [repealed].

27 Law of the People's Republic of China on Technology Contracts, 《中华人民共和国技术合同法 [失效] 》adopted at the 21st session of the Standing Committee of the Sixth National People's Congress on 23 June 1987, effective 1 November 1987 [repealed].

28 China became a signatory to the CISG on 30 September 1981 and ratified the Convention on 11 December 1986.

29 Pittman B Potter, *The Economic Contract Law of China: Legitimation and Contract Autonomy in the PRC* (University of Washington Press 1992); William C Jones, *Basic Principles of Civil Law in China* (ME Sharpe Inc. 1989) 201–202; Chen (n 6) 314–315.

of natural persons from the regulatory scope. The ECL applied only to Chinese domestic contracts between legal persons (enterprises and economic organisations).[30] Legislators amended the scope of the ECL in 1993 to include individual business households and farmers entering into agricultural contracts, but still excluded natural persons who were not merchants.[31] The FECL excluded individual Chinese citizens from being a contracting party to a foreign economic contract.[32]

[1-16] The NPC enacted an important piece of legislation in 1986 to regulate personal and property relations between civil subjects (including natural persons and legal persons): the General Principles of Civil Law of the People's Republic of China ('GPCL').[33] Although the GPCL was not a comprehensive civil code, it set out the basic principles underpinning a range of civil acts, including contractual relationships. The GPCL used the term 'contract' instead of 'economic contract' and contained a small number of general provisions concerning the definition of a contract, contractual performance, liability for breach, and 'gap filler' terms such as the price and quality of goods.[34]

[1-17] As China's transition to a 'socialist market economy with Chinese characteristics' and opening up to international trade and commerce rapidly accelerated in the 1990s, the problems and gaps associated with the fragmented 'three-pillar' contract law regime became evident. The ECL, FECL, and TCL contained numerous overlapping, inconsistent, and conflicting provisions, which created considerable difficulties in their application. At the same time, the three laws did not address some basic contract rules, such as contract formation.

[1-18] At the turn of the 21st century, China faced impending accession to membership of the World Trade Organization ('WTO'). While there is a debate over the extent to which China's entry into WTO spurred legal reform,[35] the introduction of a uniform contract statute in the late 1990s has been perceived as 'part of China's continued efforts to join the WTO'.[36]

[1-19] It was no easy task for the legislators to draft a new contract law that would reflect a greater focus on market principles (such as freedom of contract) while maintaining socialist principles and values of a Chinese communitarian society.[37] In 1993, the NPCSC Legislative Affairs Commission started the drafting process of

30 ECL, Art 2.

31 Feng Chen, 'The New Era of Chinese Contract Law: History, Development and a Comparative Analysis' (2001) 27 Brooklyn Journal of International Law 153, 159.

32 FECL, Art 2.

33 General Principles of Civil Law of the People's Republic of China 《中华人民共和国民法通则》 adopted at the 4th Session of the Standing Committee of the Sixth National People's Congress on 12 April 1986, effective 12 April 1986 revised on 27 August 2009.

34 GPCL, Arts 85 & 88.

35 Clarke, Murrell, and Whiting (n 4) 398.

36 John H Matheson 'Convergence, Culture and Contract Law in China' (2006) 15 Minnesota Journal of International Law 329, 338. See also Feng Chen (n 31).

37 For an excellent discussion of this point in relation to the good faith principle, see: Ewan McKendrick and Qiao Liu, 'Good Faith in Contract Performance in the Chinese and Common Laws', in DiMatteo and Chen, 72–111.

a new uniform contract statute. Several drafts were created in the subsequent years. In 1997, a Consultation Draft was issued. In 1998, the final draft legislation emerged. The NPC passed the CL on 15 March 1999, which came into effect on 1 October 1999. The passage of the new legislation simultaneously repealed the ECL, FECL, and the TCL.[38]

[1-20] The key objectives of the CL are set out in Article 1:

> to protect the lawful rights and interests of contracting parties, to safeguard social and economic order, and to promote socialist modernization.

[1-21] Legislators have not revised the CL since its enactment in 1999. Over the years, there have been discussions among policymakers to develop a new and comprehensive Civil Code. The NPCSC included civil law codification in its five-year legislative plan (2013–2018). The planned code will consist of general provisions, property law, contract law, tort liability, marriage and family law, and inheritance. Legislators plan to complete the codification process by 2020.

[1-22] A major recent development towards the eventuation of a comprehensive Civil Code in the PRC has been the adoption of the General Provisions of the Civil Law of the People's Republic of China on 15 March 2017 ('General Provisions of Civil Law 2017').[39] The GPCL has not been repealed in the meantime. Relevant provisions of the General Provisions of Civil Law 2017 will supersede those of the GPCL where there are discrepancies between the two laws.[40] As the opening chapter of the new Civil Code, the General Provisions of Civil Law 2017 sets out the basic principles and rules governing all civil juristic acts and does not contain any new rules specific to contract law. At the time of writing, it is not clear whether the proposed chapter on contract law under the new Civil Code will amend the substantive rules contained in the CL and related judicial interpretations. In the meantime, the CL remains the principal legislation governing the law of contracts in the PRC.

1.3 Sources and Institutions

[1-23] There are diverse sources of Chinese contract law as well as a hierarchy of institutions involved in lawmaking and administration at different levels. To start with, the Constitution of the PRC is the foundational source of the legal system. The Constitution is not justiciable in courts unless there is a statute giving

38 See CL, Art 428.

39 General Provisions of the Civil Law of the People's Republic of China 《中华人民共和国民法总则》 adopted at the 5th session of the Standing Committee of the Twelfth National People's Congress on 15 March 2017, effective 1 October 2017.

40 Legislation Law of the People's Republic of China 《中华人民共和国立法法》 adopted at the 3rd Session of the Ninth National People's Congress on 15 March 2000, and revised on 15 March 2015, Art 92.

effect to the constitutional rights and rules in question. The current version of the PRC Constitution is the one promulgated in 1982.[41]

[1-24] The legal authority of a statute (*fa lü*) sits at the next layer of the Chinese lawmaking hierarchy below the Constitution. The NPC and NPCSC are the primary legislative organs in the PRC and have the power to enact statutes.[42] This book will focus on the CL as the main contract law statute and to a lesser extent, the General Provisions of Civil Law 2017 (and where relevant, the GPCL). The PRC Legislation Law stipulates that if there is any discrepancy between two laws at the same level, the special provisions such as those of the CL (which specifically regulates contracts) apply over general provisions such as those of the General Provisions of Civil Law 2017 (which governs a range of civil juristic acts).[43]

[1-25] The State Council is the highest executive organ of State power and administration. It has the authority to issue administrative regulations (*xingzheng fagui*) as needed, except for a list of matters reserved only for the lawmaking powers of the NPC and NPCSC.[44] Local people's congresses and their standing committees of provinces, autonomous regions, and municipalities directly under the central government can promulgate local regulations (*difang fagui*) within their jurisdiction.[45] Ministries, commissions, and other organs with administrative powers and functions under the State Council may issue departmental rules (*bumen guizhang*) within their competence.[46] Similarly, local people's governments of provinces, autonomous regions, and municipalities directly under the central government can issue rules (*difang zhengfu guizhang*) in accordance with national laws, administrative regulations, and local regulations.[47] These lower-level sources of legal norms must not contravene the Constitution and the statutes enacted by the NPC and NPCSC.

[1-26] It has been observed that statutes, administrative regulations, and local regulations are generally enforced by courts, but the departmental rules issued by State Council ministries and local government rules that have lower normative status tend to be more problematic when it comes to judicial enforcement.[48] The hierarchy of legal norms is important in relation to certain aspects of the CL. As we will examine in Chapter 3, the rule on 'violation of mandatory provisions of any law or administrative regulations' that renders a contract void under Article 52(1) of the CL refers to the statutes adopted by the NPC or NPCSC and the administrative regulations issued by the State Council.

[1-27] Because there are often gaps and ambiguities in regulatory instruments, a further source of legal norms comes from interpretations of such instruments by various authorities. Only the NPCSC has the power to provide interpretations

41 Constitution of the People's Republic of China 《中华人民共和国宪法》 adopted at the 5th Session of the Fifth National People's Congress and promulgated on 4 December 1982.
42 ibid, Art 58.
43 Legislation Law of the PRC, Art 92.
44 ibid, Art 9.
45 ibid, Art 72.
46 ibid, Art 80.
47 ibid, Art 82.
48 Clarke, Murrell, and Whiting (n 4) 394.

or enact decrees on the provisions of the Constitution and statutes that need to be further clarified or supplemented.[49] Such interpretations are referred to as 'legislative interpretation' (*lifa jieshi*). Standing committees of local people's congresses can also provide interpretations of local regulations that they (or the local people's congress) have enacted.[50] There are also administrative interpretations (*xingzheng jieshi*) issued by the State Council and its ministries.[51] Local governments may interpret points of law arising from the concrete application of local regulations and rules.[52]

[1-28] The bulk of interpretative materials come from the Supreme People's Court ('SPC') and the Supreme People's Procuratorate (SPP) in the form of judicial interpretations (*sifa jieshi*) on specific application of laws in the adjudicative work of the people's courts or procuratorial work. These interpretations generally pertain to specific legal provisions and must 'conform to the objectives, principles, and original meaning of the legislation'.[53] Under the SPC's Provisions on Judicial Interpretation Work, judicial interpretations (issued by the Adjudication Committee of the SPC) have the force of law and should be cited in all court judgments where relevant.[54]

[1-29] The SPC has released two judicial interpretations in 1999 and 2009 concerning the application of specific provisions in the CL, which we will refer to throughout the book as 'SPC Interpretation I'[55] and 'SPC Interpretation II'.[56] These two SPC interpretations are important authoritative references for lower courts to date.

49 PRC Constitution, Art 67; Legislation Law of the PRC, Arts 45, 50.
50 Decision on Strengthening Legal Interpretation by the Standing Committee of the NPC,《全国人民代表大会常务委员会关于加强法律解释工作的决议》 adopted by the 19th meeting of the Standing Committee of the Fifth National People's Congress on 10 June 1981, Art 4.
51 State Council Circular Concerning Powers and Procedures for the Interpretation of Administrative Regulations, 《国务院办公厅关于行政法规解释权限和程序问题的通知》 issued by the General Office of the State Council on 3 March 1993; Regulations on Procedures for the Formulation of Administrative Regulations, 《行政法规制定程序条例》 promulgated by Decree No. 321 of the State Council on 16 November 2001, revised on 22 December 2017, Ch VI.
52 Chen (n 6) 155.
53 Legislation Law of the PRC, Art 104.
54 Provisions of the Supreme People's Court on the Judicial Interpretation Work, 《最高人民法院关于司法解释工作的规定》 No.12 [2007] adopted at the 1408th meeting of the Adjudication Committee of the SPC on 9 March 2007 and entered into force on 1 April 2007, Arts 4, 5, 27.
55 Interpretation I of the Supreme People's Court of Several Issues concerning the Application of the Contract Law of the People's Republic of China, 《最高人民法院关于适用 ＜中华人民共和国合同法＞ 若干问题的解释（一）》 Judicial Interpretation No. 19 [1999] adopted at the 1090th meeting of the Adjudication Committee of the SPC on 1 December 1999 and entered into force on 29 December 1999.
56 Interpretation II of the Supreme People's Court of Several Issues concerning the Application of the Contract Law of the People's Republic of China, 《最高人民法院关于适用 ＜中华人民共和国合同法＞ 若干问题的解释（二）》 Judicial Interpretation No. 5 [2009] adopted at the 1462nd meeting of the Adjudication Committee of the SPC on 9 February 2009 and entered into force on 13 May 2009.

[1-30] Court decisions are not formally recognised as a direct source of lawmaking within the Chinese legal system. Specific judgments do not have the same binding or authoritative effect as case law in common law jurisdictions. Nevertheless, the SPC has developed a system of 'guiding cases' since 2010, which in principle provides some form of *de facto* authority for local people's courts.[57] Decisions published in the SPC's Gazette are also considered persuasive for lower courts, although not as authoritative as guiding cases— since courts at various levels should 'refer to' relevant guiding cases when deciding similar cases.[58]

[1-31] The selected published judicial decisions mentioned in this book serve to illustrate the 'on the ground' application of key concepts, principles, and rules of Chinese contract law in disputes brought before the courts. As observed by a prominent Chinese law scholar, a study of individual cases and judicial decisions can be useful in understanding how Chinese courts apply the 'published norms' of the law found in the statutes and regulations promulgated by legislative and administrative institutions.[59]

[1-32] In recent years, there have been significant advances in the online publication of court decisions at various levels in China as part of reforms to enhance the transparency of the judicial system. Since 2014, the SPC has required all people's courts to publish effective judgments and related documents (such as rulings, payment orders, notices on dismissal of petitions, among others) on the platform of 'China Judgements Online'.[60] Certain categories of judicial documents are exempted from this requirement, such as documents related to cases involving state secrets, juvenile delinquency, divorce proceedings involving child custody, cases settled by mediation, and cases deemed unsuitable for online publication at the court's discretion.[61] If the court decides not to publish a judgment online, it must still publish the case number, court, judgment date, and reasons for non-disclosure (except where disclosure may divulge state secrets).[62] At the time of writing, the website contained around 45 million judgments and judicial documents.[63]

57 Local people's courts at various levels include Higher People's Courts, Intermediate People's Courts, and Basic People's Courts.

58 Provisions of the Supreme People's Court Concerning Work on Case Guidance, 《最高人民法院关于案例指导工作的规定》 No. 51 [2010] adopted at the 1501st meeting of the Adjudication Committee of the SPC on 15 November 2010, issued and entered into force on 26 November 2010, Art 7.

59 Nicholas Calcina Howson, 'Corporate Law in the Shanghai People's Courts, 1992–2008: Judicial Autonomy in a Contemporary Authoritarian State' (2010) 5 East Asia Law Review 303.

60 Provisions of the Supreme People's Court on the Issuance of Judgments on the Internet by the People's Courts (2016 Revision)《最高人民法院关于人民法院在互联网公布裁判文书的规定(2016修订)》 Judicial Interpretation No. 19 [2016] adopted at the 1689th meeting of the Adjudication Committee of the SPC on 25 July 2016, issued and entered into force on 1 October 2016, Arts 2 & 3.

61 ibid, Art 4.

62 ibid, Art 6.

63 China Judgements Online, 中国裁判文书网 http://wenshu.court.gov.cn/Index (accessed 29 April 2018).

[1-33] Chinese courts are not the only institutions where parties may attempt to resolve their contractual disputes. Article 128 of the CL allows parties to pursue other means of dispute resolution:

> The parties may seek to resolve a contractual dispute through settlement or mediation. If the parties do not wish, or are unable to, resolve such dispute through settlement or mediation, they may submit the dispute to an arbitration institution in accordance with their arbitration agreement. Parties to a foreign-related contract may apply to a Chinese arbitration institution or another arbitration institution. If the parties did not conclude an arbitration agreement or the agreement is invalid, either party can bring a lawsuit before the People's court. Parties must perform the judgments, arbitral awards or mediation agreements that have taken legal effect; if a party refuses to perform, the other party may request the People's Court for enforcement.

[1-34] Under Article 126 of the CL, parties to a foreign-related contract may choose the applicable law for dispute resolution, unless stipulated otherwise by law. If the parties fail to make such a choice, the law of the jurisdiction with the closest connection to the contract shall apply. It is beyond the scope of this book to examine the rules governing dispute resolution procedures and institutions.[64] Nevertheless, it is worth mentioning the rapid expansion of Chinese arbitration institutions with escalating caseloads of domestic and foreign-related contractual disputes in recent years.[65] Another notable trend has been the increasing judicial enforcement of arbitral awards, especially foreign arbitral awards.[66] The SPC has recently published two judicial interpretations that seek to enhance the consistency and transparency of judicial review of domestic and foreign-related arbitration cases.[67] China's burgeoning experience with international arbitration,

64 For example, the basic legislative framework for arbitration is the Arbitration Law of the People's Republic of China (2017 Revision)《中华人民共和国仲裁法 (2017修正)》adopted at the 9th Session of the Standing Committee of the Eighth National People's Congress on 31 August 1994, revised on 27 August 2009 and 1 September 2017. Additional rules are contained in the Civil Procedure Law of the People's Republic of China (2017 Revision) 《中华人民共和国民事诉讼法(2017修正) 》 adopted at the 4th Session of the Seventh National People's Congress on 9 April 1991, revised on 28 October 2007, 31 August 2012, and 27 June 2017.

65 These institutions include the well-established China International Economic and Trade Arbitration Commission (CIETAC), Shanghai and Shenzhen International Economic and Trade Arbitration Commissions, China Maritime Arbitration Commission, Beijing Arbitration Commission, and numerous local arbitration commissions.

66 Meg Utterback, Ronghui Li, and Holly Blackwell, 'Enforcing foreign arbitral awards in China – a review of the past twenty years', King and Wood Mallesons, 15 September 2016, http://www.kwm.com/en/uk/knowledge/insights/enforcing-foreign-arbitral-awards-in-china-20160915 (accessed 30 April 2018).

67 Relevant Provisions of the Supreme People's Court on Issues concerning Applications for Verification of Arbitration Cases under Judicial Review 《最高人民法院关于仲裁司法审查案件报核问题的有关规定》adopted at the 1727th meeting of the Adjudication Committee of the SPC on 20 November 2017 and entered into force on 1 January 2018; Provisions of the Supreme People's Court on Several Issues concerning Deciding Cases of Arbitration-Related Judicial Review《最高人民法院关于审理仲裁司法审查案件若干问题的规定》adopted at the 1728th meeting of the Adjudication Committee of the SPC on 4 December 2017 and entered into force on 1 January 2018.

the outset (*void ab initio*).[2] Regarding a voidable contract, a party must request the court or arbitration institution to revoke or alter the said contract. Upon its revocation, a voidable contract shall have no legally binding effect *ab initio*.[3] For a contract of pending validity, its legal effect upon formation cannot be ascertained until subsequent actions have been taken, such as ratification (*zhuiren*) of the contract by a person with appropriate capacity or authority.

[3-5] As we examined earlier in Chapter 1, the CL reflected a shift in the values and fundamental principles underpinning the contract law framework in China's 'socialist market economy'. A greater emphasis on the contractual freedom and autonomy of the parties can be seen in the rules governing the validity of contracts. Compared to its predecessors and the GPCL, the CL has significantly curtailed the possibility for judicial and administrative intervention in rendering contracts void. For example, by expanding the scope of voidable contracts, the CL allows the aggrieved party to decide whether a contract with certain defects affecting its validity should remain on foot or be revoked or altered. Other rules, such as those concerning contracts of pending validity, offer the parties an opportunity to remedy the defect through subsequent ratification. In contrast, the previous contract laws and the GPCL treated many types of contracts as void per se.[4]

[3-6] Professor Wang Liming has criticised the judicial practice under the pre-CL regime where rules that deemed many contracts void provided the courts with much discretion to expand 'the range of void contracts inappropriately'.[5] In his view, the excessive declaration of void contracts by the courts resulted in unnecessary wastage of expenses and resources, undermined the 'preservation of and respect for the will and interests of the parties' and did not facilitate transactions.[6] Wang and Xu argue that the CL has rectified this major weakness of its predecessors— embodying the principle of fostering transactions between different entities and individuals.[7]

[3-7] The General Provisions of Civil Law 2017 has adopted a relatively similar approach to that of the CL and only a few types of civil juristic acts are

2 CL, Art 56.
3 ibid.
4 Article 58 of the GPCL listed seven kinds of void contracts: (1) those performed by a person without capacity for civil conduct; (2) those that according to law may not be independently performed by a person with limited capacity for civil conduct; (3) those performed by a person against his true intentions as a result of fraud, coercion or exploitation of his unfavourable position by the other party; (4) those performed through malicious collusion that are detrimental to the interest of the State, a collective, or a third party; (5) those that violate the law or the public interest; (6) economic contracts that violate the State's mandatory plans; and (7) those performed under the guise of legitimate acts that actually conceal illegitimate purposes.
5 Liming Wang, 'An Inquiry into Several Difficult Problems in Enacting China's Uniform Contract Law' (1999) 8 Pacific Rim Law and Policy Journal 351.
6 ibid, 370–371.
7 Liming Wang and Chuanxi Xu, 'Fundamental Principles of China's Contract Law' (1999) 13 Columbia Journal of Asian Law 1, 23–29.

regarded as invalid.[8] In relation to a wider range of civil acts with defects in their validity, 'persons of civil conduct' have the right to request the court or arbitration institution to revoke the act in question.[9] These rules under the General Provisions of Civil Law 2017 have replaced the corresponding rules under the GPCL.

3.2 Contracts of Pending Validity

[3-8] The legal effect of such contracts is not determined at the time of their formation, but requires further actions to be taken before their validity can be confirmed. Various scholars have referred to this type of contact as an 'effect-to-be-determined contract',[10] a 'contract of undetermined effect',[11] or a contract with legal effect 'in suspense'.[12] Usually, for such a contract to be effective, a person with the appropriate capacity, authority or right to conclude the contract shall affirm or ratify the contract. The contract becomes valid *ab initio* when ratification is given. On the other hand, the contract is void *ab initio* if affirmation or ratification is refused.[13] In situations where the legal effect of a contract is pending further determination, it is important to have a clear set of rules that can reduce the risk of uncertainty for all parties concerned.

[3-9] There is debate among scholars regarding the doctrinal basis of this category of contracts and its distinction vis-à-vis void and voidable contracts. One argument is that a contract of pending validity does not concern the concluded contract itself (or as Professor Mo Zhang puts it, 'the contract itself is good'[14]) but merely a defect in a contracting party's capacity. Based on this presumption, a contract of pending validity is treated by the CL as 'a particular type of contract' subject to special provisions such as ratification by that party's legal agent.[15] An opposing view is that if a person has limited capacity, the contract cannot be concluded without the affirmation of the person's legal agent. As such, the issue of capacity directly affects the formation of the contract.[16] One may find some support for this view when examining the relevant provision regarding the parties' civil capacity in Article 9 of the CL, which is placed under the heading 'Formation/Conclusion of Contracts'.

8 See General Provisions of Civil Law 2017, Arts 144, 153, and 154 concerning incapacity, violation of mandatory legal provisions and public order, malicious collusion that damage the legitimate interests of others.
9 ibid, Arts 147–151 concerning misunderstanding, fraud, fraud by third parties, coercion, and unfairness.
10 Zhang, 155.
11 Ling, 213.
12 Yi Wang, 'Prospect of Validity in Chinese Contract Law' in Chen and DiMatteo, 215–238, 228.
13 Ling, 213.
14 Zhang, 155.
15 Liming Wang (n 7) 27–28.
16 Xun Xiao, Yaorong Wei and Shuna Zheng, *Interpretation of the Contract Law of the PRC: Pandect* 《中国人民共和国合同法释论(总则)》(China Legal System Press 1999) 185.

[3-10] Various types of contracts could fall into this category, such as a contract made by a party with limited civil capacity, a contract concluded on behalf of a principal by a person without the requisite power of agency, and a contract involving the unauthorised disposition of another person's property. These types of contracts will be examined in this section, along with contracts that are subject to approval and registration formalities and contracts with conditions that affect their validity.

3.2.1 Where a contracting party has limited civil capacity

3.2.1.1 Categories of capacity for civil conduct

[3-11] Article 9 of the CL stipulates that 'the parties shall have the appropriate capacity for civil rights and capacity for civil activities'. As mentioned earlier, this is also a condition for a valid civil act under the General Provisions of Civil Law 2017. The capacity of a natural person to undertake civil acts is categorised under the General Provisions of Civil Law 2017 as: (1) full capacity, (2) limited capacity, and (3) no capacity. [17]

[3-12] An adult ('a natural person aged 18 or over') has full capacity for civil conduct and is entitled to perform civil acts independently. A minor aged between 16 and 18 years old whose main source of income is his or her job is also deemed a person of full capacity for civil conduct.[18] Specific types of civil acts, such as marriage, may have a different minimum age requirement.[19]

[3-13] 'Limited capacity' specifically applies to two categories of natural persons under the General Provisions of Civil Law 2017: (1) a minor aged between 8 and 18 years old, and (2) an adult who is unable to account for his own conduct *fully*.[20] A person with limited capacity shall be represented in the performance of civil acts by his or her legal agent (statutory guardian).[21] In the case of a minor who has limited capacity, he or she can also obtain the consent of the agent in the performance of civil acts.[22] As we examine below, persons with limited capacity may enter into two types of contracts independently. Other types of contracts will require the legal agent's ratification to be effective.

[3-14] A minor under the age of 8 is deemed to have no capacity for undertaking civil acts.[23] An adult who is unable to account for his or her conduct is also

17 General Provisions of Civil Law 2017, Arts 18, 19, 20, 21.
18 ibid, Art 18.
19 Article 6 of the PRC Marriage Law stipulates the minimum age for marriage for men and women are 22 years old and 20 years old respectively: Marriage Law of the People's Republic of China 《中华人民共和国婚姻法》 adopted at the Third Session of the Fifth National People's Congress on 10 September 1980, effective 1 January 1981, and revised on 28 April 2001.
20 General Provisions of Civil Law 2017, Art 13.
21 ibid, Arts 18 and 22.
22 ibid, Art 19.
23 ibid, Art 20.

considered as lacking the capacity for civil acts.[24] Both groups of natural persons shall be represented by their legal agent in carrying out all types of civil acts. Furthermore, the SPC (with reference to the GPCL) has indicated that the civil acts of a person who suffers from intermittent mental illness shall be deemed void if such acts were performed while the party was mentally ill.[25]

[3-15] The General Provisions of Civil Law 2017 regards a civil act performed by persons without capacity for civil conduct as void.[26] Although the CL does not explicitly state the legal effect of a contract concluded by a person without civil capacity, this general rule regarding civil acts would also apply to contracts.

3.2.1.2 Beneficial contracts and contracts appropriate to age, intelligence, and mental health

[3-16] Under Article 47 of the CL, persons with limited civil capacity may conclude two types of contracts that would be deemed effective without requiring ratification by their legal agent: (1) contracts that are purely for their benefit; and (2) contracts that are appropriate in regard to their age, intelligence, and mental health. Article 145 of the General Provisions of Civil Law 2017 also provides the same rule for such types of civil acts.

[3-17] A contract entered into by a person purely for his or her benefit is one that confers only the enjoyment of benefits (such as receiving rewards, donations or payments) and does not impose any responsibility or liability upon him or her. Under the CL, persons with limited civil capacity may independently enter into legally binding contracts of a 'purely profit-making' nature without requiring subsequent ratification by their legal agent. The SPC has emphasised the importance of this rule (with reference to the GPCL) by stating that the lack of or limited capacity of a person accepting reward, donation, or remuneration shall not be used as a basis for claiming that his or her acceptance is invalid.[27]

[3-18] In determining the 'appropriateness' of the civil act in regard to the age, intelligence, and mental health of the person, the SPC (with reference to the GPCL) has further noted numerous factors to be taken into account:

- the extent to which the civil act relates to the person's own daily life;
- whether the person's intelligence (or the mental health condition of a person with mental illness) is adequate for him or her to understand such activity and foresee the consequences of his or her activity; and
- the amount of money involved in relation to the act.[28]

24 ibid, Art 21.
25 Opinion (For Trial Use) of the Supreme People's Court on Questions Concerning the Implementation of the General Principles of Civil Law of the People's Republic of China, 《关于贯彻执行<中华人民共和国民法通则>若干问题的意见（试行）》 adopted by the Adjudication Committee of the SPC on 26 January 1988 ('SPC Opinion on the GPCL') Art 67.
26 General Provisions of Civil Law 2017, Art 144.
27 SPC Opinion on the GPCL, Art 3.
28 ibid, ss 3 & 4.

[3-19] Some examples of contractual activities that would be considered appropriate to the age of a minor include buying a bus ticket or purchasing school books and stationery. Such actions relate to the minor's day-to-day life and importantly, do not involve 'special knowledge, sophisticated understanding or valuables'.[29]

[3-20] In determining the mental condition or status of a person, the SPC has sought to distinguish someone who is unable to understand and someone who is unable to *fully* understand and foresee the nature and consequences of his or her conduct. The former cannot make judgments for his or her self-protection and understand the consequences of his or her conduct. On the other hand, the latter (someone who is unable to *fully* understand) 'does not have the capacity to make judgments as to relatively complicated matters or relatively important acts to protect himself or herself and to foresee the consequences of his or her acts'.[30] The former is deemed lacking civil capacity, and the latter is considered to have limited capacity.

3.2.1.3 Ratification by the legal agent

[3-21] Besides beneficial contracts and contracts appropriate to the person's age, intelligence, and mental health condition, any other contract concluded by a party with limited capacity for civil acts can only become effective after ratification by the person's legal agent. As Professor Zhang explains, the concept of ratification in Chinese law is 'a civil conduct of agent *ad litem* as authorised by law to protect the legitimate interest of those who have limited civil capacity and it is rested with the agent *ad litem*'.[31] In other words, the legal agent is engaged in a civil act when he or she ratifies the contract that the person with limited civil capacity has entered into with another party.

[3-22] Under Article 47 of CL, the counterparty to the contract may request the legal agent of the person with limited capacity to provide ratification within one month (of the request). A lack of response from the legal agent in relation to the request shall be regarded as a refusal of ratification. Before the legal agent's ratification, a bona fide counterparty (who has acted in good faith) has the right to rescind the contract, and such rescission shall be made by giving notice. The SPC has clarified that the legal agent's ratification is effective upon it reaching the counterparty. Upon effective ratification, the contract is deemed effective at the point of its formation.[32]

[3-23] Article 145 of the General Provisions of Civil Law 2017 also stipulates a similar rule regarding time limits on the ratification of civil acts. It also clarifies that the counterparty may request the legal agent to confirm the relevant civil act within one month of the date the legal agent receives such a request. The CL and General Provisions of Civil Law 2017 do not have any explicit rules on the time limit in which the counterparty may request the agent's ratification. Overall, the

29 Zhang, 158.
30 SPC Opinion on the GPCL, Art 5.
31 Zhang, 157.
32 SPC Interpretation II, Art 11.

relevant rules regarding ratification appear to balance the protection of the person with limited capacity and the bona fide counterparty's interest in knowing where he or she stands in relation to the transaction in question.[33]

3.2.2 Contract made by a person without authorisation

3.2.2.1 Unauthorised agency

[3-24] Chinese civil law allows an agent to carry out a range of civil acts, such as entering into a contract, in the name of its principal. For the act to bind the principal, the agent must possess the requisite authorisation from the principal when carrying out the act.[34]

[3-25] Under Article 48 of the CL, a contract concluded in the principal's name by a person without the power of agency, who oversteps their power of agency, or whose power of agency has lapsed, shall not be legally binding on the principal without the principal's ratification. Article 48 does not render such a contract void, but imposes liability on the person who has concluded the contract without being duly authorised to do so. The contract does not bind the principal until he or she ratifies it. Hence, the contract is categorised as a contract with pending validity.

[3-26] Article 171 of the General Provisions of Civil Law 2017 contains parallel rules on unauthorised agency. It has an important addition, which concerns the counterparty's actual or imputed knowledge of the unauthorised agency. According to Article 171, if the counterparty knows or should have known that the person carrying out the civil act has no authority of agency, the counterparty and the unauthorised person carrying out the civil act shall assume liability according to their respective fault.

3.2.2.2 Ratification by the principal

[3-27] The ratification rules under Article 48 of the CL that apply to this type of contract are similar to those under Article 47. The counterparty may request the principal to ratify the contract within one month. If the principal does not respond to such a request within one month, its non-response shall be treated as its refusal to ratify the contract. A bona fide counterparty has the right to rescind the contract by giving notice before the contract is ratified. The SPC has further recognised that if the principal has already started performing its contractual obligations, the principal shall be deemed to have ratified the contract.[35]

[3-28] If the principal refuses to ratify the contract, the contract has no binding effect on the principal. Unlike a contract concluded by a person with limited

33 Mindy Chen-Wishart, 'Invalidity in Chinese and English Contract Law' in Chen and DiMatteo, 239–278, 254.
34 General Provisions of Civil Law 2017, Art 162.
35 SPC Interpretation II, Art 12.

civil capacity, an unratified contract concluded without the authorisation of the principal means that the agent directly assumes liability for the contract.[36]

[3-29] Article 171 of the General Provisions of Civil Law 2017 further specifies that if the principal refuses to ratify the act in question, a bona fide counterparty is entitled to request the (unauthorised) agent to perform the obligations in question or to compensate any injury the counterparty has suffered. However, the scope of such compensation shall not exceed the interest that the counterparty could have obtained if the principal had ratified the act.

3.2.2.3 Apparent agency or authority

[3-30] Article 49 of the CL addresses the situation of apparent agency or authority (*biaojian daili*). This is where a person without due authorisation (has no right of agency, overstepped their right of agency, or their right of agency has lapsed) has concluded the contract in the name of the principal, but the bona fide counterparty has reason to believe that the agent is duly authorised. Article 49 deems the act of agency in this situation as effective. In other words, the contract will bind the principal notwithstanding the agent's unauthorised act. Article 172 of the General Provisions of Civil Law 2017 has a similar rule pertaining to general civil acts.

[3-31] Professor Zhang has noted three common circumstances of apparent agency in cases brought before the courts:

(1) The principal's conduct created an impression that its agent was duly authorised to act on its behalf. For example, where the principal knew of the agent's conduct but did nothing to repudiate such conduct.
(2) The principal failed to notify the counterparty of a change in the scope of authority granted to the agent. As such, the counterparty believed that the agent still possessed the original scope of authority.
(3) The agent's authorisation had been terminated or expired, but the principal did not take steps to execute the termination (such as recalling or cancelling authorisation documents) or make it publicly known that the authorisation no longer existed.[37]

[3-32] If the principal assumes liability under Article 49 of the CL, the principal is entitled to recover losses from the agent.[38] The General Provisions of Civil Law 2017 also imposes civil liability on the agent if he or she fails to perform his or her duties and causes damage to the principal.[39]

[3-33] In a guiding opinion issued in 2009, the SPC stated that courts should adopt a strict application of Article 49 of the CL to cases involving major infrastructure projects, subcontracting and subleasing contracts in the context of the global financial crisis. The SPC noted that many of these contracts had

36 CL, Art 48.
37 Zhang, 159–160.
38 SPC Interpretation II, Art 13.
39 See General Provisions of Civil Law 2017, Art 164.

been concluded in the names of departments of entities, project managers, and individuals.[40]

[3-34] In the same opinion, the SPC also expounded two aspects of Article 49. First, the agent's behaviour must objectively create an impression that he or she is duly authorised. Second, the counterparty, in good faith and without fault, subjectively believed that the agent has the requisite authorisation. The counterparty bears the burden of proof to establish both elements if it seeks to rely on apparent agency to claim that the agent's act was effective.[41] In other words, the SPC's opinion suggests that the counterparty must prove the existence of objective facts that would give rise to a reasonable belief of the apparent agency as well as demonstrate that it acted in a bona fide manner based on that belief.

[3-35] In deciding whether the counterparty has acted in good faith and without fault on its part, the SPC further indicated that courts should consider various factors relating to the conclusion and performance of the contract to ascertain whether the counterparty has fulfilled a 'duty of reasonable care'. Specifically, courts should take into account:

- the time of the contract's conclusion,
- the name in which the contract is signed,
- whether the relevant seal is affixed to the contract and the authenticity of the seal,
- the manner and place of delivery of the subject matter,
- the materials purchased and equipment leased,
- the use of any loans, and
- whether the construction entity is aware of the project manager's behaviour or participates in the performance of contract.[42]

3.2.2.4 Representative of a legal person overstepping his/her authorisation

[3-36] In its reasons for believing that the principal has duly authorised the agent, a bona fide counterparty may rely on the existence of a particular relationship between the principal and agent. One such example is the relationship between a legal person (such as a company)[43] and its legal representative. The legal representative represents the legal person in civil acts according to the provisions

40 Guiding Opinions of the Supreme People's Court on Several Issues concerning the Trial of Cases of Disputes over Civil and Commercial Contracts under the Current Situation《最高人民法院关于当前形势下审理民商事合同纠纷案件若干问题的指导意见》issued by the SPC on 7 July 2009, No 40 [2009] ('Guiding Opinions of the SPC on Contracts under the Current Situation') Art 12.
41 ibid, Art 13.
42 ibid, Art 14.
43 General Provisions of Civil Law 2017, Art 57 defines 'legal persons' as 'organisations who have the capacity for civil rights and capacity for civil conduct, and can independently enjoy civil rights and bear civil liability according to the law'.

of the law or the articles of association/ bylaws of the legal person. When the legal representative engages in civil acts under the name of the legal person, the legal consequences of such acts shall be borne by the legal person.[44] The legal person may restrict the legal representative's authority through the bylaws or the governing body of the legal person. However, such restrictions shall not be set up against bona fide counterparties.[45]

[3-37] Under Article 50 of the CL, where the legal representative or person in charge of a legal person or an organisation exceeds the limits of his or her authority in concluding a contract, the contract shall be deemed effective unless the counterparty knew or should have known that the legal representative overstepped his or her authority.

3.2.3 Unauthorised disposition of property

[3-38] Article 51 of the CL deals with another type of contract of pending validity:

> Where a piece of property belonging to another person was disposed of by a person without the power to do so, and the principal ratifies the act afterwards or the person without the right of disposal subsequently obtains the right after concluding a contract, the contract shall be deemed valid.

[3-39] The above rule only spells out the conditions in which a contract concluded by a person without the right to dispose the property (*wuquan chufen*) would be effective. There is still an unresolved question regarding whether the contract would be void or the act of disposal would be invalid *without* subsequent ratification or attainment of the power of disposal. The basic rights of property ownership include the right to possess, utilise, benefit from, and dispose of the property. Nevertheless, the right to dispose the property is considered the core of ownership.[46]

[3-40] Article 51 has generated considerable scholarly debate concerning the protection of the bona fide counterparty who purchases the property through a contract with a seller who did not have the right to dispose the property. Some scholars have argued such a contract should not be void because the principal (who has the right to dispose the property) refuses to ratify the contract. From the perspective of maintaining certainty and security of transactions, the refusal of ratification by the principal should not bind the bona fide purchaser.[47]

44 ibid, Art 61.
45 ibid.
46 Zhang, 165.
47 Liming Wang, Shaokun Fang, and Yi Wang, *Contract Law* 《合同法》(4th edn, China Renmin University Press 2013) 118.

[3-41] The SPC has adopted an approach that largely favours the bona fide purchaser in a sales contract, which suggests that an unauthorised disposal of property in this context affects only the act of disposal itself but not the validity of the contract:

> Where any party claims that a contract is void because the seller has no right to own or dispose of the subject matter at the time of contract formation, the court shall not support such claims.
>
> If the title of the subject matter is unable to be transferred because the ownership of or the right to dispose the subject matter could not be obtained, the buyer has a right to demand the seller bear liability or request the termination of the contract and claims for liquidated damages.[48]

[3-42] The distinction between the validity of a contract and an act involving the exercise of a property ownership right can also be found in Article 15 of the Property Law.[49] This provision recognises that a contract concerning the creation, alteration, transfer or extinction of (real) property rights shall become effective upon the conclusion of the contract, unless otherwise provided for by law or agreement. It further states that where the property right is not registered, it shall not affect the validity of the contract. The following case illustrates the application of these rules.

Illustrative case: *Mao Shuguang v Liu Ping*[50]

The appellant and respondent jointly owned the property involved in this dispute. The title of the property was registered in the respondent's name. The respondent sold the property to a third party (through an intermediary real estate broker) without the appellant's consent. The appellant challenged the validity of the intermediary housing sales contract, which was signed between the respondent, third party purchaser, and the broker.

The first instance court determined the disputed contract to comprise a housing sales contract between the respondent (seller) and the purchaser as well as another contract between the respondent, purchaser, and the intermediary broker. It held that the sales contract did not violate mandatory provisions of the law and none of the grounds under Article 52 of the CL applied in this case. The court held that the housing sales contract between the respondent and the purchaser was legal and effective. The contract with the intermediary broker was also valid on that basis.

48 SPC Interpretation on Sales Contracts, Art 3.
49 Property Law of the People's Republic of China 《中华人民共和国物权法》 adopted at the 5th session of the Tenth National People's Congress on 16 March 2007, effective 1 October 2007.
50 毛曙光、刘萍房屋买卖合同纠纷案，天津市第一中级人民法院民事判决书 (2017) 津01民终1703号.

In its reasoning, the first instance court relied on Article 15 of the PRC Property Law as well as Article 3 of the SPC's Interpretation on Sales Contracts. In explaining the SPC's Interpretation, the court pointed out that in a contractual relationship involving the sale of property, the contract itself is only a causal act (*yuanyin xingwei*) — that is, the contract causes the change in property rights. Transfer of ownership is the result of the change in property rights. The seller in this case did not have the full ownership of or the right to dispose the property at the time of contracting with the buyer. However, this fact did not affect the validity of the sale contract as the causal act. Furthermore, the seller was the registered title owner of the property and issued a housing ownership certificate to the buyer at the time of concluding the contract. Based on the public trust that underpinned the system of property registration, the buyer had reason to believe that the respondent was the owner of the property. Therefore, there was no factual or legal basis for supporting the appellant's claim that the contract was invalid. If the appellant was of the view that the respondent had infringed his lawful rights and interests, he may pursue a separate lawsuit against the respondent.

The court of second instance affirmed the decision of the first instance court, with a further emphasis on the fact that the purchaser had obtained the house in good faith. It added that since the appellant and respondent were now divorced, the property dispute should be resolved through other channels.

3.2.4 Requirement of approval and registration

[3-43] As mentioned earlier, Article 44 of the CL stipulates that if relevant laws or administrative regulations require the approval or registration of a contract before it can become effective, then those provisions shall apply. The SPC has applied a more flexible approach to this rule. In many circumstances, the failure to comply with procedural formalities of approval or registration would not be fatal to the validity of a contract.

[3-44] Where a contract does not become effective until the formalities of approval or registration are handled under the relevant laws or administrative regulations, the parties may undertake such formalities before the completion of the court debate in the first instance trial. It is only when the parties have failed to do so that the contract is regarded as not coming into effect.[51] In other words, parties have the opportunity to rectify this procedural defect even when court proceedings have commenced—up until the end of the first instance court debate when the parties have exchanged evidence and presented their claims and arguments.

[3-45] If a party has the duty to undertake the approval or registration formalities and fails to do so, such failure shall be deemed a breach of that party's precontractual obligations, namely a violation of the principle of good faith under Article 42(3) of the CL. In this situation, the court may rule that the other party go through the relevant formalities on its own.[52]

51 SPC Interpretation I, Art 9.

52 SPC Interpretation II, Art 8.

[3-46] The application of Article 44 seems less rigid when it comes to registration requirements. If the law or administrative regulation provides for contract registration but does not specify that the contract shall become effective upon registration, the parties' failure to handle the formalities of registration will not affect the validity of the contract. However, ownership and other property rights in relation to the subject matter of the contract cannot be transferred in this case.[53] Such an approach further reflects the distinction between the validity of a contract and the transfer of ownership and property rights as discussed earlier in the context of contracts involving unauthorised dispositions of property.

3.2.5 Conditions affecting the validity of contracts

[3-47] The parties may agree that the effectiveness of a contract is subject to certain conditions. These conditions are comparable to the concepts of 'condition precedent' and 'condition subsequent'. Article 45 of the CL addresses how such conditions affect the validity of a contract.

[3-48] There are two types of conditions associated with the legal effect of a contract under Article 45. First, there are 'effecting conditions' that determine if and when a contract comes into effect. A contract subject to such conditions shall become effective upon the fulfilment of the conditions. In other words, the validity of the contract depends on the occurrence or satisfaction of the effecting condition. As such, it has also been referred to as a 'suspensive condition'.[54] For example, the parties may agree that their contract for the sale of a technological invention will be effective upon the successful testing of the product. In this case, the contract will not take effect until the product has been tested successfully.

[3-49] Second, there are 'dissolving conditions' (or 'extinguishing conditions') that apply to contracts that are already effective.[55] A contract subject to such conditions shall cease to be effective upon the fulfilment of the conditions. In other words, the contract is no longer valid when the dissolving conditions are realised. For example, the parties may agree that a contract for the supply of specialised computer equipment will cease to be effective if/when a party needs to update its operating system that would render the (incompatible) equipment useless.

[3-50] Article 45 further seeks to prevent improper, opportunistic behaviour by a party to manipulate or abuse the condition in question. If a party improperly precludes the fulfilment of a condition for its own gain, the condition shall be regarded as fulfilled. If a party improperly facilitates or hastens the realisation of a condition, such a condition shall be regarded as unsatisfied.

[3-51] Under Article 46 of the CL, the parties may also agree on a time limit pertaining to the effectiveness of the contract. A contract with an 'effecting time limit'

53 SPC Interpretation I, Art 9. As mentioned earlier, Article 15 of the Property Law states that if the property right is not registered, it shall not affect the validity of the contract.

54 Zhang, 196.

55 ibid.

shall come into effect upon the expiry of the time limit — that is, the contract becomes effective when a specific date has passed. A contract with a 'dissolving time limit' shall cease to be effective upon the expiry of the time limit.

[3-52] As Professor Zhang explains, the key difference between 'conditions' under Article 45 and 'time limits' under Article 46 is that the former concerns an uncertain fact at the time of concluding the contract (that is, the parties do not know whether and when the condition will occur). In contrast, the latter (time limit) is a certain fact at the time of the contract.[56]

3.3 Voidable Contracts

[3-53] A voidable contract usually involves some defect in (at least) one party's expression of intent. The defect arises because the contract was concluded against a party's true intention through fraud, coercion, or exploitation of one party's unfavourable position. In these circumstances (and where there is no State interest involved), Article 54 of the CL gives the injured party the right to request a court or an arbitration institution to modify or revoke such a contract. Article 54 also provides a party with the right to seek the alteration or revocation of a contract that was concluded because of substantial misunderstanding or a contract that was evidently unfair at the time of its conclusion.

[3-54] It should be emphasised that a party may only exercise the right to alter or revoke a contract under Article 54 by way of petition to a court or an arbitration institution. The party itself cannot declare a voidable contract as altered or revoked. The original contract remains on foot until the court or arbitration institution has altered or revoked it. A revoked contract has no legally binding effect *ab initio*.[57] We examine below the grounds that render a contract voidable under Article 54: fraud, coercion, exploitation, evident unfairness, and substantial misunderstanding.

3.3.1 Fraud

[3-55] If a party engaged in fraud to induce the other party to conclude a contract against the other party's true intention, Article 54 of the CL gives the injured (defrauded) party the right to request the court or arbitration institution to alter or revoke the contract. This rule is also reflected in Article 148 of the General Provisions of Civil Law 2017.

[3-56] Article 149 of the General Provisions of Civil Law 2017 further deals with a civil act that resulted from the fraud of a third party:

> Where a civil act is performed by a party against his or her true will as a result of fraud by a third party, the defrauded party shall have the right to request a court or an arbitration institution to revoke the act if the other party knew or should have known about the fraud.

56 ibid, 197.
57 CL, Art 56.

[3-57] The definition of 'fraud' in the context of Article 54 is not found in the CL or the two SPC interpretations concerning the CL. Reference may be made to the SPC Opinion on the GPCL, which stipulates that:

> If one party wilfully conveys false information to the other party or deliberately conceals facts from the other party and thereby induces the other party into making a false expression of intention, such act is determined a fraudulent act.[58]

[3-58] As Professor Wang Yi argues, the element of 'deliberately concealing facts is premised on the actor's duty of disclosure'.[59] Professor Zhang further notes that a fraudulent act would include a party's failure to disclose certain facts that he or she is obliged to disclose under the provisions of the law, existing agreements, or trade customs.[60]

[3-59] It should also be noted that Article 42 of the CL imposes precontractual liability on a party that intentionally conceals 'material facts' relating to the conclusion of the contract. The deliberate concealment of material facts is likely to fall within the SPC's definition of a fraudulent act.

[3-60] Based on the SPC's definition, scholarly commentary points to the following components of 'fraud' under Article 54:

(1) An act of fraud or misrepresentation, which can be active or passive, express or implicit (in conveying or concealing information);
(2) The defrauding party has the intent to defraud, that is, it has knowledge of the fraudulent circumstances (such as the falsity of the information given) and the purpose of its act is to induce the other party into concluding the contract;
(3) The defrauded party's erroneous belief regarding the information that the defrauding party has given or concealed (that is, the state of mind of the defrauded party);
(4) The defrauded party's erroneous manifestation of intent, which concerns the action taken by the defrauded party in reliance on the misrepresentation (that is, the causation between the misrepresentation and the defrauded party entering into the contract).[61]

3.3.2 Coercion/duress

[3-61] Where one party makes the other party enter into the contract through coercion or duress against the other party's true intent, the coerced party is entitled under Article 52 of the CL to seek the revocation or alteration of the contract. Under Article 150 of the General Provisions of Civil Law 2017, the right of revocation is also available where coercion by third parties has caused the coerced party to carry out a civil act against its true intent.

58 SPC Opinion on the GPCL, Art 68.
59 Yi Wang (n 12) 220.
60 Zhang, 173.
61 ibid, 172-174.

[3-62] In some cases, one party may attempt to get the other party to accede to its demands by exerting a high degree of pressure or negotiating in a 'tough' manner. The distinction between aggressive yet legitimate bargaining tactics and acts of coercion can be difficult to draw in practice. Guidance may be drawn from the SPC Opinion on the GPCL, which defines coercion as an act whereby:

> A person forces another person to make an expression of intention that is contrary to his or her true will by threatening harm to the life, health, honour, reputation, or property of that person or his or her relatives or friends or to cause damage to the honour, reputation, or property of a legal person.[62]

[3-63] Based on the above definition, coercion entails a threat to cause personal harm or property damage to the coerced party or his or her relatives or friends. The threat is wrongful and causes fear of harm in the mind of the coerced party. Under such threat, the coerced party has no other alternative but to make a declaration of intent, against his or her true will, pursuant to the threat (such as concluding the contract with the coercing party).

[3-64] Scholars have pointed to four aspects of coercion:

(1) an intent to coerce, where the coercing party knows that its conduct will create fear in the coerced party and does so with the expectation that the coerced party will have no choice but to succumb to its demands;
(2) an act of coercion, which includes threats to cause potential harm or damage as well as threats that the coerced party is actually experiencing;
(3) the wrongfulness of the coercive act, for example, the act is contrary to legal or contractual obligations or serves an illegitimate purpose; and
(4) causation, which requires the threat to be so imminent and severe to cause fear in the coerced party that it has no other choice except to conclude the contract.[63]

[3-65] Professor Zhang argues that the SPC's definition of coercion sets out a subjective test for determining whether the will of the coerced party has been overcome to such an extent because of the threat. As such, it is irrelevant whether a 'reasonable person' would be in fear under the same or similar circumstance.[64] In his view, the threat must be one that caused the coerced party 'to fear that the harm or damage threatened is so imminent and serious that he would have no other alternative, and under this fear, the contract is concluded according to the terms and conditions produced by the coercing party'.[65] In contrast, Professor Wang Yi asserts that 'the coerced party must be in fear or *reasonably* believe

62 SPC Opinion on the GPCL, Art 69.
63 Zhang, 176–177; Junwei Fu, *Modern European and Chinese Contract Law: A Comparative Study of Party Autonomy* (Wolters Kluwer 2011) 108.
64 Zhang, 175.
65 ibid, 177.

the possibility of the damage and threat claimed by the party'.[66] Similarly, the UNIDROIT Principles apply a test based on 'no reasonable alternative' for evaluating the imminence and severity of the threat.[67]

[3-66] The threat itself must be wrongful. If a party has a lawful basis for putting pressure on the other party, a case of coercion is unlikely to be made out. An example of a lawful threat is where a party threatens to bring a lawsuit against the other party because the other party has failed to perform its obligations under an existing agreement. Nevertheless, if the motivation for such a threat is not to exercise one's legal rights but to pursue a wrongful purpose such as forcing the other party to conclude a contract on one's terms and conditions, the threat may be considered coercion.[68]

[3-67] In the following case, the court did not consider the 'threat' of the respondent to exercise his legal rights (namely, to enforce a contractual right against a third party, which affected the claimant's interests) as coercion.

Illustrative case: *Hangzhou Xiaoxin House Exchange Co Ltd v Cao Xiaoyun*[69]

Through the appellant's real estate brokerage services, the respondent sold a house to a buyer for an agreed price of 2.29 million yuan. Under the sales contract for the house, the buyer shall make the first payment of 690,000 yuan towards the purchase price before 6 October 2016 and the second payment of 1.6 million yuan before 6 November 2016. The contract contained a liquidated damages clause in relation to late payments. The appellant later arranged a contract for the property transfer in which the buyer shall pay the first payment to an account supervised by the appellant within 15 working days of the contract date and the second payment directly to the respondent. The appellant also agreed to settle the transaction.

The buyer paid the initial payment three days late on 9 October 2016 (but paid the full purchase price on 13 October 2016). The respondent demanded the payment of liquidated damages from the buyer for the late payment of the initial amount or else the respondent would not hand over the keys. To facilitate the completion of the transaction, the appellant paid the respondent the liquidated damages on behalf of the buyer. Afterwards, the appellant brought a claim seeking to revoke the contract (relating to the liquidated damages it paid to the respondent) based on coercion. The appellant argued that it was forced to pay the liquidated damages due to the respondent's threat of not handing over the keys to complete the property transfer.

66 Yi Wang (n 12) 220.
67 Article 3.2.6. of the UNIDROIT Principles states that: 'A party may avoid the contract when it has been led to conclude the contract by the other party's unjustified threat which, having regard to the circumstances, is so imminent and serious as to leave the first party no reasonable alternative'.
68 See UNIDROIT Principles, Art 3.2.6 (Comment 2); Liming Wang, *Research on Contract Law Vol. 1*《合同法研究（第一卷）》(China Renmin University Press 2002) 646–647.
69 杭州萧新房屋置换有限公司与曹筱鋆居间合同纠纷上诉案，浙江省杭州市中级人民法院民事判决书(2017)浙01民终694号.

The court of first instance concluded that the appellant could not substantiate its claim. In the court's view, the appellant believed that if it did not pay the respondent the liquidated damages, the respondent would not deliver the keys to the buyer and as such, the appellant would default on its own obligations to the buyer. The court reasoned that the payment of liquidated damages pertained to the contract between the buyer and seller. The appellant was acting as a 'substitute' for the buyer when it decided to pay the liquidated damages arising from the buyer's breach of the said contract. Based on the privity of contract, there were no legal consequences for the appellant flowing from the buyer's breach. In the court's view, the appellant's payment to the respondent could be seen as an extension of its provision of brokerage services to facilitate successful completions, so it was aligned with its own interests (not only in relation to the profit from the transaction but also the market's evaluation of its service quality).

The second instance court also reached the same conclusion. The court found that the respondent sought to enforce his contractual rights arising from the buyer's breach by not cooperating with the completion until the dispute was resolved. Such a measure did not constitute coercion. The respondent also did not force the appellant to assume liability for the liquidated damages, since the late payment pertained to the contract between the buyer and seller. In the process of consulting the buyer and seller, the appellant recognised that there were flaws in its brokerage services. The appellant's decision to pay the respondent liquidated damages was based on the respective demands of the buyer and seller, the appellant's own recognition of flaws in its services that contributed to the dispute, and the facilitation of the transaction's completion. As such, the appellant's manifestation of intent was genuine. The court held that there was no coercion and dismissed the appellant's petition.

3.3.3 Exploitation of the other party's unfavourable position

[3-68] When one party takes advantage of the other party's unfavourable position such as a situation of distress, the innocent party has the right to request the court or arbitration institution to revoke or alter the contract under Article 54 of the CL.

[3-69] According to the SPC Opinion on GPCL, exploitation of another party's unfavourable position refers to a situation where:

> A party, in order to secure a wrongful benefit, takes advantage of another party's unfavourable position to force the other party to make an expression of intention that is contrary to his or her true will, thereby severely damaging the other party's interests.

[3-70] It could be said that there are four general requirements:

(1) the innocent party is under a difficult, distressful, or unfavourable position;[70]

70 Some translations of 'unfavourable position' have referred to 'distress', 'difficult position', 'jeopardy position', or 'precarious position'.

(2) an act of exploitation, involving a statement or conduct through which a party compels the other party (innocent party) to conclude the contract against his or her true intent;
(3) the deliberate nature of the exploitation, where the exploiting party knows of the other party's unfavourable position and leaves the other party with no alternative other than entering into the contract against his or her true intent;
(4) the innocent party has suffered damages as a result of the exploitation.

[3-71] The scope of the other party's 'unfavourable position' can include urgent and desperate needs of an economic nature.[71] Some scholars have referred to situations where the interests of the other party or its relatives such as life, health, reputation, or property are in serious jeopardy.[72] As the following case suggests, the scope of 'unfavourable position' can include economic compulsion or pressure (although in this case, the court did not find the existence of an act of exploitation).

Illustrative case: *Qiqihar Xinyuan Real Estate Development Co Ltd v Song Ping*[73]

The appellant, a property developer, obtained state-owned land use rights to carry out a reconstruction project in an old urban area where the respondent resided. The appellant was responsible for relocating and resettling the residents in the area. The respondent initially had two houses in the area, including a certified house (69.05 square metres in size) and an uncertified house (15.6 square metres in size). Based on the resettlement plan, the respondent would be moved to an 80-square-metre house. However, based on plans to change the whole area to non-residential use, the respondent requested a commercial lot of 100 square metres in size and two sets of residential housing (80 square metres per set).

The appellant argued that the respondent exploited the appellant's unfavourable position by forcing the appellant to conclude a contract in accordance with the respondent's unreasonable demands. The appellant claimed that it had a tight schedule for relocating the affected households within one year before the expiry of the demolition permit granted by the government (2010–2015) and that the respondent knew this and kept postponing the conclusion of a resettlement agreement. The appellant alleged that the contract it concluded with the respondent in 2014 violated the principle of fairness and caused a serious imbalance in the parties' rights and obligations that was evidently unfair. The appellant argued that the contract severely damaged its interests and was also unfair to the other relocated households. The appellant sought the alteration of the contract so that the respondent would move to an 80-square-metre house. The respondent argued that the defendant was not in an unfavourable position and that any developer should have foreseen a tight schedule for construction.

71 Zhang, 185.
72 Liming Wang and Jianyuan Cui, *New Study on the Law of Contract: General Principles (Revised edition)* 《合同法新论总则（修订版）》 (China University of Political Science and Law Press 2000) 287–288.
73 齐齐哈尔鑫苑房地产开发有限责任公司与宋平房屋拆迁安置补偿合同纠纷案，依安县人民法院民事判决书 （2015）依民初字第 614 号.

[6-4] After examining the small handful of rules (Articles 77 and 78) in the CL regarding contract modification by agreement, we devote most of this chapter to understanding the main provisions (Articles 79-90) that address the transfer of contractual rights and obligations.

6.2 Modification of Contract

[6-5] Under Article 77 of the CL, parties may modify an existing valid contract based on mutual agreement. The fundamental principle of *pacta sunt servanda* in Article 8 means that one party cannot unilaterally alter the contract. Unilateral modification of a contract is only permitted if the parties' agreement or the law provides for such a right. The parties' freedom to modify a contract may also be subject to certain legal requirements. Notably, Article 77 states that if the contract modification must go through approval and registration procedures under relevant laws or administrative regulations, those legal provisions shall apply. According to the SPC, the parties may undertake the formalities of approval and/or registration at any point before the completion of the first instance court hearing, if a contract modification is challenged in court in order for the modification to become effective.[4]

[6-6] Contract modification under Article 77 essentially involves the parties entering into a separate agreement with the object of varying the terms of the existing contract. As such, the modification agreement is subject to the general rules on contracts. While the parties' original contractual rights and obligations may have changed, modification does not extinguish the original contract. The terms of the original contract that have not been modified, as well as the collateral rights and defences attached to the contract, remain effective after modification — unless their continuation is discordant with the modification.[5]

[6-7] The general rules on the formation of contracts apply to modification. Accordingly, modification can be in written, oral, or other forms.[6] The parties may agree that modification to the contract must be in a particular form. Furthermore, if a law or an administrative regulation requires contract modification to be in a particular form, the modification in question will take effect only if such requirements are satisfied.[7] Otherwise, it is possible that the existing contract can be modified by 'other forms', including the parties' conduct where the conduct clearly evinces their intention to modify the contract based on consensus.

[6-8] It is important to highlight that modification of contract based on mutual agreement requires an unequivocal indication of the parties' assent to the modification. Article 78 of the CL sets out a presumption against modification where the purported agreement to modify the contents of an existing contract is ambiguous. In the following case before the SPC, a party unsuccessfully invoked Article 78 to challenge a new modification agreement that the parties had signed.

4 SPC Interpretation I, Art 9.
5 Ling, 304.
6 CL, Art 10.
7 SPC Interpretation I, Art 9.

Illustrative case: *Beidahuang Xinya Trade LLC v Beidahuang Qingfeng Linen Textile Co Ltd*[8]

The appellant and respondent entered into eight Ownership Confirmation Agreements for cargo processing in 2012 and 2013. The appellant was the owner of cargo and the respondent agreed to store and deliver the final processed cargo to the appellant. Under the agreements, the respondent would be liable for the quantity, quality, and safety of all cargo in the inventory. After concluding the Ownership Confirmation Agreements, the parties signed an Ownership Transfer Agreement that stated the respondent would process and deliver specific goods after the transfer of ownership from a third party to the appellant for those goods. The respondent did not deliver all the processed goods. The appellant brought a claim seeking the delivery of the remaining goods. The respondent applied for adjournment of the trial, claiming the court should make judgement after the warehouse owner and the two contracting parties made an inventory on the quantity, categories, and values of the goods.

An issue of contention in the case was the legal nature of the Ownership Transfer Agreement. The appellant claimed that the Ownership Transfer Agreement could not be executed and insisted that the respondent should deliver the cargo in accordance with the Ownership Confirmation Agreement.

The first instance court ruled that the Ownership Confirmation Agreements and Ownership Transfer Agreement were lawfully made and truly expressed the two parties' intention. As per Article 8 of CL, the contracts shall be binding. The court found that the parties had not made any inventory on the goods or calculated the value of the goods before delivery under the Ownership Transfer Agreement. The insistence of the appellant on the delivery of the remaining goods according to the Ownership Confirmation Agreements lacked factual and legal basis.

The appellant argued that the first instance court did not clearly identify the legal relationship at stake. It claimed that the Ownership Transfer Agreement was a supplementary document of the Ownership Confirmation Agreements and not a new contract per se. It should be read together with the Ownership Confirmation Agreements. The appellant argued that Article 78 of the CL should be applied, which presumes a contract as not having being modified if the content of the purported modification is ambiguous.

The respondent claimed that the Ownership Confirmation Agreements and the Ownership Transfer Agreement were binding on both parties. It maintained that there was nothing unclear in the Ownership Transfer Agreement and Article 78 was not applicable. The transfer of ownership should be done in accordance with the new Ownership Transfer Agreement.

8 北大荒鑫亚经贸有限责任公司与北大荒青枫亚麻纺织有限公司保管合同 纠纷上诉案，最高人民法院民事判决书（2015）民二终字第 199 号.

The second instance court held that the execution of Ownership Confirmation Agreements should abide by the Ownership Transfer Agreement. In accordance with Article 8 of the CL, the Ownership Transfer Agreement was a lawfully established contract and shall be legally binding on the parties thereto. The parties had not made an inventory of the cargo nor settled the account of the known cargo. The transfer of ownership requirement stipulated by the Ownership Transfer Agreement was therefore not satisfied. The court concluded that the appellant's claim lacked legal basis and was contradictory to the contractual agreement made by the two parties. The appeal was dismissed.

[6-9] There may be special rules on modification that relate to particular types of contracts. For example, where there is a guarantee arrangement, the creditor and debtor must obtain written approval from the guarantor prior to modifying the principal contract. If modification takes place without such approval, the guarantor will no longer be bound by its guarantee responsibilities. An exception to this rule is if the guarantor and debtor have agreed on other arrangements.[9] The type and effect of modification also has a bearing on the liability of the parties. For example, if the creditor and debtor modify the quantity, price, currency, interest rate, and other aspects of the principal contract without the guarantor's consent and the modification in question reduces the debtor's obligation, the guarantor shall still be liable for the modified contract. On the other hand, if the (unapproved) modification increases the debtor's obligation, the guarantor will not be liable for the increased portion.[10]

6.3 Transfer of Contract

[6-10] A contracting party may enter into an agreement with a third party for the purpose of transferring its rights and/or obligations, either wholly or partially, to a third party. There are different rules under the CL pertaining to the assignment of contractual rights (Articles 79-83), delegation of contractual obligations (Articles 84-86), and combined transfer of rights and obligations (Articles 88-90). The rule in Article 87 is concerned with any transfer of rights and/or obligations that is subject to approval and/or registration procedures. The relevant laws and administrative regulations relating to such procedures shall apply. The parties may undertake such procedures at any point before the completion of the first instance court hearing, if a contract modification is challenged in order for the modification to become effective.[11]

[6-11] Transfer of contract can be distinguished from the situations under Articles 64 and 65 of the CL (which we examined in Chapter 5) where the contracting parties agree that the debtor performs the obligations to a third party or a third party performs the obligations to the creditor. An assignment of rights and/or delegation of obligations essentially change the original contractual relationship between the debtor and creditor. Under an effective assignment of rights, the creditor/assignor's interest in the contract is relinquished to the extent

9 Security Law of the People's Republic of China 《中华人民共和国担保法》 Art 24.
10 SPC Interpretation on the Security Law, Art 30.
11 SPC Interpretation I, Art 9.

that its contractual rights have been assigned to the third party. The debtor does not need to agree to the assignment, but must be notified. In the case of delegation, the original debtor (transferor) is released from the transferred obligations and the third party effectively becomes the new debtor.

[6-12] An important difference between the transfer of contract and performance rendered to/by a third party is the standing of third parties in judicial proceedings. As discussed in Chapter 5, in the context of Articles 64 and 65 of CL, a third party cannot be listed as an independent claimant or defendant in a contract lawsuit.[12] On the other hand, the courts will support a third party seeking to modify and add itself as an applicant in a civil enforcement claim where the creditor has lawfully assigned its rights to the third party in writing.[13] As the following case shows, courts can sometimes struggle to draw a clear line. In this case, the first and second instance courts reached different conclusions regarding the characterisation of the disputed claim as involving performance by a third party or an assignment of contractual rights.[14]

Illustrative case: *Wang Rong v Wenzhou Yate Steel Co Ltd*[14]

The respondent and another party, Chen Bingrong ('Chen'), concluded a contract in which the respondent was obliged to deliver a batch of steel ingots to Chen. The appellant entered into a contract with Chen with the purpose of transferring Chen's contractual right (to receive the ingots from the respondent) to the appellant. Notification of the transfer was sent to the respondent so that the respondent would directly deliver the steel ingots to the appellant. However, the respondent failed to prepare and deliver the ingots to the appellant. As such, the appellant brought a claim directly against the respondent.

The first instance court relied on Article 65 of CL and concluded that the respondent was a third party to the contract between the appellant and Chen. It held that the appellant could not bring its claim against a third party for its non-performance of the contract. Instead, the appellant should have pursued the claim against Chen for breach of contract. The appellant's claim against the respondent was dismissed.

The second instance court found that the first instance court had mischaracterised the legal nature of the relationship between the parties. In this case, the second instance court found that there was an assignment of contractual rights by Chen to the appellant pursuant to Articles 79, 80, and 82 of the CL. The respondent had acquired Chen's contractual rights through the assignment and could therefore claim directly against the appellant.

12 SPC Interpretation II, Art 16.
13 Provisions of the Supreme People's Court on Several Issues Concerning the Modification and Addition of Parties in Civil Enforcement, Judicial Interpretation No. 21 [2016]《最高人民法院关于民事执行中变更、追加当事人若干问题的规定》法释 (2016) 21号, Art 9.
14 王荣等诉温州超特轧钢有限公司保管合同纠纷案, 浙江省温州市中级人民法院民事裁定书 (2017) 浙03民终813号.

6.3.1 Assignment of contractual rights

[6-13] Under Article 79 of the CL, the creditor (assignor) may assign all or part of its rights under the contract to a third party (assignee) by way of an agreement between the assignor and assignee. Where the contractual rights are assigned in whole, the assignee effectively takes the place of the creditor and the debtor is obliged to render performance of the contract to the assignee. In the absence of specific rules in the CL, the possibility for partial assignment raises the question of the status of the assignor and assignee vis-à-vis the debtor. The general view among scholars is that the assignee joins the assignor as a 'co-creditor' after the assignment. The assignor and assignee have independent claims against the debtor in relation to performance of the relevant obligations. The debtor may also exercise separate defences against each co-creditor and bears separate liability for breach in relation to each co-creditor.[15]

[6-14] An important aspect of valid assignments is that the contractual right must be assignable. Under Article 79, there are certain circumstances in which a creditor cannot transfer its rights under a contract to a third party. First, the assignment is not permitted by virtue of the nature of the contract. Here, the unassignable contractual right must be so closely related to the particular identities of or the personal relationship between the contracting parties that the right cannot be assigned to others. For example, where the performance by the creditor entails a personal skill on its part or where performance is premised on mutual personal trust and confidence between the creditor and debtor, it is unlikely that the contractual right could be assigned.

[6-15] Second, the contracting parties may have agreed in the first place that the assignment of contractual rights is prohibited or restricted. In this situation, the creditor cannot subsequently demand that the debtor comply with an assignment to the third party. The CL does not address the consequences of a prohibition on assignment in relation to a bona fide assignee, where the assignee had no knowledge or reason to know about the prohibition at the time of entering into the assignment agreement with the assignor. An influential view among commentators is that the contracting parties' agreement to prohibit the assignment of rights cannot be used against a bona fide assignee.[16]

[6-16] Finally, a party cannot assign its contractual rights where the assignment is proscribed by provisions of law. For example, under Article 61 of the Security Law, the creditor's rights in a principal contract for a maximum mortgage cannot be assigned. In the following illustrative case, a main aspect of the parties' dispute concerned the validity of an assignment agreement. The respondent claimed that the agreement was void as it concealed an illegitimate purpose under the guise of a legitimate form.

15 Ling, 311; Zhang, 239.

16 Ling, 312.

Illustrative case: *Beijing Yihehua Technology Development Co Ltd v Shanghai Green Engineering Co Ltd and Shanghai Flower Harbour Development Co Ltd*[17]

In 2002, the second respondent (Shanghai Flower Harbour Development Co Ltd) and Asia ADC Ltd signed a contract to jointly set up an enterprise. Asia ADC Ltd appointed the chairman of the board and controlled the operations of the enterprise. When the enterprise's operations incurred significant losses in 2005, the second respondent brought a claim against Asia ADC Ltd for compensation (of almost 16 million yuan). In 2007, the Shanghai Higher People's Court handed down a judgment that supported the second respondent's claim.

Meanwhile, in 2004, Asia ADC Ltd had also signed a sales agreement with the two respondents in this case. After Asia ADC Ltd had performed its contractual obligations, it did not receive the remaining payment of 1.4 million yuan from the respondents. In July 2006, Asia ADC Ltd and the appellant sent a 'Notification of Assignment of the Creditor's Right' to the two respondents, which stated that the creditor's rights of Asia ADC Ltd under the sales agreement were assigned to the appellant henceforth. The appellant later sought to exercise its assigned rights against the respondents. However, the respondents refused to recognise the validity of the assignment. The appellant brought the case against the respondents in 2009.

The first instance court dismissed the appellant's claim in 2011. The court considered the circumstances of the claim between the second respondent and Asia ADC Ltd. It concluded that Asia ADC Ltd's assignment of rights to the appellant was carried out maliciously. The court's view was that Asia ADC Ltd was fully aware of its legal obligations to compensate for the losses of the enterprise it controlled and of potential solvency problems. In such circumstances, Asia ADC Ltd assignment of its creditor's rights to the appellant was 'obviously malicious'. On the basis of Article 52(3) of the CL (which renders a contract void where an illegitimate purpose is concealed under the guise of a legitimate act), the court ruled that the assignment did not have legal effect.

The second instance court reversed the judgment of the first instance court and supported the appellant's claim. The Shanghai Higher People's Court held that Asia ADC Ltd's assignment of its creditor's rights to offset the debt it owed to the appellant was a lawful act. Although the assignor and assignee were affiliated, the appellant was a legitimate creditor of Asia ADC Ltd and the law did not forbid the debtor from paying a creditor (including an affiliated company) while the debtor was solvent, even if the assignment may affect its ability to repay other creditors. As such, the assignment was valid.

It should be noted that in related proceedings, the second respondent had petitioned the court for revocation of Asia ADC Ltd's assignment to the appellant in accordance with Article 74 of the CL. The second respondent argued that the

17 北京以合华科技发展有限公司与上海都市绿色工程有限公司等买卖合同纠纷上诉案, 上海市高级人民法院民事判决书 (2011)沪高民二(商)终字第39号.

transfer of the creditor's right occurred without any reward. However, this argument was not supported by the court since Asia ADC Ltd could prove that it had owed the appellant various service charges and commission fees.

[6-17] The debtor's consent to the assignment of rights is not necessary. Most importantly, Article 80 of the CL imposes a duty on the creditor to notify the debtor about the assignment. The assignment in question will not be effective in relation to the debtor until the debtor receives such a notice. There is no requirement as to the form of the notice, which may be made in writing or orally. Furthermore, once the creditor has notified the debtor of the assignment, such notice cannot be revoked unless the assignee gives its consent to the revocation. This rule serves to protect the assignee against the risk of the assignor unilaterally depriving the assignee of the assigned claim.[18] The case below demonstrates the importance of the notice requirement under Article 80.

Illustrative case: *Enforcement of Judgment in relation to Yang Xiaomin, Yang Xiaobin and others*[19]

The appellant and enforcee (Yin Deshan) and the respondents signed an Assignment Contract on 10 July 2014 pursuant to which the respondents transferred their creditors' rights to the appellant. Notification of the assignment did not reach the respondents' debtor, China Railway Group, until 30 September 2014. On 27 August 2014, the Taizhong Intermediate Court had sealed up[20] the respondents' claim against its debtor, China Railway Group, in a separate legal proceeding.

The Suzhou Higher People's Court held that in accordance with Article 80 of the CL, the assignment between the appellant and respondents did not become effective until the notice had reached China Railway Group. Although the parties concluded the assignment contract in August 2014, by the time China Railway Group was notified of the assignment, the Court had already sealed up the respondents' creditor claim. Under Article 26(1) of the Supreme People's Court Provisions on the Sealing up, Distraint and Freezing of Properties in Civil Enforcement, any act by an enforcee in respect of transferring or setting up an encumbrance to or impeding enforcement of civil judgments with regard to sealed up, distrained or frozen properties shall not frustrate the attempt of the party applying for enforcement. In this case, the court dismissed the appellant's petition for administrative reconsideration.

[6-18] Upon the valid assignment of contractual rights, Article 81 of the CL provides that the assignee acquires any collateral or accessory rights that are connected to the principal rights that have been assigned. Examples of collateral rights include security rights, claims to interest, liquidated damages, and claims for remedies arising from

18 Ling, 318.

19 杨晓敏、杨晓彬等执行裁定书, 江苏省高级人民法院执行裁定书（2016）苏执复 91 号.

20 'Sealing up' (*cha feng*) refers to the act of a court 'when sealing up real properties, attach a strip of sealing or make an announcement, and may draw relevant certificates and licenses of the property rights for preservation': Article 9, Provisions of the Supreme People's Court for the People's Courts to Seal up, Distrain and Freeze Properties in Civil Enforcement, adopted by the Adjudication Committee of the SPC on 4 November 2004 and effective 1 January 2005 (revised).

the contract. However, if the collateral rights are strictly personal or exclusive to the creditor, such collateral rights cannot be assigned along with the principal rights. For example, an employee's priority claim in bankruptcy proceedings for outstanding wages and social insurance indemnities could be deemed a personal right on the basis of his or her employment status.[21] Some scholars have casted doubt on whether the right to dissolve or terminate a contract can be assigned on the basis that such a right is strictly personal to the original contracting parties.[22]

[6-19] The assignment does not affect the defences available to a debtor against the original creditor/assignor. When the debtor receives notice of the assignment, Article 82 of the CL allows the debtor to assert against the assignee such defences. It is also possible that the debtor may have separate defences against the assignee after the assignment. For example, if the assignee does not exercise the contractual rights within a prescribed limitation period, the debtor may refuse to perform the contract.[23]

[6-20] The CL does not deal with a situation in which a debtor has rendered performance to the assignee without knowing that the assignment agreement was ineffective or revoked. Scholars have proposed the doctrine of 'ostensible assignment', which would allow the bona fide debtor to invoke defences against the assignor that it may utilise against the assignee. As such, if the debtor has received notice of the assignment and performed its obligation to the assignee, the assignor may not enforce its claim against the debtor on the basis that the assignment was ineffective or revoked.[24]

[6-21] Another provision that seeks to protect the debtor's legal position is Article 83 of the CL. Upon the debtor receiving notice of the assignment, the debtor may set off against the assignee any rights the debtor has against the assignor that were vested before or at the same time as the assignment. The debtor's right of set-off is premised on certain conditions (which we will examine further in Chapter 7). First, the original contracting parties must have mutual claims under the contract. To put it simply, the contracting parties are indebted to one another. Second, the claims to be set off must be due before or at the time of the assignment. Third, the subject matter of such claims are the same type and nature or quality. Fourth, the setoff is not barred by provisions of the law or the nature of the contract.[25]

[6-22] The CL does not have specific rules regarding assignments of the same contractual rights to multiple assignees. Scholars have proposed that it is the first assignee who has priority over subsequent assignees in the case of multiple assignments.[26] Within this order of assignment, it has been further suggested that an assignment for value should be prioritised over a gratuitous assignment and an

21 Ling, 319–320. See the Enterprise Bankruptcy Law of the People's Republic of China《中华人民共和国企业破产法》adopted by the Standing Committee of the 10th National People's Congress on 27 August 2006 and effective 1 June 2007, Art 113.

22 Liming Wang and Jianyuan Cui, *New Study of Contract Law: General (Revised edn,* China University of Political Science and Law Press 2000*)* 423.

23 Zhang, 246.

24 Ling, 318.

25 CL, Art 99.

26 Ling, 319.

assignment in whole takes precedence over a partial assignment.[27] Another approach is based on the order of notice, which prioritises the first assignment that the debtor was notified of, regardless of the order of assignment. Such an approach is based on the premise that an assignment of rights only binds the debtor upon notification.

6.3.2 Delegation of contractual obligations

[6-23] Under Article 84 of the CL, a contracting party may delegate its contractual obligations, in whole or in part, to a third party with the consent of the creditor. Compared to the assignment of contractual rights, the consent of the creditor is a precondition for the delegation of contractual obligations to a third party. If the creditor does not agree to the delegation, the delegation will not be effective. As such, the delegation of obligations requires the agreement of the creditor, debtor (transferor), and third party (transferee).

[6-24] Upon the valid delegation of contractual obligations in whole, the original debtor is released from the contract and the third party (transferee) assumes all obligations under the contract as the new debtor. Where the obligations are delegated in part, the third party is added as a joint debtor alongside the original debtor. In other words, the original debtor and third party jointly assume the contractual obligations. However, the CL does not clarify, in the context of partial delegation, the liability of the debtor and third party in relation to the creditor. The issue of liability in these circumstances would depend on the parties' intention or any specific provisions of law. One view is that the debtor and third party should only be responsible for performing their own parts of the contract. Another view posits that the debtor and third party would be jointly and severally liable for the contract.[28]

[6-25] According to Article 86 of the CL, the transferee shall assume the incidental obligations that are attached to the principal obligations that have been effectively delegated. Examples of collateral obligations include payment of accrued interest, payment of liquidated damages, or other compensation in the event of breach. However, where the collateral obligations belong personally or exclusively to the original obligor (such as those pertaining to the personal status or attributes of the debtor), those obligations may not be delegated to the transferee. If the contractual obligations are subject to a guarantee provided by a third party, the obligations may not be delegated unless the guarantor provides its written approval. If the obligations are delegated without its approval, the guarantor's responsibilities over such obligations shall come to an end.[29]

[6-26] As mentioned earlier, the delegation of contractual obligations to a third party does not extinguish the original contract. As such, any defence that the original debtor has against the creditor is unaffected by the delegation. Article 85 of the CL allows the new debtor (transferee) to assert any defence of the original debtor (transferor) against the creditor upon an effective delegation of obligations. The original debtor's right of defence must have existed before or at the time of the delegation. Unlike an assignment of rights, the CL does not provide for the

27 Zhang, 240.
28 Ling, 322–323; Zhang 247–248.
29 Security Law, Art 23.

possibility of a set-off arising from the delegation of obligations. The transferee/new debtor cannot set off any claims that the original debtor has against the creditor.

[6-27] Overall, the most important requirement of an effective delegation is the consent of the creditor. Once the creditor has given its consent to the transfer agreement between the original debtor and new debtor, the delegation takes effect on the terms of such an agreement. The transferor and transferee are generally barred from modifying or cancelling the delegation without the creditor's consent. The consent of the creditor can be in any form, such as written, verbal, or other form. The creditor's consent may be inferred from its conduct, such as accepting the transferee's performance.

[6-28] In the following case, the court sought to examine the relationship between Article 84 of the CL which is concerned with creditor's consent and Article 51 of the CL which is concerned with the unauthorised disposition of another's property.

Illustrative case: *Zhuangding Chun v People's Government of Xianning City, Xian An District, Hubei Province*[30]

The appellant claimed that the respondent had formed a company, Beilin Ltd, in order to evade its debt obligations to the appellant arising from a construction project. The appellant was a stakeholder and investor in the project. The appellant claimed that contrary to Article 84 of the CL, the respondent had transferred its debt of 2.13 million yuan to Beilin Ltd without the appellant's consent. After the transfer, Beilin Ltd subsequently applied for bankruptcy. The respondent also relied on Article 124 of the Enterprise Bankruptcy Law, which stipulates that after the conclusion of bankruptcy proceedings, the guarantor and joint-and-several debtors of the bankrupt enterprise will continue to bear liability for payment of claims that have not been paid according to the procedures for liquidation.

The court confirmed the following facts. In 2003, the respondent signed a delegation agreement with Beilin Ltd that transferred all of its obligations without the prior consent of the appellant (who was the creditor). In 2007, Beilin Ltd filed for bankruptcy. In 2008, Beilin Ltd began liquidation procedures before the Xian An District People's Court. In 2015, the appellant disputed the amount that he received as a creditor from the liquidation.

The court held that the respondent signed the delegation agreement without the appellant's consent, which was required under Article 84 of the CL. The transfer constituted an unauthorised disposition of the appellant's claims. In accordance with Article 51 of the CL, where a person without the right of disposal disposes another's property, the contract shall be effective when the person with the right of disposal ratifies the disposal.

30 庄定春、湖北省咸宁市咸安区人民政府建设工程施工合同纠纷案，最高人民法院民事裁定 书（2017）最高法民申 456 号.

In the court's view, the fact that the appellant had filed a claim with the administrator in Beilin Ltd's bankruptcy proceedings, participated in the distribution of bankruptcy assets, and received its proportion share based on its creditor's rights indicated the appellant's ratification of the respondent's act. Upon such ratification, the transfer/delegation of obligations between the respondent and Beilin Ltd was effective. As such, the creditor-debtor relationship between the appellant and respondent was extinguished, along with the debts owed by the respondent to the appellant. The Court dismissed the appellant's application for a retrial.

6.3.3 Combined transfer of rights and obligations

[6-29] Under Article 88 of the CL, a contracting party may transfer its rights together with its obligations under the contract to a third party, with the consent of the other contracting party. This 'combined transfer' or 'general transfer' simultaneously involves the assignment of contractual rights and the delegation of contractual obligations from the transferor to the transferee/third party. A combined transfer is ineffective without the other party's consent. The following case suggests that once the other party has given its consent to the combined transfer, it cannot subsequently 'change its mind' and revoke such consent.

Illustrative case: *Hohhot Dongwayao Real Estate Development Co Ltd v Inner Mongolia Fenghua (Group) Construction and Installation Co Ltd (Third Party: Hohhot Saihan District People's Government)*[31]

In December 1998, the Hohhot Saihan District People's Government (third party in the claim) and the respondent entered into an agreement to jointly reconstruct staff housing for the respondent's employees. In May 2001, the respondent signed an agreement with the appellant to transfer its contractual obligations and rights to the appellant. In its performance of its contractual obligations, the appellant failed to fulfil its obligation relating to the housing placements. The Hohhot Saihan District People's Government subsequently expressed its disagreement with the transfer arrangement. The appellant brought a claim before the Higher People's Court of Inner Mongolia Autonomous Region seeking to assert its assigned rights arising from the transfer.

The respondent argued that the transfer was not effective since the Hohhot Saihan District People's Government did not give its consent to the transfer. The appellant argued that such consent did not affect the effectiveness of the transfer and the rights transferred to the appellant were still valid. The first instance court supported the respondent's argument. The appellant brought an appeal to the SPC.

The SPC held that a mandatory requirement for an effective transfer of rights and obligations under Article 88 of the CL is the agreement of the other contracting party. In this case, the effectiveness of the transfer depended

31 呼和浩特市东瓦窑房地产开发有限责任公司与呼和浩特市赛罕区人民政府综合建设项目债权债务概括转让合同纠纷案，最高人民法院民事判决书（2012）民一终字第 102 号.

on whether the Hohhot Saihan District People's Government agreed to the transfer. Based on the evidence submitted, the SPC concluded that the Hohhot Saihan District People's Government was aware of the respondent entering into the transfer agreement with the appellant and initially approved the performance of the contractual obligations by the appellant. It was only later that the Hohhot Saihan District People's Government expressed its disapproval, which could not negate its initial agreement to the transfer. Based on these facts, the court held the agreement to be valid.

[6-30] The aforementioned rules in this section regarding the assignment of rights and the delegation of obligations apply concurrently to a combined transfer. Article 89 of the CL stipulates that a combined transfer is subject to the rules under Articles 79, 81-83, and 85-87. A combined transfer must entail assignable rights (Article 79). The transferee acquires the collateral rights and obligations associated with the principal rights and obligations, except those that are exclusive or personal to the transferor (Articles 81 and 86). The other party may invoke against the transferee any defence it has against the transferor (Article 82). The transferee may exercise any defence that the transferor has against the other party (Article 85). The other party may also set off against the transferee any rights it has against the transferor that vested before or at the same time as the combined transfer (Article 83). If the combined transfer is subject to mandatory registration and/or approval, the relevant legal provisions shall apply (Article 87).

[6-31] The combined transfer may also be effected by operation of law. Here, Article 90 of the CL addresses a common situation of combined transfer resulting from the merger or division of a party to the contract after the contract's conclusion. The general rule is that the existing contractual rights and obligations continue to apply to the legal successor of the original contracting party after the merger or division. An underlying goal is to promote the stability and security of transactions, as a party to the contract cannot attempt to evade its obligations by restructuring its business organisation.

[6-32] Under Article 90, where a contracting party has merged after the contract has been concluded, the legal person or other organisation established after the merger shall exercise the contractual rights and perform the contractual obligations. Where there has been a division of a party's business entity after the contract's conclusion, the legal persons or other organisations arising from the division shall jointly enjoy the rights as well as assume joint liability for the obligations under the contract, unless otherwise agreed upon by the debtor and creditor.

[6-33] Since the combined transfer in these circumstances arises from the operation of law, it does not require the consent of the other party. There are statutory provisions in the Company Law that require a company to give notice to its creditors and issue a public announcement within set timeframes after the company makes the decision regarding the merger or division.[32] Consistent with the CL, the Company

32 Company Law of the People's Republic of China (2013 Revision)《中华人民共和国公司法（2013 修正）》, adopted at the fifth session of the Standing Committee of the National People's Congress on 29 December 1993, revised in 1999, 2005, and 2013, Arts 173, 175.

agreement. For example, the agreement could be in written, oral, or other form unless particular laws or administrative regulations require it to be in writing.[1] The agreement must be made voluntarily and reflect the parties' true intention.[2]

[7-4] The second option under Article 93 is where the parties stipulate the conditions under which either party may dissolve the existing contract. For example, the parties may agree on the specific types of breaches or other circumstances that give rise to this right. Upon fulfillment of the conditions, the party with the right to dissolve the contract may do so. Article 93 does not refer to the possibility that the parties can agree to confer upon one party an unconditional right to dissolve the contract. Such a contractual term would be enforceable and subject to the general provisions and principles of the CL, including the principle of good faith.[3]

[7-5] An agreed condition in relation to a party's right to dissolve a contract under Article 93 is distinct from the concept of a 'condition subsequent' under Article 45 of the CL. Where there is a condition subsequent, the contract ceases to be effective upon the fulfillment of that particular condition. Any performance that the parties have already rendered is unaffected by the materialisation of the condition subsequent that brings the contract to an end. In comparison, if the condition for the exercise of the right to termination is fulfilled, the contract does not automatically come to an end unless the party with the right to dissolve the contract chooses to exercise such a right. Also, the parties may seek a claim for restitution of any performance rendered under the contract.

7.3 Statutory Grounds for Dissolution of Contract

[7-6] Dissolution of a contract can be an extremely powerful remedy for the aggrieved party to exercise in circumstances where the other party's breach makes the purpose of the contract impossible to achieve or where the other party unreasonably delays performance. The right of dissolution release the aggrieved party from future performance of the contract, preserves its claim for damages and other remedies arising from the defaulting party's liability for breach, and allows for restitution of performance that it has already rendered. However, a party purporting to dissolve the contract when such a right may not actually exist runs the risk of the other party claiming damages due to wrongful termination.

[7-7] Article 94 of the CL provides a list of circumstances in which contracting parties may exercise the right to dissolve a contract:

(1) the purpose of contract is rendered impossible to achieve due to an event of force majeure;
(2) prior to the expiration of the period of performance, the other party expressly states, or indicates through its conduct, that it will not perform its main obligation;

1 CL, Art 10.
2 CL, Art 4.
3 Ling, 336.

(3) the other party delays performance of its main obligation after such performance has been demanded, and fails to perform within a reasonable period;
(4) the other party delays performance of its obligations, or breaches the contract in some other manner, rendering it impossible to achieve the purpose of the contract;
(5) other circumstances as provided by law.

7.3.1 *Force majeure* and change of circumstances

7.3.1.1 *Force majeure*

[7-8] Under Article 94(1), a party is entitled to dissolve a contract in the event of *force majeure* (*buke kangli*) that frustrates the purpose of the contract. Article 117 further defines *force majeure* as 'any objective circumstances which are unforeseeable, unavoidable and insurmountable'. In other words, the occurrence of force majeure must be an objective circumstance that is beyond the control of the non-performing party. The event could not have been foreseen at the time the contract was concluded. It could not have been avoided even if the parties had made arrangements in advance. Finally, the event could not be overcome when it occurred. All three elements must be present. In Chapter 8, we will further discuss *force majeure* as a ground for exemption from liability for breach and the mitigation of loss under Articles 117 and 118 of the CL.

[7-9] Natural disasters such as earthquakes, hurricanes, floods, and droughts, as well as abnormal social or man-made events such as wars, acts of terrorism, and social unrest would be typically regarded as 'unforeseeable, unavoidable, and insurmountable' occurrences. Amendments or changes in relevant laws and government policies after the conclusion of the contract are less likely to meet the definitional threshold of *force majeure*. In practice, courts have often treated such cases with reference to the doctrine of 'change of circumstances', which we will examine below.

[7-10] It should be highlighted that the occurrence of an event of *force majeure* is not enough to trigger the statutory right to dissolve contract under Article 94(1). A party can only rely on this provision where the occurrence of such an event renders the purpose of the contract impossible to accomplish. A party may not dissolve the contract on the basis of Article 94(1) if it has assumed the risk of *force majeure* under the parties' agreement, commonly through a *force majeure* clause in the contract.

[7-11] Article 94(1) does not clarify which party has the right to dissolve the contract. A literal interpretation of Article 94, which refers to 'the parties', would suggest that both parties possess this right. However, given that Article 94(1) provides a lawful excuse for the debtor not to perform its contractual obligations and the debtor may only be partially excused under Article 117 (in relation to liability for non-performance) due to *force majeure*, a suitable interpretation is that only the aggrieved party has the right to dissolve the contract in this situation.[4]

4 ibid, 344.

7.3.1.2 Change of circumstances

[7-12] The doctrine of 'change of circumstances' is found in numerous civil law systems and serves a similar function as the common law concept of frustration. The doctrine applies to a situation where an unforeseeable event occurs after the contract's formation, giving rise to significant impediments to performance. The changed circumstances may, in some cases, frustrate the purpose of the contract. In other cases, even if performance is not impossible, maintaining the original contract in light of the changed circumstances would be contrary to the principles of good faith and fairness. In comparison to the CISG (which adopts a unified regulatory approach to *force majeure* and change of circumstances), Chinese contract law draws a distinction between the two concepts.[5]

[7-13] There is no specific statutory provision in the GPCL or CL recognising 'change of circumstances'. The concept was originally found in the earlier drafts of the CL but was ultimately excluded from the final legislation. The doctrine is now found in Article 26 of the SPC Interpretation II:

> Where any major change in the objective environment has taken place after the formation of a contract which could not have been foreseen by the parties at the time of entering into the contract, and is not a commercial risk and is not occasioned by *force majeure*, rendering the continuous performance of the contract evidently unfair to the other party or rendering it impossible to realise the purpose of the contract, the People's Court shall decide whether to vary or rescind contract in accordance with the principle of justice taking into account the actual circumstance, where a relevant party petitions a People's Court to vary or dissolve the contract.

[7-14] The above provision distinguishes 'change of circumstances' and 'commercial risks'. The distinction is important since the doctrine is not intended for the court to intervene in a 'bad bargain' between the parties who must assume certain commercial risks when entering into transactions. The parties can reasonably anticipate commercial risks that are inherent in business activities. For example, normal fluctuations in the market price would not be considered as change of circumstances, but a commercial risk.

[7-15] It is difficult to ascertain whether the principle would apply to a major economic crisis that the parties could not have foreseen. We should keep in mind that the SPC Interpretation II was introduced against the background of a global financial crisis and an economic downturn in China. There were a growing number of related contractual disputes as many businesses found it increasingly difficult to perform the contracts they had entered into before the crisis. One could argue that the development of this doctrine based on Article 26 would increase the discretion of courts to undermine the stability of transactions by allowing a party to 'exit' from a loss-making commercial contract. Moreover, the potential reach of this doctrine could significantly encroach on the fundamental principle of *pacta sunt servanda*.

5 Shiyuan Han, 'Force Majeure, Change of Circumstances and Termination of Contract' (2016) 3 Journal of Law, Society and Development 31.

[7-16] Nevertheless, the SPC has issued a guiding opinion alongside the SPC Interpretation II, which directs local courts to apply the doctrine prudently to protect the interests of parties and strictly review applications for modifying or terminating contracts on such basis.[6] In this guiding opinion, the SPC sets out the standard for interpreting whether or not the major change in the objective environment was 'unforeseen':

> Commercial risks are inherent in business activities, such as changes in supply and demand and price changes not reaching the level of abnormal changes. The change of situation is not a risk that is inherent in the market system and cannot be foreseen by the parties when they entered into a contract. When deciding whether a major objective change is a change of situation, the people's court shall take into account such factors as whether the type of risk is one unforeseeable in the common sense, whether the degree of risk is far beyond the reasonable expectation of a normal person, whether the risk can be prevented and controlled and whether the nature of transaction falls within the usual scope of 'high risk and high return', and distinguish between the change of situation and commercial risks in the specific cases in combination with the specific situation of the market.[7]

[7-17] It can be seen that the SPC has sought to impose some limitations on the scope of 'change of circumstances'. As the following cases illustrate, the courts have generally taken a cautious case-by-case approach in determining whether the parties could have foreseen a particular event.

Illustrative case: *Shanghai Tongzai Industrial Co Ltd v Far East Cable Company Ltd*[8]

In December 2007, the appellant and respondent entered into a futures contract whereby the appellant provided raw materials (copper cathode) and related services for the respondent's production and operations. The parties agreed that the settlement price would be based on the offer/asking price of copper futures contracts of the Shanghai Futures Exchange. After the conclusion of the original contract, the parties entered into a series of supplementary agreements throughout 2008. The dispute arose due to the drastic fall of the price of copper in international markets and the respondent's refusal to fulfill the remaining payment obligations.

On the issue of whether the drastic decrease in copper price constituted change of circumstances, the court pointed to numerous price fluctuations in the price chart of copper on the Shanghai futures market during the period of 2004–2011. It concluded that the appellant and respondent agreed that the

6 Guiding Opinions of the SPC on Contracts under the Current Situation.

7 ibid, Art 3.

8 上海同在国际贸易有限公司与远东电缆有限公司买卖合同纠纷案, 最高人民法院民事判决书（2011）民二终字第 55 号.

the contract pricing would be in reference to the Shanghai Futures Exchange offer price and should have anticipated the business risks associated with the price volatility of the non-ferrous metals futures market (given the lively nature of this market). During certain periods of 2009, the price of copper in fact rose and the price trend was favourable to the respondent. The price fluctuations are an inherent risk of commercial activity. The SPC further reiterated that the global financial crisis and the general economic situation in China represent a gradually evolving process, during which market participants should still be able to foresee and estimate market risks to a certain extent. In this case, the price fluctuation due to the global financial crisis and economic downturn was foreseeable and fell within the category of commercial risk. The principle of change of circumstances did not apply here.

[7-18] Unlike *force majeure*, the doctrine of change of circumstances does not require the event in question to be unavoidable and insurmountable. Moreover, one of the effects of change of circumstances is that continuous performance of the contract would be evidently unfair to the other party. However, the abovementioned rules do not address the situation where an event of *force majeure* results in evident unfairness between the parties but does not frustrate the purpose of the contract or render performance impossible. Article 26 of the SPC Interpretation II makes it clear that a change of circumstance can not be due to an event of *force majeure*. Nevertheless, it has been observed that courts, in practice, have incorporated such a situation within the scope of change of circumstances.[9]

Illustrative case: *People's Government of Yongxiu County of Jiangxi Province and Office of the Leading Group for the Administration of Sand Mining of Poyang Lake, Yongxiu County v Chengdu Pengwei Industry Co Ltd*[10]

The respondent through auction had acquired the sand mining rights in the Yongxiu County section of Poyang Lake and entered into a contract with the appellant. In performing the contract, the respondent encountered a rare occurrence of low water level, which had not taken place for 36 years. The low water level made it impossible for the sand dredgers to continue operations in the sand mining lots. The sand mining operations ended earlier than expected and the purpose of the contract could not fulfilled. The respondent incurred significant losses as a result and applied to the court, requesting a partial refund of the contract price from the appellant on the basis of change of circumstances.

9 Chunyan Ding, 'Pespectures on Chinese Contract Law: Performance and Breach', in DiMatteo and Chen, 320.

10 江西省永修县人民政府、永修县鄱阳湖采砂管理工作领导小组办公室与成都鹏伟实业有限公 司采矿权纠纷案，最高人民法院民事判决书（2011）民再字第 2 号.

The SPC held that the objective change of situation in this case was unforeseeable to both parties when the contract was concluded and the respondent's losses were not caused by a commercial risk. Under such circumstances, continuing to perform the contract would necessarily lead to the result that the appellant obtained all the benefits under the contract while the respondent suffered all investment losses. Such a scenario would be unfair to the respondent and contrary to the basic principles of the CL. The court highlighted that fairness was a basic principle that must be followed by the parties in concluding and performing a contract. The respondent's request for a partial refund of the contract price was an application to the court for modifying the contractual terms and conditions. The request was in accordance with the provisions of the CL and the court's judicial interpretation and should be supported.

7.3.2 Anticipatory repudiation

[7-19] Article 94(2) of the CL allows the aggrieved party to dissolve a contract whereby before the time for performance is due, the repudiating party clearly indicates through words or conduct, that it will not perform its principal or main obligation under the contract. Anticipatory repudiation does not, of itself, bring about the dissolution of the contract. The aggrieved party may choose to exercise the right to dissolve the contract in this situation. Alternatively, the aggrieved party may choose to disregard the repudiation, treat the contract as continuing, and insist on performance by the repudiating party.

[7-20] A key requirement of Article 94(2) is that the repudiating party evinces an intention not to perform its principal contractual obligation. Therefore, the repudiation of a minor or accessory obligation would not trigger this statutory provision. What constitutes a 'principal obligation' depends on the nature and purpose of the contract and is subject to the construction of relevant contractual terms.

[7-21] A related provision is Article 108 of the CL, which grants the aggrieved party the right to demand that the repudiating party bear liability for breach before performance is due. As we will examine in greater detail in the next chapter, liability under Article 108 arises where a party declares explicitly or indicates by its conduct that it will not perform its contractual obligations. Unlike Article 94(2) which gives rise to the aggrieved party's right to dissolve the contract, liability for anticipatory breach under Article 108 does not need to concern a principal obligation.

[7-22] There are some notable differences between the defence of insecurity (which we have examined in Chapter 5) and anticipatory repudiation. Articles 68 and 69 of the CL allow the first performing party to suspend performance of its obligations under a bilateral contract where it has conclusive evidence that the other party has lost or is likely to lose the ability to perform. The first performing party is entitled to dissolve the contract where the other party fails to regain the ability to perform and provide appropriate security within a reasonable time.

[7-23] On the other hand, anticipatory repudiation involves an explicit statement or indicative conduct by the repudiating party that it does not intend to fulfill its

main obligations. In this sense, anticipatory repudiation focuses on the expression or manifestation of the repudiating party's intent not to perform. Moreover, either party may engage in anticipatory repudiation that gives rise to the aggrieved party's right to dissolve the contract and/or claim for liability for breach. It does not matter which party is obliged to perform first, unlike the defence of insecurity.

[7-24] Anticipatory repudiation would be more applicable in some circumstances than the defence of insecurity, and vice-versa. Since the defence of insecurity allows the first performing party to suspend its performance, such a defence would be meaningless for the said party if it has already performed its obligations. It would be appropriate to claim anticipatory repudiation in this situation. On the other hand, where the first performing party could definitively demonstrate the circumstances in which the other party *may* lose the ability to perform but could not prove that the other party has clearly indicated it will not perform its obligations, the defence of insecurity would be more suitable. If both legal grounds are applicable in cases involving non-performance of principal obligations, a party may prefer to rely on Article 94(2) which allows the party to dissolve the contract without waiting for the other party to perform or provide security within a reasonable time.[11]

[7-25] Some scholars have adopted a broad understanding of the scope of anticipatory breach under Article 94(2) and Article 108 as including the repudiating party's anticipatory refusal to perform as well as its anticipatory inability to perform. As Professor Ding argues, such an approach 'better achieves two intended functions' of anticipatory repudiation, namely: to release the aggrieved party from the contract as soon as possible where the contract's purpose fails because of the repudiation and to avoid unnecessary delay for the aggrieved party to claim remedial measures under Article 107 of the CL.[12]

[7-26] The notion of anticipatory repudiation can be found in common law systems, while the defence of security has its origins in civil law systems. The adoption of both concepts in the CL has been subject to criticism. For example, Professors DiMatteo and Wang assert that 'this bifurcation serves no reasonable purpose and has caused much confusion and debate',[13] pointing to the conflation of the two concepts in judicial practice.[14] However, others have noted the complementary nature of the two legal doctrines in offering parties 'with alternative legal solutions to situations where it becomes evident that the debtor will either fail or likely fail to provide the promised performance'.[15]

7.3.3 Delayed performance

[7-27] There are two situations where delayed performance of obligations by one party can trigger the other party's right to dissolve the contract under

11 Ding (n 9) 316–217.
12 ibid, 309.
13 Larry A DiMatteo and Jingen Wang, 'CCL and CISG: A Comparative Analysis of Formation, Performance, and Breach' in DiMatteo and Chen, 466–500, 494.
14 ibid, 494–496.
15 Ding (n 9) 322.

Article 94 of the CL. It is apparent that a delay in performance can only occur when the time for performance has expired. Moreover, the delay in question must not have been caused by the impossibility of performance. In other words, the obligor was able and willing to perform the obligations before the expiry of the performance period but failed to do so without a legitimate excuse.

[7-28] The first situation of delayed performance is addressed under Article 94(3), which reflects the German concept of *Nachfrist* (*kuanxianqi*). Here, the aggrieved party does not have the right to unilaterally dissolve the contract when the other party has delayed its performance of the main obligation. In order to exercise such a right, the aggrieved party must have notified the other party with a demand for performance within a reasonable period and the other party had failed to comply with the demand upon the expiry of the additional time given for performance. A reasonable period of additional time would depend on the nature and circumstances of the particular transaction. This procedure effectively allows an aggrieved party to dissolve the contract without needing to show that the delay in performance frustrated the purpose of the contract (which is required under Article 94(4)). Nonetheless, the delay in question must still relate to the performance of a principal or main obligation.

[7-29] The second situation of delayed performance, addressed under Article 94(4) of CL, applies to delayed performance that makes it impossible to achieve the purpose of the contract. As such, this type of delay can be conceptualised as fundamental non-performance and is likely to arise where the timing of the performance is essential to the contract and any delay in performance renders the contract meaningless.[16] In this case, there is no need to demand the other party's performance and provide additional time, since the delay itself would give rise to the aggrieved party's right to dissolve the contract.

7.3.4 Fundamental non-performance

[7-30] Article 94(4) gives the aggrieved party a statutory right to dissolve the contract where the other party has breached the contract in some other manner (besides delay in performance) that makes it impossible to accomplish the purpose of the contract. Besides the requirement that the breach in question frustrates the purpose of the contract, there is no further clarification as to the types of breaches that would fall within the scope of Article 94(4). It should be noted that special laws and regulations may specify certain types of breach that would trigger a party's right to dissolve a contract.

[7-31] The general type of breach under Article 94(4) is commonly regarded as fundamental non-performance (*genben weiyue*). The CISG defines a case of non-performance or breach as fundamental if 'it results in such detriment to the other party as substantially to deprive him of what he is entitled to expect under the contract, unless the party in breach did not foresee and a reasonable person of the same kind in the same circumstances would not have foreseen such result'.[17] This definition points to two key elements of substantial detriment and reasonable

16 Zhang, 266.
17 CISG, Art 25.

foreseeability. Meanwhile, the UNIDROIT Principles list a number of factors in determining whether the non-performance of an obligation is 'fundamental', that is, 'material and not merely of minor importance'.[18]

[7-32] Professor Ling has identified a number of useful consideration to take into account when determining a fundamental breach under the CL:[19]

(a) whether the parties entered into contract for a particular purpose;
(b) whether the unperformed obligation was key to accomplishing the parties' expected interests under the contract;
(c) the extent to which the wrongdoing party has performed any part of the contract;
(d) the extent of detriment to the aggrieved party as a consequence of the breach;
(e) the willingness and ability of the wrongdoing party to cure its breach;
(f) whether it is a contract involving personal confidence between the parties;
(g) whether the breach is intentional or grossly negligent;
(h) the desirability and viability of further performance.

[7-33] In order to rely on Article 94(4) to dissolve a contract, the aggrieved party purporting to exercise such a right must show that the other party's delay in performance or breach of its obligations renders it impossible to achieve the purpose of the contract. As the following case demonstrates, it is not always easy for the aggrieved party to prove that the breach in question meets the threshold of fundamental non-performance. Wrongful dissolution could give rise to liability for breach of contract by the party purporting to rely on Article 94(4) and potentially constitute a fundamental non-performance in itself.

Illustrative case: *Ningxia Dongling Real Estate Development Ltd v Sunbo and Sun Jiangong*[20]

The appellant and respondent entered into several contracts for the sale and purchase of commercial properties. The respondent (purchaser) fulfilled 72.24% of his payment obligations in relation to the total purchase price. He failed to pay the remaining balance on time in accordance with the contract. Consequently, the appellant purported to dissolve the contracts on the basis of Article 94(4) of the CL.

The SPC held that the appellant did not have the right to dissolve the contract on the ground of Article 94(4). In this case, the respondent's delay in paying the remaining balance did not constitute a delay in performance that rendered it impossible to achieve the purpose of the contract. In the first instance trial, the respondent had offered to pay the remaining balance to the appellant, but the appellant refused to accept it. The respondent's actions indicated that it had the intention and capacity to perform its contractual obligations. The court reasoned that the appellant should have demanded the respondent to bear liability for breach of contract and compensate the appellant for any losses. However, the appellant did not satisfy the statutory requirement for the right to dissolve the contract.

18 See UNIDROIT Principles, Art 7.3.1 and Official Commentary.
19 Ling, pp 340–344.
20 宁夏东灵房地产开发有限公司与孙波、孙建功房屋买卖合同纠纷抗诉再审案，最高人民法院民事判决书（2014）民抗字第 46 号.

7.3.5 Termination for other reasons provided by law

[7-34] Article 94(5) serves as a 'catch-all' provision for other circumstances that may provide grounds for the lawful termination of a contract. For example, Article 69 of the CL provides the party invoking the defence of insecurity a right to terminate the contract where the other party is unable to regain its ability to perform and fails to provide adequate security within a reasonable period.

[7-35] In relation to specific contracts, the special provisions of the CL provide additional rules regarding the right of termination. For example, in sales contracts involving the delivery of the subject matter in instalments, where the seller fails to deliver an instalment or the delivery fails to comply with the contract so that the delivery of subsequent instalments cannot realise the contract's purpose, the buyer can terminate the portion of the contract in respect of that instalment and subsequent instalments.[21] In the context of lease contracts, the lessor may terminate the contract and claim damages where damage to the lease item was caused by the lessee's failure to use it in the agreed manner or in a manner consistent with its nature.[22] If the lessee subleases the item without its consent, the lessor may terminate the contract.[23] These rules essentially reflect the application of the 'fundamental breach' principle that entitles the aggrieved party to terminate the contract.

[7-36] Beyond the CL, there is a wide range of specialist regulatory regimes covering different contracts, such as labour contracts, property sales contracts, insurance contracts, guarantee contracts, maritime contracts, etc. When dealing with such contracts, it is important to identify and examine the special provisions governing the right of termination in that particular context, which may differ considerably from the principles and rules found in the CL. As a general legal principle in Chinese law, where there is inconsistency between special provisions and general provisions, the special provisions shall prevail.[24]

7.4 Procedural Aspects and Effect of Termination

7.4.1 Time limit for exercising the right to terminate

[7-37] The exercise of the right of termination can be subject to certain time limits. A party's failure to exercise this right within the time limit can result in the

21 CL, Art 166.
22 CL, Art 219.
23 CL, Art 224.
24 Legislation Law of the PRC (2015 Revision), Art 92.

loss of the right. The purpose of this rule, as articulated in Article 95 of CL, is to preserve certainty and stability in transactions.

[7-38] Where the law stipulates or the parties have agreed on a period of time for the exercise of the right of termination, the right shall be extinguished when the party does not exercise it upon the expiry of the period. If there is no legal provision or agreement on such a time limit, the right shall be extinguished when the party does not exercise it within a reasonable time period after receiving the other party's demand. What constitutes a 'reasonable time period' would depend on the circumstances of each case. Once a party has lost its right to terminate the contract, it must perform its obligations under the contract in the absence of other legitimate defences.

Illustrative case: *Tianjin Tianyi Industry & Trading Co Ltd v Tianjin Binhai Commerce & Trading World Co Ltd (Third party: Wang Xifeng)*[25]

On 8 March 2004, the appellant and respondent signed a commercial building transfer agreement. Under the agreement, the appellant would pay the respondent a down payment of 34 million yuan for the properties transferred. On 11 July 2005, the appellant and respondent signed a supplementary agreement with a third party, Wang Xifeng. All parties agreed to change the procedures of purchase, mortgage, and ownership transfer in Wang's name. The supplementary agreement further stated that the appellant and Wang would be responsible for handling the mortgage loan on their own and the remaining balance of 51 million yuan was to be paid within thirty days of the contract's conclusion. The appellant and Wang failed to fulfil their contractual obligations. On 18 December 2005, the appellant issued a 'circular' to the respondent stating that it did not agree to pay the 34 million yuan (down payment) to Wang personally and it could not obtain the mortgage to pay the remaining amount within the agreed time limit. In the 'circular', the appellant proposed the dissolution of the contract.

On 28 June 2006, the respondent filed a lawsuit, requesting the dissolution of the original transfer agreement and the supplementary agreement. At the first and second instance trials, the courts supported the respondent's request. The appellant appealed to the SPC, seeking a retrial. One of the appellant's main arguments was that based on a provision in the SPC's Interpretation regarding Commodity Housing Contracts, the respondent did not exercise the right of dissolution within three months after the appellant had issued the 'circular'. Accordingly, the respondent lost its right to dissolve the contract before the trial.

The SPC rejected the appellant's argument. The court stated that the SPC's Interpretation regarding Commodity Housing Contracts did not apply to the type of transaction in this case. The court further stated that a party's right to dissolve a contract is extinguished upon the expiry of the time limit for exercising such a right. The determination of the relevant time limit has a significant impact on the parties' rights and obligations. The court referred

25 天津市天益工贸有限公司与天津市滨海商贸大世界有限公司、王锡锋财产权属纠纷案, 最高人民法院民事裁定书（2012）民再申字第 310 号.

to Article 95 of the CL, which stipulates that if the law or the parties have not agreed upon a time limit to exercise the right to dissolve the contract, the said right is extinguished within a reasonable period after being urged by the other party. The court shall determine a 'reasonable period of time' with reference to the specific facts of the case.

In this case, the dissolution of the contract involved numerous considerations beyond the parties' rights and obligations, such as issues relating to the transfer of assets and tenants (since the appellant had already started collecting rent from tenants of the building). Furthermore, the appellant had only proposed to negotiate with the respondent to dissolve the contracts. The respondent would need sufficient time to inquire into whether it should dissolve the contracts. Finally, after issuing the 'circular', the appellant neither performed its payment obligations under the contract nor expressed its willingness to continue performing the contract. Taking these facts on the whole, the SPC decided that the respondent did not exceed a 'reasonable period of time' in filing a lawsuit in June 2006 to dissolve the contract.

7.4.2 Notice and other procedures

[7-39] A party exercising the right to dissolve the contract in accordance with the parties' agreement or any of the statutory grounds under Article 94 must notify the other party. Pursuant to this rule in Article 96, the contract shall be dissolved when the notice reaches the other party, that is, when it arrives in the place under the control of the other party. In other words, the dissolution of the contract takes effect upon the receipt of the notice by the other party, unless special provisions apply otherwise. The notice cannot be revoked once it is received. There is no requirement that the notice must be in writing.

[7-40] Article 96 provides the other party with the opportunity to object to the dissolution of the contract. The other party may petition the court or an arbitration institution to adjudicate on whether the dissolution was effective. However, it will lose its entitlement to object if it lodges a lawsuit after the expiration of any agreed time limit for raising objections. If the parties have not agreed on the time limit for raising objections, the party must lodge the lawsuit within three months after the day when the notice of dissolution is served on the party. The court will not accept such a lawsuit beyond the three-month limit.[26]

[7-41] Article 96 further stipulates that where the laws and administrative regulations so provide, the approval and registration procedures for dissolving the contract shall be carried out in accordance with such laws and regulations. The dissolution will not be effective if these mandatory procedures have not been undertaken, although the parties have until the end of the court hearing in the first instance trial to complete the relevant registration or approval formalities.[27]

26 SPC Interpretation II, Art 24.
27 SPC Interpretation I, Art 9.