

China Insight



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## Overview on Key Issues of the Contract Part of China's First Civil Code

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The People's Republic of China's ("PRC") first combined codification of the civil law ever, i.e. the PRC Civil Code ("**PRC Civil Code**") which was adopted on 28 May 2020 and which will enter into effect on 1 January 2021, consists of 7 Parts and supplementary provisions. The Part on Contracts constitutes Part III of the *PRC Civil Code* and consists of 3 Subparts, i.e. General Rules, Typical Contracts and Quasi Contracts, in 29 chapters and 526 clauses in total.

### 1. Introduction

The Part on Contracts is mainly based on the current *PRC Contract Law* first effective as of 1 October 1999, however, it includes quite a few new provisions (i.e. 526 provisions in the *PRC Civil Code* compared to 428 provisions in the current *PRC Contract Law*). Concurrently with the entering into effect of the *PRC Civil Code*, the *PRC Contract Law* will cease to be effective on 1 January 2021.

- a) Subpart I, same as in the *PRC Contract Law*, prescribes general rules on contracts. This Subpart is further divided into 8 chapters, i.e.:
  - (1) Chapter I General Provisions;
  - (2) Chapter II Conclusion of Contracts;
  - (3) Chapter III Effectiveness of Contracts;
  - (4) Chapter IV Performance of Contracts;
  - (5) Chapter V Preservation of Contracts;
  - (6) Chapter VI Modification and Assignment of Contracts;
  - (7) Chapter VII Termination of Contractual Rights and Obligations; and
  - (8) Chapter VIII Liability for Breach of Contract.
  
- b) Subpart II sets forth more detailed rules for 19 types of "typical contracts", i.e.:
  - (1) Chapter IX Sales Contracts;
  - (2) Chapter X Contracts for the Supply and Consumption of Electricity, Water, Gas or Heat;

- (3) Chapter XI Donation Contracts;
- (4) Chapter XII Loan Contracts;
- (5) Chapter XIII Guarantee Contracts;
- (6) Chapter XIV Lease Contracts;
- (7) Chapter XV Financial Leasing Contracts;
- (8) Chapter XVI Factoring Contracts;
- (9) Chapter XVII Contracts for Works;
- (10) Chapter XVIII Construction Project Contracts;
- (11) Chapter XIX Transportation Contracts;
- (12) Chapter XX Technology Contracts;
- (13) Chapter XXI Deposit Contracts;
- (14) Chapter XXII Warehousing Contracts;
- (15) Chapter XXIII Commission Contracts;
- (16) Chapter XXIV Property Service Contracts;
- (17) Chapter XXV Brokerage Contracts;
- (18) Chapter XXVI Intermediary Contracts; and
- (19) Chapter XXVII Partnership Contracts.

- c) Subpart III newly provides for stipulations on the following legal principles:
  - (1) Chapter XXVIII Agency without Authority (*Gestio Negotiorum*); and
  - (2) Chapter XXIX Unjust Enrichment.

Please find below a comparison of some key provisions of the *PRC Civil Code* and the relevant, currently-effective laws, i.e. mainly the *PRC Contract Law*, as well as regulations and judicial interpretations of the PRC Supreme People’s Court (“SPC”).

**2. Key Aspects in Chapter I, General Rules**

**a) Applicability**

<b>PRC Contract Law</b>	<b>PRC Civil Code</b>
/	<b>Article 468</b> For a creditor-debtor relation not arising from a contract, the provisions of the law on such a creditor-debtor relation shall apply; or in the absence of such provisions, the relevant provisions of the General Rules of this Part shall apply, unless its nature precludes the application.

<p><b>Article 126</b> Parties to a foreign related contract may select the applicable law for resolution of a contractual dispute, except otherwise provided by law. Where parties to the foreign related contract failed to select the applicable law, the contract shall be governed by the law of the country with the closest connection thereto.</p> <p>For a Sino-foreign Equity Joint Venture Enterprise Contract, Sino-foreign Cooperative Joint Venture Contract, or a Contract for Sino-foreign Joint Exploration and Development of Natural Resources which is performed within the territory of the People's Republic of China, the law of the People's Republic of China applies.</p>	<p><b>Article 467</b> [...] Contracts for Sino-foreign joint ventures, Sino-foreign contractual joint ventures and Sino-foreign cooperative exploration and development of natural resources which are performed within the territory of the People's Republic of China, shall be governed by the laws of the People's Republic of China.</p>
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Article 468 of the *PRC Civil Code* clarifies that, in the absence of special regulations on non-contractual creditor-debtor relationships, generally, the ones of Part III, Contracts, Subpart I, General Rules of the *PRC Civil Code* shall apply accordingly.

Article 126, paragraph 1, of the *PRC Contract Law* dealing with choice of law for foreign-related contracts and what law applies in the absence of a choice of law has not been transferred to the *PRC Civil Code*. Actually, this is not necessary, since these questions are already comprehensively dealt with in the *PRC Law on the Application of Laws to Foreign-related Civil Relations* ("**PRC IPR**") effective since 1 April 2011.

However, Article 126, paragraph 2, of the *PRC Contract Law* has been transferred into Article 467, paragraph 2, of the *PRC Civil Code* and it is still clarified that contracts regarding Sino-foreign joint ventures as well as Sino-foreign cooperative explorations and developments of natural resources within the PRC remain mandatorily governed by PRC law. Such clarification is necessary, since the *PRC IPR* does not deal with this issue and since the special laws and implementing regulations on Sino-foreign joint ventures, which provided for respective stipulations, have been abolished since 1 January 2020. Interestingly, the *PRC Civil Code* still expressly refers to Sino-foreign contractual joint ventures, although the special rules and regulations on Sino-foreign contractual joint ventures have been abolished since 1 January 2020 concurrently with the entering into effect of the *PRC Foreign Investment Law*. Thus, actually, there is no legal basis anymore for Sino-foreign contractual joint ventures and the related reference in the *PRC Civil Code* appears unnecessary.

b) **Contracts Subject to Approval or Other Procedures**

<b>SPC Interpretation on Disputes Involving Foreign-funded Enterprises (I)</b>	<b>PRC Civil Code</b>
<p><b>Article 1</b> In instances where any law or administrative regulation prescribes that a contract shall not come into effect until being approved by the approval authority for foreign-funded enterprises if concluded during the process of establishment of or alteration made by a foreign-funded enterprise, or pending matters related to a foreign-funded enterprise, the People's Court shall uphold that such contract has not come into effect where no such approval has been granted. Where the concerned parties apply for recognition of the invalidity of the contract, the People's Courts shall deny such application.</p> <p>In instances where the aforesaid contracts are deemed invalid due to their failure of being approved, it shall not affect the validity of the relevant clauses which the parties to the contract conclude concerning their obligations of submission for approval and other clauses created due to the obligation to submit for approval.</p>	<p><b>Article 502</b> [...] With regard to contracts for which approval or other procedures shall be completed according to provisions of laws or administrative regulations, such provisions shall govern. Where non-performance of approval or other procedures affect the coming-into-force of such a contract, it shall not affect the validity of clauses relating to the performance of obligations such as submission for approval and the relevant clauses in the contract. Where the party that shall apply for approval fails to perform its obligations, the other party may request it to assume liability for breach of the obligations.</p> <p>[...]</p>

Article 502 of the *PRC Civil Code*, to quite a large extent, follows Article 1 of the *Provisions of the Supreme People's Court on Several Issues Concerning the Hearing of Cases about Disputes Involving Foreign-funded Enterprises (I)* ("**SPC Interpretation on Disputes Involving Foreign-funded Enterprises (I)**") and affirms the independence of the provisions of the approval obligation and related provisions. It also clarifies that where non-performance of approval or other procedures affect the coming-into-effect of a contract, this shall not affect the validity of clauses relating to the performance of obligations, such as submission for approval, and the relevant clauses in the contract. However, Article 8 of the *Interpretation of the Supreme Court on Certain Issues Concerning the Application of the PRC Contract Law (II)* ("**SPC Interpretation on PRC Contract Law (II)**") stipulates relevant consequences as that a "People's Court may order the opposite party to independently go through the relevant procedures based on the specific circumstances of the case and at the request of the opposite party" and that the "other party shall be liable for compensation for the resulting expenses and the actual losses incurred by the opposite party" only. In contrast to a mere "compensation for the resulting expenses and the actual losses incurred", Article 502 of the *PRC Civil Code* now stipulates that "where the party that shall apply for approval fails to perform its obligations, the

*other party may request it to assume liability for breach of the obligations", which potentially is more extensive and provides for further protection of the affected party. However, the actual implementation of Article 502 of the PRC Civil Code in practice remains to be seen.*

**c) Conclusion of Contracts**

PRC Contract Law	PRC Civil Code
<p><b>Article 13</b> The parties shall conclude contracts in the manner of offer and acceptance.</p>	<p><b>Article 471</b> The parties shall conclude contracts in the manner of offer and acceptance <i>or otherwise</i>.</p>
<p><b>Article 25</b> A contract is established when the acceptance becomes effective.</p>	<p><b>Article 483</b> A contract is established when the acceptance becomes effective, <i>unless otherwise stipulated by the law or agreed between the parties</i>.</p>

The current *PRC Contract Law* only provides for the conclusion of contracts through offer and acceptance. Article 471 of the *PRC Civil Code*, however, adds "or otherwise". Yet, such other methods to conclude contracts are not further specified in the *PRC Civil Code* and it remains to be seen whether this has any practical implications and, if so, what these implications are.

Article 483 of the *PRC Civil Code* stipulates that contracts can be established by other means than an acceptance becoming effective, if stipulated by law or agreed between the parties. For example, if two parties have orally reached an agreement by offer and acceptance, but also agreed that the agreement shall be in writing before it is established, a contract will only be established from the time when each party signs, seals or affixes its fingerprint to the contract document in accordance with Article 490 of the *PRC Civil Code*.

**d) Conclusion of and Time of Delivery regarding Electronic Contracts**

PRC Contract Law	PRC E-commerce Law	PRC Civil Code
<p><b>Article 33</b> Where the parties conclude a contract in the form of a letter, electronic message or otherwise, they may require that a letter of confirmation be signed before the conclusion of the contract. The contract shall be established when the letter of confirmation is signed.</p>	<p><b>Article 49</b> Where the information on any commodity or service released by an e-commerce operator meets the conditions of an offer, and a client selects the said commodity or service and successfully submits an order, a contract is concluded. If the parties concerned have any other agreement in this regard, such agreement shall prevail.</p>	<p><b>Article 491</b> Where the parties conclude a contract in the form of a letter, electronic message or otherwise and require that a letter of confirmation shall be signed, the contract is established when the letter of confirmation is signed.</p> <p><i>Where the information on any commodity or service published by a party via the Internet or any other</i></p>

	[...]	<i>information network meets the conditions for an offer, the contract is concluded when the other party succeeds in choosing such commodity or service and submitting an order, unless otherwise agreed upon by the parties.</i>
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Article 491 of the *PRC Civil Code* specifically deals with the conclusion of electronic contracts. I.e. where the information on any commodity or service released by a party through information networks, such as the Internet, meets the conditions of an offer, and the other party selects the said commodity or service and successfully submits an order, a contract is concluded, unless otherwise agreed by the parties. Such offer, as regulated under Article 472 of the *PRC Civil Code*, shall be a manifestation of intent to conclude a contract with other parties while (i) its contents shall be specific and definite and (ii) it shall indicate that the offeror will be bound by it upon acceptance by the offeree. While Article 49 of the *PRC E-commerce Law* deals with e-commerce operators that conduct e-commerce activities on an information network, such as the Internet, only, Article 491 of the *PRC Civil Code* may also cover, for example, non-e-commerce operators' activities on online second-hand platforms.

Article 512, sub-clause 1, of the *PRC Civil Code*, following Article 51 of the *PRC E-commerce Law*, further regulates that, unless otherwise agreed, where the subject matter of an electronic contract concluded through the Internet or other information network is the delivery of goods and the goods are delivered through express logistics, the time of signing for receipt by the consignee shall be the time of delivery. If the subject matter of an electronic contract is the provision of services, the time specified in the generated electronic voucher or in the physical voucher shall be the time of provision of services. If the above voucher does not specify the time or the time specified is inconsistent with the time of the actual provision of the services, the time of the actual provision of the services shall be decisive. Where the subject matter of an electronic contract is delivered by online transmission, the time of entry of the subject matter into the specific system designated by the other party and which can be searched and identified shall constitute the time of delivery. Lastly, if the parties to an electronic contract otherwise agree on the method and time of delivering goods or providing services, the agreement of the parties shall prevail and be decisive.

**e) State Procurement Contracts**

<b>PRC Contract Law</b>	<b>PRC Civil Code</b>
<b>Article 38</b> In the case that the State, based on necessity, issues a mandatory assignment or a state procurement order, the relevant legal persons or other organizations shall conclude contracts based on the rights and obligations	<b>Article 494</b> If the State, based on necessity of disaster response and relief or <i>epidemic prevention and control or other necessity</i> , issues a state procurement order or a mandatory assignment, the relevant civil

<p>as provided for by the relevant laws and administrative regulations.</p>	<p>subjects shall conclude contracts based on the rights and obligations as provided for by the relevant laws and administrative regulations.</p> <p><i>The party which is obliged to make an offer in accordance with the provisions of laws and administrative regulations shall make a reasonable offer promptly.</i></p> <p><i>A party which is under an obligation to make an acceptance in accordance with the provisions of the law or administrative regulations must not refuse to comply with the other party's reasonable request to conclude a contract.</i></p>
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In comparison to the stipulations on State procurement as provided for in the current *PRC Contract Law*, Article 494 of the *PRC Civil Code* stipulates that in case the State, based on necessities due to emergency situations, disaster relief and prevention and control of epidemics or other necessities, issues a mandatory assignment or a state procurement order, the relevant civil subjects shall conclude contracts based on the rights and obligations as provided for by the relevant laws and administrative regulations. Further, a party that is under the obligation to make an offer in accordance with the provisions of laws and administrative regulations shall make a reasonable offer promptly and a party that is under the obligation to make an acceptance in accordance with the provisions of the law or administrative regulations must not refuse to comply with the other party's reasonable request to conclude a contract. These amendments to the provisions as contained in the current *PRC Contract Law* very likely appear to be a consequence of and response to the COVID-19 epidemic.

**f) Pre-contracts**

<p><b>SPC Interpretation on Sale and Purchase Contracts</b></p>	<p><b>PRC Civil Code</b></p>
<p><b>Article 2</b> Where parties sign an order to buy, order to purchase, reservation book, letter of intention, memorandum or any other pre-contract specifying that the parties will enter into a sale and purchase contract in a certain period, but one party does not discharge the obligation on entering into the sale and purchase contract and the other party requests such party to bear the liability for breach of the pre-contract or requests to terminate the pre-contract and claims for liquidated damages, the People's Court shall uphold such claim.</p>	<p><b>Article 495</b> A subscription order, purchase order, pre-order, etc., under which the parties agree to enter into a contract within a certain time limit in the future shall constitute a pre-contract.</p> <p>If one party fails to perform the obligation to contract as agreed in the pre-contract, the other party may <i>claim liability of the party for breach of the pre-contract</i>.</p>

Pre-contracts are currently dealt with in Article 2 of the *Interpretations of the Supreme People's Court on Issues Concerning the Application of Law for the Trial of Cases Involving Disputes over Sale and Purchase Contracts* ("**SPC Interpretation on Sale and Purchase Contracts**"). Article 495 of the *PRC Civil Code* implements general rules on pre-contracts and extends the applicable scope of pre-contracts from sale and purchase contracts only to now all kinds of contracts regulated under the *PRC Civil Code*.

After the effectiveness of the *PRC Civil Code* on 1 January 2021, enterprises are advised to increase awareness when signing, e.g., letters of intent, memoranda of understanding or framework agreements and to clearly check and stipulate whether such documents shall have a binding effect or not. Regarding the "relevant liabilities for breach of pre-contracts", the *PRC Civil Code* leaves it open whether such liabilities only refer to the compensation of loss or may also include specific performance, i.e. subsequent signing and performance of a formal contract. How this will be dealt with in practice remains to be seen.

**g) Standard Terms and Conditions**

<b>PRC Contract Law</b>	<b>PRC Civil Code</b>
<p><b>Article 39</b> Where standard terms are adopted in a contract, the party providing the standard terms shall observe the principle of fairness in defining the rights and obligations of the parties, draw the attention of the other party in a reasonable manner to the terms that exclude or restrict the other party's liabilities, and explain the standard terms at the request of the other party. [...]</p>	<p><b>Article 496</b> [...] Where standard terms are adopted in a contract, the party providing the standard terms shall observe the principle of fairness in defining the rights and obligations of the parties, draw the attention of the other party in a reasonable manner to the terms that exclude or mitigate the other party's liabilities <i>or other terms related to the material interest of the other party</i>, and explain the standard terms at the request of the other party. If the party providing the standard terms fails to perform the obligation of drawing attention or explanation, causing the other party not to notice or understand the terms with its significant interest, <i>the other party may claim that such terms do not constitute part of the contract.</i></p>
<p><b>SPC Interpretation on PRC Contract Law (II)</b></p>	
<p><b>Article 9</b> Where the party providing the standard clauses violates the provisions of paragraph 1 of Article 39 of the <i>PRC Contract Law</i> on the obligation of reminder and explanation, resulting in the failure of the other party to pay attention to the exemptible and restrictive clauses regarding its liability, a People's Court shall uphold the request of the other party for the revocation of such standard clauses.</p>	



In line with Article 39 of the current *PRC Contract Law*, Article 496 of the *PRC Civil Code* defines standard terms as clauses (i) which are prepared in advance by one party for repeated use and (ii) which are not negotiated with the other party when the contract is concluded.

Article 496 of the *PRC Civil Code* extends the scope of the obligations of the party providing the standard terms compared to Article 39 of the *PRC Contract Law* by stipulating that attention shall not only be drawn and explanations shall not only be made regarding "*terms that exclude or mitigate the other party's liabilities*" but also regarding "*other terms related to the material interest of the other party*".

The scope of the "reasonable manner" as referred to in Article 496 of the *PRC Civil Code* is not further clarified. Article 6 of the current *SPC Interpretation on PRC Contract Law (II)* stipulates in this regard that the party providing the standard terms shall be deemed to have adopted a "reasonable manner", if the party highlights the clauses that exclude or limit its liability with special features using words, symbols or fonts at the execution of the contract to draw the attention of the other party and makes explanations on such standard terms as required by the other party. It appears not unlikely that a similar explanation on "reasonable manner" might be included in the upcoming interpretation of the SPC on the *PRC Civil Code*.

Further, Article 9 of the current *SPC Interpretation on PRC Contract Law (II)* provides that in case of failure of drawing the attention of the other party in a reasonable manner to the terms that exclude or restrict the first party's liabilities, and of explaining the standard terms at the request of the other party, "*a People's Court shall uphold the request of the other party for the revocation of such standard clauses*". Article 496 of the *PRC Civil Code* now stipulates that in such case, the other party may claim that such standard terms are not part of the contract. The stipulation in the *PRC Civil Code* does not require a request to a People's Court and is more in favour of the party the standard terms are addressed to.

**h) Emphasis on Protection of the Environment when Performing Contracts**

<b>PRC Contract Law</b>	<b>PRC Civil Code</b>
<p><b>Article 60</b> The parties shall fully perform their obligations as agreed.</p> <p>The parties shall, observing the principle of good faith, perform such obligations as notification, rendering assistance and maintaining confidentiality based on the nature and purpose of the contract and in accordance with trade practices.</p>	<p><b>Article 509</b> The parties shall fully perform their obligations as agreed.</p> <p>The parties shall, observing the principle of good faith, perform such obligations as notification, rendering assistance and maintaining confidentiality based on the nature and purpose of the contract and in accordance with trade practices.</p> <p><i>The parties shall avoid wasting resources, polluting the environment and damaging the ecology during the performance of the contract.</i></p>

Compared to the respective stipulation of Article 60 of the *PRC Contract Law*, Article 509 of the *PRC Civil Code* emphasizes that the parties when performing contracts shall "*avoid wasting resources, polluting the environment and damaging the ecology*", which is in line with recent attempts of the State Government to promote environmental protection.

**i) Alternative Obligations**

Articles 515 and 516 of the *PRC Civil Code* newly introduce general rules on alternative obligations. I.e., where there are several items in the subject matter of the obligation and the obligor is required to perform only one of them, the obligor shall have the right of choice, unless otherwise stipulated by the law or agreed by the parties or there are other transaction practices. Where the party with the right to choose fails to make a choice within the agreed period or upon expiry of the performance period, and still fails to make a choice within a reasonable period after having been urged to do so, the right to choose shall be transferred to the respective other party.

Further, the relevant party shall promptly notify the respective other if it exercises its option. Upon receipt of such notice, the subject matter shall be determined and may not be changed, unless otherwise agreed by the respective other party. When there is impracticability in the alternative subject matter, the party entitled to the choice may not choose the subject matter which is impracticable, unless the impracticability is caused by the opposing party.

**j) Joint and Several Claims and Obligations**

Articles 517 to 521 of the *PRC Civil Code* newly introduce general rules on joint and several claims and obligations.

It is clarified that, when there are two or more obligees, and all or part of the obligees may request the obligor to perform his or her obligations, the claims shall be joint and several. Vice versa, when there are two or more obligors, and the obligee may request all or part of the obligors to perform all of their obligations, the debts shall be joint and several.

Such provisions, for the first time, expressly stipulate the legal consequences arising from the behaviour of any of the multiple obligors or obligees towards the other "joint and several" obligors or obligees.

E.g., according to Article 519 of the *PRC Civil Code*, where the proportions between joint and several obligors are difficult to determine, they shall be deemed to be equal. If a joint and several obligor actually assumes obligations in excess of his or her own share of the debt, it shall have a right of recourse against the other joint and several obligors to the extent of the share not performed by the other joint and several obligors for the excess and shall be entitled to the rights of an obligee, provided that the interests of the obligee are not prejudiced.

Article 520 of the *PRC Civil Code* stipulates that where some joint and several obligors perform or offset against the obligations or place the subject matter in escrow, the obligations of other obligors towards the obligee shall be extinguished within the corresponding scope and the first mentioned obligors may exercise recourse against other obligors in accordance with the provisions Article 519 of the *PRC Civil Code*.

According to Article 521 of the *PRC Civil Code*, where the proportions between joint and several obligees are difficult to determine, they shall be deemed to be equal. Joint and several obligees who have actually accepted obligations shall be reimbursed by the other joint and several obligees pro rata. Further, the provisions on joint and several debts in Chapter IV of the *PRC Civil Code*, Performance of Contracts, shall apply mutatis mutandis to joint and several claims.

**k) Obligations in Favour of Third Parties**

PRC Contract Law	PRC Civil Code
<p><b>Article 64</b> Where the parties agree that the obligor performs obligations for a third party, if the obligor fails to perform the obligations for the third party or the performance does not comply with the terms of the contract, the obligor shall be liable to the obligee for breach of contract.</p>	<p><b>Article 522</b> Where the parties agree that the obligor performs obligations for a third party, if the obligor fails to perform the obligations for the third party or the performance does not comply with the terms of the contract, the obligor shall be liable to the obligee for breach of contract.</p> <p><i>Where the law stipulates or the parties agree that a third party may directly request an obligor to perform the obligations to the third party, if the third party fails to expressly refuse [that performance is made to the third party] within a reasonable time limit, if the obligor does not perform the obligations to the third party or the performance does not comply with the terms of the contract, the third party may request that the obligor assume the liability for breach of contract; and any defence of the obligor against the obligee may be asserted against the third party.</i></p>

Different from Article 64 of the current *PRC Contract Law* and the current legal practice in the PRC, Article 522 of the *PRC Civil Code* introduces a third party’s right to directly request an obligor to perform the obligations to the third party, if so provided by law or agreed between the obligor and the obligee. It is also clarified that in such case, if the obligor does not perform the obligations to the third party or the performance does not comply with the terms of the contract, the third party may request that the obligor assume liability for breach of contract towards the third party.

**l) Third Party’s Performance of Obligations and Debt Joining**

Articles 524 and 552 of the *PRC Civil Code* newly provide for general rules on third party’s performance of obligations and debt joining.

According to Article 524 of the *PRC Civil Code*, where an obligor fails to perform his or her obligations, and a third party has lawful interests in the performance of such obligations, the third party is entitled to perform the obligations on behalf of the obligor, unless the obligations can only be performed by the obligor as agreed upon by the parties or in accordance with legal provisions or the nature of the obligations. After the obligee has accepted the performance of a third party, its obligatory right against the obligor shall be assigned to the third party, unless it is otherwise agreed upon by the obligor and the third party.

Article 552 of the *PRC Civil Code* provides that where a third party agrees with the obligor on joining in the obligations and notifies the obligee, or the third party expresses to the obligee his or her willingness to join in the obligations, and the obligee does not expressly reject the joining within a reasonable period, the obligee may request the third party to join the obligor in bearing joint and several obligations within the scope of obligations which it is willing to bear.

**m) Unforeseeable Change of Circumstances**

<b>SPC Interpretation on PRC Contract Law (II)</b>	<b>PRC Civil Code</b>
<p><b>Article 26</b> Where a party to a contract petitions the court to modify or terminate the contract on the grounds that the continuous performance of the same is obviously unfair to the party <i>or the purpose of the contract will not be realized</i> due to occurrence of any material change of circumstances that is unforeseeable, <i>not caused by force majeure</i>, and not a commercial risk after the conclusion of the contract, the court shall decide whether the contract shall be modified or terminated according to the principle of fairness on a case-by-case basis.</p>	<p><b>Article 533</b> After a contract has been concluded, and the basic conditions for the contract have undergone a major change which was unforeseeable by the parties at the time of conclusion and which does not belong to commercial risks, if it is obviously unfair to one party to continue to perform the contract, the party adversely affected <i>may renegotiate with the other party</i>; if the negotiation fails within a reasonable period, the parties may request a People's Court <i>or an arbitration institution</i> to modify or rescind the contract.</p> <p>The People's Court or arbitration institution shall take into account the actual circumstances of the case and amend or rescind the contract pursuant to the principle of fairness.</p>

Article 533 of the *PRC Civil Code* implemented the legal concept of an unforeseeable change of circumstances which is currently provided for in Article 26 of the *SPC Interpretation on PRC Contract Law (II)* at a formal legal level. Compared to Article 26 of the *SPC Interpretation on PRC Contract Law (II)*, Article 533 of the *PRC Civil Code* does not require anymore that the change of circumstances shall not be caused by *force majeure*. Thus, it is expected that also if a party is subject to *force majeure*, it may still assert Article 533 of the *PRC Civil Code* and apply for an amendment or rescission of the contract. This change appears to be a consequence of the COVID-19 epidemic, where it was broadly discussed whether Article 26 of the *SPC*

*Interpretation on PRC Contract Law (II)* is applicable, in addition or alternatively to stipulations on *force majeure*, or not.

Further, Article 533 of the *PRC Civil Code* emphasizes that the parties shall first negotiate and try to find an amicable solution. Only if negotiations fail, they shall forward the matter to competent institutions. With regard to the latter, Article 533 of the *PRC Civil Code* clarifies that such competent institutions are not only People's Courts, but also arbitration institutions.

**n) Obligee's Right of Subrogation**

PRC Contract Law	PRC Civil Code
<p><b>Article 73</b> If the obligor neglects to exercise its due claims, thus damaging the interests of the obligee, the obligee may petition a People's Court to subrogate it to the claims of the obligor, unless such claims belong exclusively to the obligor.</p> <p>The subrogation shall be exercised to the extent of the obligee's claims. The necessary expenses incurred by the obligee in exercising the subrogation shall be borne by the obligor.</p>	<p><b>Article 535</b> If the obligor neglects to exercise its claims <i>or the collateral rights relating to the claims</i>, thereby affecting the obligee's realization of due claims, the obligee may petition a People's Court to subrogate the exercise of the obligor's rights against the counterparty in its own name, unless such rights belong exclusively to the obligor.</p> <p>The subrogation shall be exercised to the extent of the obligee's <i>due</i> claims. The necessary expenses incurred by the obligee in exercising the subrogation shall be borne by the obligor.</p> <p><i>The counterparty's defense against the obligor may be asserted against the obligee.</i></p>
SPC Interpretation on PRC Contract Law (I)	PRC Civil Code
<p><b>Article 20</b> Where in a subrogation suit brought by the obligee against the secondary obligor, the People's Court finds after trial that a right to subrogation exists, the obligation between the obligee and the obligor and that between the obligor and the secondary obligor shall be extinguished upon the performance of obligation to the obligee by the secondary obligor.</p>	<p><b>Article 537</b> Where a People's Court affirms the subrogation, the counterparty of the obligor shall perform the obligations to the obligee, and <i>after the obligee has accepted the performance</i>, the corresponding rights and obligations between the obligee and the obligor, and between the obligor and the counterparty, shall be terminated. <i>Where the obligor's claims or the collateral rights relating to the claims against the counterparty are subject to preservation or enforcement measures, or the obligor is bankrupt, the matter shall be dealt with pursuant to the provisions of the relevant laws.</i></p>

The subrogation of claims has been implemented in Articles 535 et. seq. of the *PRC Civil Code*. Article 535 of the *PRC Civil Code* added "*collateral rights relating to the claims*" into the circumstances where the obligee may apply before a People's Court for a subrogation.

According to Article 536 of the *PRC Civil Code*, prior to the maturity of the obligee's claims, where the limitation of action for the obligor's claims or the collateral rights relating to the claims is about to expire or the obligor fails to declare bankruptcy claims in a timely manner, thus affecting the realization of obligee's claims, the obligee may be subrogated to the counterparty of the obligor to request that the counterparty performs the rights for the obligor, or to declare to the bankruptcy administrator, or to perform any other necessary act.

Article 537 stipulates that the rights and obligations between an obligee and an obligor and between an obligor and a secondary obligor (now called "the obligor's counterparty" in the *PRC Civil Code*) shall be terminated where a People's Court has affirmed the subrogation, and the counterparty of the obligor has performed the obligations to the obligee, and the obligee has accepted the performance.

Article 537 of the *PRC Civil Code* clarifies that where the obligor's claims or the collateral rights relating to the claims against the counterparty are subject to preservation or enforcement measures, or the obligor is bankrupt, the matter shall be dealt with pursuant to the provisions of the relevant special laws.

**o) Obligor's Right of Revocation of Acts of an Obligor**

Articles 538 and 539 of the *PRC Civil Code* combine the current stipulations of Article 74 of the *PRC Contract Law* and Article 18 of the *SPC Interpretation on PRC Contract Law (II)* regarding the circumstances where the act of an obligor can be revoked by a competent People's Court and adds 2 additional circumstances.

According to Article 538 of the *PRC Civil Code*, where the obligor (i) disposes of property rights or interests free of charge, (ii) abandons his or her claims, (iii) abandons a guarantee of claims, (iv) transfers assets without compensation or otherwise, or (v) maliciously extends the period for performance of its due claims, thus affecting the realization of claims by the obligee, the obligee may request that a People's Court revokes the obligor's action.

According to Article 539 of the *PRC Civil Code*, where (i) an obligor transfers its property at a low price which is obviously unreasonable, or (ii) accepts the property of another person at a high price which is obviously unreasonable, or (iii) provides a guarantee for another person, thereby affecting the realization of the obligee's claims, and the counterparty of the obligor knows or should have known of the relevant circumstances, the obligee may petition a people's court for cancelation of the obligor's act.

**p) Assignment of Claims**

Article 79 of the *PRC Contract Law* and Article 545 of the *PRC Civil Code* deal with the assignment of claims, which is subject to notification of the obligor, and state that the obligee may assign, in whole or in part, its claims to a third party, except under any of the following circumstances: (i) the claims shall not be assigned in light of the nature of the claims; (ii) the

claims shall not be assigned in accordance with the agreement between the parties; or (iii) the claims shall not be assigned in accordance with the law.

In relation to the *PRC Contract Law*, it was disputed whether contractually agreed non-assignment clauses are valid against *bona fide* third parties or not (as far as we can see, the prevailing opinion among scholars and courts favored invalidity in such case). Article 545 of the *PRC Civil Code* now clarifies such issue by expressly stating that if "*the parties agree that a non-monetary claim shall not be assigned, the agreement shall not be effective against a third party in good faith*" and if "*the parties agree that a monetary claim shall not be assigned, the agreement shall not be effective against a third party*".

Articles 547 and 550 of the *PRC Civil Code* further expressly clarify (i) that the assignee's acquisition of collateral rights shall not be affected by non-performance of registration procedures or non-transfer of the possession of such collateral rights and (ii) that any additional expenses incurred as a result of the assignments of claims shall be borne by the assignor.

**q) Assignment of Obligations**

Article 84 of the *PRC Contract Law* and Article 551 of the *PRC Civil Code* deal with the assignment of obligations which is subject to the prior consent of the obligee. Article 551 of the *PRC Civil Code* clarifies that the obligor or the third party may urge the obligee to give his or her consent within a reasonable period of time; if the obligee does not give his or her consent, his or her consent shall be deemed to have been refused.

Article 559 of the *PRC Civil Code* newly stipulates that when an obligation is terminated, any collateral right accessory to the obligation shall extinguish, except as otherwise provided by the law or agreed upon by the parties.

**r) Termination of Contracts**

PRC Contract Law	PRC Civil Code
<p><b>Article 94</b> The parties to a contract may terminate the contract under any of the following circumstances:</p> <ol style="list-style-type: none"> <li>1. the purpose of the contract is rendered impossible to achieve due to force majeure;</li> <li>2. any party to the contract indicates expressly or by conduct, before the expiration of the performance period, that it will not perform its principal obligations;</li> <li>3. any party to the contract delays performing its principal obligations and fails to perform the same within a</li> </ol>	<p><b>Article 563</b> The parties to a contract may terminate the contract under any of the following circumstances:</p> <ol style="list-style-type: none"> <li>1. the purpose of the contract is rendered impossible to achieve due to force majeure;</li> <li>2. any party to the contract indicates expressly or by conduct, before the expiration of the performance period, that it will not perform its principal obligations;</li> <li>3. any party to the contract delays performing its principal obligations and fails to perform the same within a</li> </ol>

<p>reasonable time period after being urged to do so;</p> <p>4. any party to the contract delays performing the obligations or commits other acts in breach of the contract, resulting in the impossibility to achieve the purpose of the contract; or</p> <p>5. other circumstances as provided by the laws.</p>	<p>reasonable time period after being urged to do so;</p> <p>4. any party to the contract delays performing the obligations or commits other acts in breach of the contract, resulting in the impossibility to achieve the purpose of the contract; or</p> <p>5. other circumstances as provided by laws.</p> <p><i>A non-fixed-term contract with the obligation of continuous performance as the content may be terminated by a party at any time, provided that the party notifies the other party in advance of a reasonable time limit.</i></p>
<p><b>Article 95</b> Where the law provides for or the parties agree upon a time limit for the exercise of the right to terminate a contract, and no party has exercised the right within the time limit, the said right shall be extinguished.</p> <p>Where the law does not provide for or the parties does not agree upon a time limit for the exercise of the right to terminate a contract, and no party exercises the right within a reasonable time period after being urged by the other party to do so, the said right shall be extinguished.</p>	<p><b>Article 564</b> Where the law provides for or the parties agree upon a time limit for the exercise of the right to terminate a contract, and no party has exercised the right within the time limit, the said right shall be extinguished.</p> <p>Where the law does not provide for or the parties do not agree upon a time limit for the exercise of the right to terminate a contract, and <i>no party exercises the right within one year after the party has known or should have known about the cause for rescission or</i> within a reasonable time period after being urged by the other party to do so, the said right shall be extinguished.</p>
<p><b>Article 96</b> Either party to a contract shall give a notice to the other party if it proposes to terminate the contract in accordance with the provisions of Paragraph 2 of Article 93 and Article 94 of the Law. The contract shall be terminated when the notice reaches the other party. Where the other party objects to such termination, it may petition a People's Court or an arbitration institution to confirm the effectiveness of the termination of the contract.</p>	<p><b>Article 565</b> Either party to a contract shall give a notice to the other party if it proposes to terminate the contract in accordance with the law. The contract shall be terminated upon receipt of the notice by the other party. <i>If the notice states that the contract will be automatically terminated by the obligor's failure to perform the obligation within a time limit, and the obligor fails to do so, the contract shall be terminated at the expiration of the time limit stated in the notice.</i> Where the other party objects to such termination, <i>either party</i> may petition a</p>



<p>Where the laws or administrative regulations provide that the termination of a contract shall be subject to approval or registration procedures, the provisions thereof shall govern.</p>	<p>People's Court or an arbitration institution to confirm the effectiveness of the termination of the contract.</p> <p><i>Where a party does not notify the other party but directly asserts rescission of the contract pursuant to the law by way of filing a lawsuit or applying for arbitration, and the People's Court or the arbitration institution confirms the said assertion, the contract shall be terminated upon delivery of the duplicate copy of the statement of claim or the duplicate copy of the arbitration application to the other party.</i></p>
<p><b>Article 97</b> After the termination of a contract, for the part of the contract that has not yet been performed, the performance shall be terminated; and for the part that has been performed, a party to the contract may, in light of the status of the performance and the nature of the contract, request that the original position be restored or other remedial measures be taken, and has the right to claim compensation for any loss</p>	<p><b>Article 566</b> After the termination of a contract, for the part of the contract that has not yet been performed, the performance shall be terminated; and for the part that has been performed, a party to the contract may, in light of the status of the performance and the nature of the contract, request that the original position be restored or other remedial measures be taken, and has the right to claim compensation for any loss.</p> <p><i>Where a contract is terminated due to breach of contract, the party entitled to terminate the contract may request the breaching party to bear the liability for breach of contract, unless otherwise agreed upon by the parties.</i></p> <p><i>Unless a security contract provides to the contrary, the security provider shall continue to bear security liability for the civil liability borne by the obligor following the termination of the principal claim-obligation contract.</i></p>

- Termination of Non-fixed-term Contracts

The *PRC Contract Law* does not provide for a general stipulation regarding the termination of non-fixed-term contracts. Only the stipulations on certain "typical contracts" provide for a respective termination right. E.g.,

- With regard to lease agreements, Article 232 of the *PRC Contract Law* stipulates that where the term of a lease was not prescribed or clearly prescribed and cannot be determined in accordance with Article 61 of the *PRC Contract Law*, such lease is deemed a non-fixed-term lease and either party may terminate the contract at any time, provided that the lessor shall give the lessee a reasonable advance notice before it terminates the contract;
- With regard to work contracts, Article 268 of the *PRC Contract Law* stipulates that the hirer may terminate the contract of hired work at any time, provided that it shall indemnify the hiree for its loss as a result, if any; and
- With regard to agency agreements, Article 410 of the *PRC Contract Law* stipulates that either the principal or the agent may terminate the agency appointment contract at any time. Where the other party sustains any loss due to termination of the contract, the terminating party shall indemnify the other party, unless such loss is due to a reason not attributable to the terminating party.

For all non-fixed-term contracts other than the ones mentioned above, a termination is only possible if the respective contract provides for a relevant contractually agreed termination reason, if the parties to the contract mutually agree to terminate the contract or if a statutory termination reason, especially one of those stipulated in Article 94 of the *PRC Contract Law*, applies.

This has now changed considerably. Article 563 of the *PRC Civil Code* which repeats the statutory termination reasons stipulated in Article 94 of the *PRC Contract Law* now expressly adds that "*non-fixed-term contracts with the obligation of continuous performance as the content may be terminated by a party at any time, provided that the party notifies the other party in advance of a reasonable time limit*". This constitutes a remarkable change and, in our view, improvement compared to the *PRC Contract Law*.

In addition to the general stipulation of Article 563 of the *PRC Civil Code*, the *PRC Civil Code* provides for more special rules on the termination of specific non-fixed-term contracts, e.g. non-fixed-term Property Service Contracts (Article 948 of the *PRC Civil Code*), non-fixed-term Partnership Contracts (Article 976 of the *PRC Civil Code*), and contracts on the permitted use of a portrait (Article 1022 of the *PRC Civil Code*). Either party may terminate the relevant non-fixed-term contracts at any time, provided that it has informed the other party within a reasonable period in advance.

- Time period for termination

According to Article 564 of the *PRC Civil Code*, in the absence of relevant statutory provisions or a respective agreement between the parties, a contract shall be terminated "*within one year after the party has known or should have known about the cause for the termination or within a reasonable time period after being urged by the other party to do so*". Otherwise, the termination right shall extinguish.

So far, such a one-year time period has only been provided for in Article 15 of the *Interpretation of the Supreme People's Court on Issues concerning the Application of Law*

*in the Trial of Cases Involving Disputes over Contracts for the Sale and Purchase of Commodity Housing* which stipulates that the right to terminate a house sales contract shall be exercised within one year of the date on which the relevant circumstances occurred. Article 564 of the *PRC Civil Code* now states and clarifies that such one-year time period shall, generally, apply to all kind of contracts.

- Time of termination

According to both Article 96 of the *PRC Contract Law* and Article 565 of the *PRC Civil Code*, a contract shall, generally, be terminated if the (valid) termination notice is received by the other party.

Article 565 of the *PRC Civil Code* further adds the following specifics:

- If the termination notice states that the contract will be automatically terminated by the debtor's failure to perform the obligation within a certain time limit, and the debtor fails to do so, the contract shall be terminated automatically at the expiration of the time limit stated in the notice; and
- Where one party fails to notify the other party and directly claims the termination of the contract by instituting a lawsuit or applying for arbitration, if the People's Court or arbitration institution affirms the claim, the contract shall be terminated when a copy of the written letter of claims or a copy of the request for arbitration is served to the other party.

- Consequences of termination

Article 97 of the *PRC Contract Law* and Article 566 of the *PRC Civil Code* stipulate that after the termination of a contract, for the part of the contract that has not yet been performed, the performance shall be terminated; and for the part that has been performed, a party to the contract may, in light of the status of the performance and the nature of the contract, request that the original position be restored or other remedial measures be taken, and has the right to claim compensation for any loss.

Article 566 of the *PRC Civil Code* further adds and clarifies that where a contract is terminated due to breach of contract, the party entitled to terminate the contract may request the breaching party to bear the liability for breach of contract, unless otherwise agreed upon by the parties.

s) **Specific Performance and Termination**

<b>PRC Contract Law</b>	<b>PRC Civil Code</b>
<b>Article 110</b> Where either party to a contract fails to perform non-monetary obligations or its performance of the non-monetary obligations does not comply with the terms of the contract, the other party may request the	<b>Article 580</b> Where either party to a contract fails to perform non-monetary obligations or its performance of the non-monetary obligations does not comply with the terms of the contract, the other party may request the

<p>party to render performance except under any of the following circumstances:</p> <ol style="list-style-type: none"> <li>1. the performance is impossible in law or in fact;</li> <li>2. the subject matter of the obligation is unfit for compulsory performance or the performance costs are too high; and</li> <li>3. the obligee fails to demand performance within a reasonable time limit.</li> </ol>	<p>party to render performance except under any of the following circumstances:</p> <ol style="list-style-type: none"> <li>1. the performance is impossible in law or in fact;</li> <li>2. the subject matter of the obligation is unfit for compulsory performance or the performance costs are too high; and</li> <li>3. the obligee fails to request performance within a reasonable time limit.</li> </ol> <p><i>If any of the exceptions set out in the preceding paragraph results in the impossibility to realize the purpose of the contract, a People's Court or an arbitral institution may, as requested by a party, terminate the contractual rights and obligations between the parties, which however does not affect the liability for breach of contract to be borne.</i></p>
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Article 580 of the *PRC Civil Code* now provides for a termination reason in case that the purpose of the contract cannot be realized anymore because (i) the performance is impossible due to legal or factual reasons, (ii) the subject matter of the obligation is unfit for compulsory performance or the performance costs are too high; or (iii) the obligee fails to request performance within a reasonable time limit. The right to apply to a competent People’s Court or arbitration institution to terminate a contract in these cases is available for both the defaulting as well as the non-defaulting party.

Under the current PRC laws and regulations, the defaulting party may raise an objection against the non-defaulting party’s request on specific performance, but is normally not entitled to terminate the contract, unless a contractually agreed or statutory termination reason, especially one of those as set out in Article 94 of the *PRC Contract Law*, applies. This has changed under the *PRC Civil Code*.

However, in case of a termination due to Article 580 of the *PRC Civil Code*, the defaulting party may still be held liable for breach of contract. According to Article 584 of the *PRC Civil Code*, the amount of compensation for losses shall, in general, be equal to the losses caused by the breach of contract, including benefits receivable after the performance of the contract, provided that it shall not exceed the probable losses caused by breach of contract which were foreseen or ought to have been foreseen by the breaching party at the time of conclusion of the contract.

**t) Additional Stipulations regarding Liability for Breach of Contract**

According to both Article 107 of the *PRC Contract Law* and Article 577 of the *PRC Civil Code*, where a party to a contract fails to perform the contractual obligations or its performance does not comply with the terms of the contract, the party shall bear liability for breach of contract

such as continuing its performance of the obligations, taking remedial measures or paying compensation for losses. Article 581 of the *PRC Civil Code* further adds that, where a party fails to perform its obligations or its performance fails to satisfy the terms of the contract and is not allowed to be enforced in light of the nature of the obligation, "*the other party may request the party to bear the expenses incurred in the performance by a third party*".

Article 589 of the *PRC Civil Code* deals with a delay in acceptance and now expressly stipulates that where the obligor has performed his or her obligations as agreed, and the obligee refuses to accept them without justified reasons, the obligor may claim compensation for the additional expenses. During the delay in acceptance by the obligee, the obligor is not required to pay interest.

**u) Shared Liability and Contributory Negligence**

<b>PRC Contract Law</b>	<b>PRC Civil Code</b>
<b>Article 120</b> Where both parties breach the contract, each party shall bear its corresponding liability.	<b>Article 592</b> Where both parties breach the contract, each party shall bear its corresponding liability.
<b>SPC Interpretation on Sale and Purchase Contracts</b>	Where a breach of contract by one party causes losses to the other party, and the other party is at fault in regard to the occurrence of such losses, the corresponding amount of compensation for the losses may be reduced.
<b>Article 30</b> Where any party to a sale and purchase contract breaches such contract and causes the other party to suffer losses, the other party is in fault for the occurrence of such loss, and the breaching party claims to reduce corresponding compensation for such loss, the People's Court shall uphold such claim.	

Article 592 of the *PRC Civil Code*, similarly to Article 495 of the *PRC Civil Code*, transforms relevant stipulations from the *SPC Interpretation on Sale and Purchase Contracts* into the *PRC Civil Code* and extends the applicable scope of the respective rule from sale and purchase contracts only to all kinds of contracts that are governed under the *PRC Civil Code*. In accordance with Article 592, for all contracts, the amount of compensation for losses may be reduced if the other party is (also) at fault for the occurrence of the losses.

**3. Typical Contracts**

Rules on typical contracts, such as Sales Contracts, Loan Contracts, Lease Contracts and Passenger Transportation Contracts, have been amended and are now more specific compared to the respective provisions contained in the current *PRC Contract Law*.

Below is a summary on some key changes in Subpart II, Typical Contracts:

a) **Sale and Purchase Contracts**

**(1) Unauthorized Disposition**

<b>PRC Contract Law</b>	<b>SPC Interpretation on Sale and Purchase Contracts</b>	<b>PRC Civil Code</b>
<p><b>Article 51</b> A contract under which a person without the right of disposition disposes of the property of another person shall be valid upon the ratification by the person with such right or upon the acquisition of such right by the person without such right after the conclusion of the contract.</p> <p><b>Article 132</b> The subject matter to be sold shall be owned by the seller or shall be the one that the seller is entitled to dispose of.</p> <p>Where the transfer of a subject matter is prohibited or restricted by laws and administrative regulations, the provisions thereof shall govern.</p>	<p><b>Article 3</b> Where any party claims that a contract is void on the ground that the seller does not obtain the title to or the right to dispose of the subject matter upon entering into the contract, the People's Court shall not support such claim.</p> <p>If the seller causes the title of the subject matter unable to be transferred for not obtaining the title to or the right to dispose of the subject matter and the buyer requests the seller to bear the default liability or requests to terminate the contract and claims for liquidated damages, the People's Court shall uphold such claim.</p>	<p><b>Article 597</b> Where the ownership of the subject matter cannot be transferred due to the seller's failure to obtain the right of disposition, the buyer may terminate the contract and request the seller to bear liability for breach of contract.</p> <p>Where the transfer of the subject matter is prohibited or restricted by laws and administrative regulations, the provisions thereof shall govern.</p>

According to Article 51 of the current *PRC Contract Law*, a contract under which a person without the right of disposition disposes of the property shall be valid only upon the ratification or upon the acquisition of such right by such person. Article 3 of the *SPC Interpretation on Sale and Purchase Contracts*, however, differently stipulates that, in general, such a contract shall be valid. Article 597 of the *PRC Civil Code* basically follows Article 3 of the *SPC Interpretation on Sale and Purchase Contracts* and stipulates that where the ownership of the subject matter cannot be transferred due to the seller's failure to obtain the right of disposition, the relevant contract is still valid but can be terminated.

Further, according to Article 646 of the *PRC Civil Code* which states that "*where there is any provision on other non-gratuitous contracts in laws, such provision shall apply; if there is no such provision, the relevant provisions regarding sales contracts shall apply mutatis*

*mutandis*", Article 597 of the *PRC Civil Code* may also apply to contracts other than sales and purchase contracts if there are no relevant special provisions.

## (2) Reduced or Waived Liability for Defects in Products

Article 618 of the *PRC Civil Code* deals with general rules on reduced or waived liabilities for quality defects. It newly adds that, where the parties agree on reducing or waiving the seller's liability for a defect in the subject matter, the seller shall have no right to assert a reduction or waiver of liability if it failed to notify the buyer of the defect in the subject matter as a result of the seller's intentional misconduct or gross negligence.

## b) Guarantee Contracts

Articles 681 to 702 of the *PRC Civil Code* newly deal with Guarantee Contracts. Such provisions mainly follow the current *PRC Securities Law* and the *Interpretation of the Supreme People's Court on Certain Issues Regarding the Application of the PRC Security Law*.

A guarantee contract is a contract whereby the guarantor and the obligee agree that he or she shall perform his or her obligation or bear liability when the obligor fails to perform his or her obligation or any circumstance agreed upon by the parties occurs, in order to ensure the realization of the obligation.

### (1) General Guarantee for Debts

PRC Securities Law	PRC Civil Code
<p><b>Article 19</b> Where the parties have not agreed on the form of guarantee or the agreement is unclear, guarantee liability shall be borne as that of a <i>guarantee with joint and several liability</i>.</p>	<p><b>Article 686</b> ...Where the parties have not agreed on the form of guarantee or the agreement is unclear in a guarantee contract, guarantee liability shall be borne as that of a <i>general guarantee</i>.</p>
<p><i>SPC Interpretation on PRC Securities Law</i>  <b>Article 34</b> Where the creditor in a general deed of guarantee brings a lawsuit against the debtor or applies for arbitration before the expiry of the guarantee term, <i>the limitation period for action to be taken in relation to the guarantee shall be calculated from the effective date of the relevant judgment or arbitration award</i>.            [...]</p>	<p><b>Article 694</b> If the obligee secured by a general guarantee institutes a legal action or applies for arbitration against the obligor before the expiration of the guarantee term, <i>the statute of limitations on the guarantee obligation commences from the date on which the guarantor's right to refuse to assume the guarantee liability is extinguished</i>.            [...]</p>
<p><b>Article 22</b> Where a creditor lawfully assigns a principal credit to a third party during the term of a guarantee, the guarantor shall continue to bear guarantee liability within the scope of the original guarantee.</p>	<p><b>Article 696</b> If the obligee assigns his or her claim, in whole or in part, without notifying the guarantor, such assignment is not binding on the guarantor.</p>

Where the guarantee contract provides for a separate agreement, such agreement shall be observed.	Where a guarantor and an obligee agree that the assignment of a claim is prohibited and the obligee assigns his or her claim without the written consent of the guarantor, the guarantor shall no longer bear guarantee liability in respect of the assignee.
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According to Article 686 of the *PRC Civil Code*, where the parties have not agreed on the form of guarantee or the agreement is unclear in a Guarantee Contract, the guarantee liability shall be borne as that of a general guarantee instead of a guarantee with joint and several obligations. Article 687 of the *PRC Civil Code* defines a general guarantee as a guarantee whereby the parties agree that the guarantor shall bear guarantee liability when the obligor fails to perform his or her obligations. The guarantor under a general guarantee is entitled, if (i) the dispute regarding the principal contract has not undergone litigation or arbitration yet and (ii) the legal enforcement measures have not been made regarding the obligor's property when the obligor still fails to perform his or her obligation, to refuse to assume the guarantee obligations, except under the following circumstances: (i) the whereabouts of the obligor are unknown, and there is no property for execution; (ii) a People's Court has accepted the obligor's bankruptcy case; (iii) where the obligee has evidence to prove that the obligor's property is insufficient to fulfil all the obligations or the obligor loses the ability to perform the obligations; and (iv) the guarantor has indicated in writing a waiver of the right mentioned in this paragraph.

Further, according to Article 694 of the *PRC Civil Code*, the statute of limitations for guarantee obligations now commences from "*the date on which the guarantor's right to refuse to assume the guarantee liability is extinguished*" instead of "*the effective date of the relevant judgment or arbitration award*".

**(2) Guarantor's Right of Recourse in Debts**

<b>PRC Securities Law</b>	<b>PRC Civil Code</b>
<b>Article 31</b> After a guarantor has borne his guarantee liability, he shall have a recourse against the debtor.	<b>Article 700</b> After the guarantor has assumed his or her guarantee liability, except as otherwise agreed upon by the parties, he or she shall have a right of recourse against the obligor to the extent of the guarantee liability assumed by him or her and shall enjoy the rights of the obligee against the obligor provided that the interests of the obligee are not prejudiced.

Article 700 of the *PRC Civil Code* expressly stipulates that the guarantor's right of recourse against the obligor is limited to the extent of the guarantee liability assumed by him or her.



Different from Article 31 of the current *PRC Securities Law*, the guarantor shall further, provided that the interests of the original obligee are not prejudiced, enjoy the rights of the obligee against the obligor. Article 702 of the *PRC Civil Code* now confirms that, where the obligor has the right to offset or cancel against the obligee, the guarantor may, within the corresponding scope, refuse to bear guarantee liability.

### **c) Construction Contracts**

Articles 788 et. seq. of the *PRC Civil Code* deal with Construction Project Contracts, i.e. contracts whereby a contractor performs the construction of a project and a developer pays the price, including contracts for project survey, design and construction.

According to Article 793 of the *PRC Civil Code*, if a construction contract for a construction project is invalid, but the construction project has passed the acceptance inspection, indemnification may be made to the contractor in an amount as agreed upon in the contract. It also deals with the legal consequences where a construction contract for a construction project is invalid, and the construction project fails to pass the acceptance inspection. In such case, the following applies: (i) if the remedied construction project passes the acceptance inspection, the developer may request the contractor to bear the costs of the remedy; and (ii) if the remedied construction project fails to pass the acceptance inspection, the contractor has no right to claim an indemnification. Where the developer is at fault with regard to the losses arising from a substandard construction project, it shall bear the corresponding liability.

Article 806 of the *PRC Civil Code* is newly inserted and stipulates that, where the contractor assigns or illegally subcontracts a construction project, the developer may terminate the contract. The contractor may terminate the contract if the main building materials, components, fittings and equipment provided by the developer fail to meet the compulsory standards, or the developer fails to perform its assistance obligations, resulting in the contractor's failure to perform the construction work, provided that the developer continues to fail to perform the corresponding obligations within a reasonable period after having been urged to do so. If, after a construction contract is terminated, the quality of the completed construction project is qualified, the developer shall pay the corresponding construction price in accordance with the terms of the contract. If the quality of the completed construction project is unqualified, Article 793 of the *PRC Civil Code* shall apply *mutatis mutandis*.

### **d) Technology Transfer Contracts and Technology License Contracts**

Articles 862 to 877 of the *PRC Civil Code* deal with Technology Transfer Contracts and Technology License Contracts. Stipulations on Technology License Contracts have been newly introduced into the contract part. Article 862 newly provides for definitions of Technology Transfer Contracts and Technology License Contracts. I.e. a technology Transfer Contract is “*a contract concluded by the right owner of a lawfully owned technology for transferring the relevant rights to an existing specific patent, patent application or know-how to another person*”. A Technology License Contract is “*concluded by the right owner of a lawfully owned technology for licensing the relevant rights to an existing specific patent and know-how to another person for exploitation and use*”. Article 863 of the *PRC Civil Code* further clarifies that a Technology Transfer Contract and a Technology License Contract shall be made in written form. The other

stipulations regarding Technology License Contracts, are basically the same as the current provisions on Technology Transfer Contracts in the *PRC Contract Law*.

e) **Commission Contracts**

PRC Contract Law	PRC Civil Code
<p><b>Article 411</b> A commission contract shall be terminated by the death, loss of capacity for civil conduct or bankruptcy of the principal or the agent, unless the parties have agreed otherwise or it is inappropriate to terminate the contract given the nature of the entrusted affair(s).</p>	<p><b>Article 933</b> <i>The principal or the agent may terminate a commission contract at any time. Where the other party sustains any loss due to the termination of the contract, except for causes not attributable to the terminating party, the terminating party of a commission contract without compensation shall compensate the other party for direct losses caused by the improper time of the termination, and the terminating party of a commission contract with compensation shall compensate the other party for direct losses and anticipated benefits after the performance of the commission contract.</i></p>

According to Article 411 of the current *PRC Contract Law*, a Commission Contract shall be terminated by the death, loss of capacity for civil conduct or bankruptcy of the principal or the agent, unless the parties have agreed otherwise or it is inappropriate to terminate the contract given the nature of the entrusted affair(s).

According to Article 933 of the *PRC Civil Code*, the principal or the agent may terminate a Commission Contract at any time. Where the other party sustains any loss due to the termination, except for causes not attributable to the terminating party, the terminating party of a Commission Contract without compensation shall compensate the other party for direct losses caused by the improper time of the termination. The terminating party of a Commission Contract with compensation shall compensate the other party for direct losses as well as the anticipated benefits after the performance of the Commission Contract.

f) **Intermediary Contracts**

Articles 961 to 966 of the *PRC Civil Code* deal with Intermediary Contracts, i.e. contracts whereby the intermediary presents to the client an opportunity for entering into a contract or provides the client with intermediary services in connection with the conclusion of a contract and the client pays a remuneration. The original Chinese terminology of Intermediary Contracts has been changed from "居间合同" as used in the current *PRC Contract Law* to "中介合同" in the *PRC Civil Code*.

Article 965 of the *PRC Civil Code* now expressly confirms that where a client uses the trading opportunity or intermediary services provided by the intermediary to bypass the intermediary and directly contracts after accepting the services from the intermediary, the client shall pay

remuneration to the intermediary. Such provision aims to protect the legitimate rights of intermediaries. Further, according to Article 966 of the *PRC Civil Code*, for items in relation to Intermediary Contracts which are not regulated under Articles 961 to 966 of the *PRC Civil Code*, the relevant provisions on Commission Contracts shall apply.

#### **g) Other Changes**

In addition to the above-mentioned changes, the *PRC Civil Code* provides some further changes to the current typical contracts. E.g., according to Article 641 of the *PRC Civil Code*, with regard to retention of title in a sales contract, where the ownership of the subject matter retained by the seller has not been registered, the seller may not challenge any *bona fide* third party. Article 680 of the *PRC Civil Code* now expressly stipulates that it is prohibited to lend at high interest rates and loan interest rates shall not violate the relevant provisions of the State. Further, Article 734 of the *PRC Civil Code* adds that upon the expiration of a lease term, the lessee shall have the priority to lease premises under the same conditions. According to Article 819 of the *PRC Civil Code*, passengers are required to render active assistance and cooperation regarding reasonable arrangements made by a carrier for safe transportation.

#### **h) Newly introduced Typical Contracts**

In addition to the 15 types of typical contracts contained in the current *PRC Contract Law*, 4 additional kinds of typical contracts have been included into Chapter III of the *PRC Civil Code*, i.e. Factoring Contracts, Guarantee Contracts, Property Service Contracts and Partnership Contracts.

##### **(1) Factoring Contract**

Articles 761 to 769 of the *PRC Civil Code* deal with Factoring Contracts, i.e. contracts whereby the obligee of accounts receivable assigns its existing or future accounts receivable to a factor, who provides services such as financial facilities, management or collection of accounts receivable, and guarantees for the payment by obligors of accounts receivable.

So far, there were no specific provisions dealing with factoring in the *PRC Contract Law* and People's Courts normally deal with relevant disputes according to the general stipulations on assignments and in line with the general (international) practices regarding factoring. The *PRC Civil Code* now clarifies the definition, content and form of Factoring Contracts, the legal consequences in case of fictitious receivables, the obligation of the factor to indicate its identity, the consequences of changing or terminating the basic transaction contract without justifiable reasons which has an adverse impact on the factor, factoring with recourse, factoring without recourse, the order of settlement of multiple factorings and the application of the transfer of obligees' rights.

##### **(2) Property Service Contracts**

Articles 937 to 950 of the *PRC Civil Code* deal with Property Service Contracts. Most stipulations have been drafted on the basis of the current *Regulations on Property Management (Revised in 2018)* and the *Interpretations of the Supreme People's Court on Several Issues concerning the Specific Application of Law in Hearing Cases of Property*

*Service Disputes.* A Property Service Contract is a contract whereby a property management service provider provides an owner with property management services, such as maintenance of buildings and auxiliary facilities, environmental cleaning, and management and maintenance of good order in the property management service area, and the owner pays a management fee. Articles 937 to 950 of the *PRC Civil Code*, inter alia, deal with the rights and obligations of property service providers as well as the establishment and termination of Property Service Contracts.

### **(3) Partnership Contract**

Articles 967 to 978 of the *PRC Civil Code* deal with Partnership Contracts and transformed relevant provisions of the current *General Principles of the PRC Civil Law* into the *PRC Civil Code*. A Partnership Contract is an agreement whereby two or more partners share the profits and risks for a common cause. Articles 967 to 978 of the *PRC Civil Code* contain stipulations, inter alia, on the contribution liability of partners, partnership property, decisions on partnership affairs, remuneration of partners, distribution or sharing of profits or losses of a partnership, transfer of property to third parties, the partners' right of subrogation, the term of a partnership, the termination of Partnership Contracts and the distribution of the remaining partnership property.

## **4. Quasi Contracts**

Subpart III, Quasi Contracts, of Chapter III of the *PRC Civil Code* newly provides for general rules on agency without authority (*gestio negotiorum*) and unjust enrichment.

### **a) Agency Without Authority (*Gestio Negotiorum*)**

Articles 979 to 984 of the *PRC Civil Code* deal with agency without authority (*gestio negotiorum*). These provisions, inter alia, state that where an administrator who does not have statutory or contractual obligations manages the affairs of others to avoid losses to the interests of others, the administrator may request the beneficiaries to reimburse the necessary expenses for managing the affairs. Where the administrator suffers losses from managing relevant affairs, the administrator may further request the beneficiaries to pay appropriate compensation. However, where the management matters do not comply with the true intent of the beneficiaries, the administrator shall not be entitled to the rights stipulated above, except where the true intent of the beneficiaries is contrary to laws or public order and morals. Further, the administrator shall manage the affairs of others in a manner in favour of the beneficiaries. Where the discontinued administration is unfavourable to the beneficiaries, it shall not be discontinued without justified reasons. In addition, the administrator shall promptly notify the beneficiaries when managing their affairs (if possible), it shall report the status of administration matters to the beneficiaries upon completion of the respective administration and promptly hand over the property obtained from managing relevant affairs to the beneficiaries.

### **b) Unjust Enrichment**

Articles 985 to 988 of the *PRC Civil Code* deal with unjust enrichment. According to these provisions, where a beneficiary obtains unjust benefits without any legal basis, the person who suffers losses may request the beneficiary to return the benefits obtained, except under any of

the following circumstances: (i) payments made for the fulfilment of moral obligations; (ii) payment of debts prior to maturity; and (iii) repayment of debts knowingly with no payment obligation. Where a beneficiary does not know and should not have known that the benefit it obtains has no legal basis and the benefit it obtains no longer exists, the beneficiary shall not be obligated to return such benefit. Where a beneficiary knows or should have known that the benefit it has obtained does not have a legal basis, the person suffering losses may request the beneficiary to return the benefit it has obtained and compensate the person for his or her losses in accordance with the law. Where a beneficiary has transferred the obtained benefits gratuitously to a third party, the person suffering losses may request the third party to bear the obligation to return the benefits within a corresponding scope.

## 5. Conclusion

Part III of the *PRC Civil Code*, generally, maintains the structure and the main concepts of the current *PRC Contract Law*, while adding numerous clarifications and more detailed stipulations. Altogether, Part III of the *PRC Civil Code* constitutes an improvement compared to the *PRC Contract Law*. However, same as for the other Parts of the *PRC Civil Code*, it still remains to be seen how Part III of the *PRC Civil Code* will be implemented and enforced in practice. Only this will show the real impact of the new law. Further, it is highly expected, but so far still not entirely clear, whether the numerous existing SPC interpretations related to the current *PRC Contract Law* will continue to be effective or whether they will be amended in order to be consistent with the *PRC Civil Code*. The SPC intends to publish an interpretation of the *PRC Civil Code* within this year. It is to be expected that this will provide for more guidance and clarity in this regard and on Part III of the *PRC Civil Code*.

In our series on the new *PRC Civil Code*, next CMS, China will issue a newsletter regarding Chapter VII, Tort Liability, to provide a comprehensive analysis on the tort liability part of the *PRC Civil Code*.

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