

Commercial Contracts 2021

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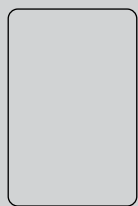
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Duncan Reid-Thomas
Baker McKenzie

Lexology Getting The Deal Through is delighted to publish the sixth edition of *Commercial Contracts*, which is available in print and online at www.lexology.com/gtdt.

Lexology Getting The Deal Through provides international expert analysis in key areas of law, practice and regulation for corporate counsel, cross-border legal practitioners, and company directors and officers.

Throughout this edition, and following the unique Lexology Getting The Deal Through format, the same key questions are answered by leading practitioners in each of the jurisdictions featured. Our coverage this year includes new chapters on Sweden and Ukraine.

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Every effort has been made to cover all matters of concern to readers. However, specific legal advice should always be sought from experienced local advisers.

Lexology Getting The Deal Through gratefully acknowledges the efforts of all the contributors to this volume, who were chosen for their recognised expertise. We also extend special thanks to the contributing editor, Duncan Reid-Thomas of Baker McKenzie, for his continued assistance with this volume.



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CONTRACT FORMATION

Good faith in negotiating

1 | Is there an obligation to use good faith when negotiating a contract?

The Chinese Civil Code, since its effectiveness on 1 January 2021, brought the principle of good faith into the provision of liability for negligence in contracting. Under article 500 of the Chinese Civil Code, when entering a contract, the parties shall not:

- negotiate the contract in bad faith under the pretext of concluding a contract;
- deliberately conceal material facts relating to the conclusion of the contract or providing false information; or
- other acts that violate the principle of good faith.

If a party conducts behaviour as mentioned above and thereby causes losses to the other party, it shall be liable for compensation. In addition to article 500, the Chinese Civil Code also puts good faith as a general principle for all civil activities. Thus, the usage of good faith has become an obligation for parties in the negotiation of a contract.

'Battle of the forms' disputes

2 | How are 'battle of the forms' disputes resolved in your jurisdiction?

When resolving the 'battle of the forms' disputes, the Chinese Civil Code adopts a resolution with reference to the Last Shot Rule and the Knock-out Rule.

The Chinese Civil Code recognises the 'mirror-image' principle by providing that the contents of an acceptance shall be consistent with those of the offer, that is to say, the offeree must accept the terms of the offer in their entirety.

However, as to encourage the formation of a contract and to ensure the business efficiency, the Chinese Civil Code makes a distinction between the substantial alternations and the non-substantial alternations, and only if the offeree substantially alters the contents of the offer, it shall constitute a new offer. Substantial alternations, under the Chinese Civil Code, refers to alternations on the subject matter to the contract, quantity, quality, price or remuneration, time limit, place and method of performance, liability for breach of contract and method of dispute resolution, etc.

If the offeree makes non-substantial alternations to the contents of the offer, the offeree's acceptance shall be effective, and the contents of the contract shall be subject to those of the acceptance, except as rejected promptly by the offeror or indicated in the offer that an acceptance may not alter the offer at all.

On the other hand, under the Chinese Civil Code, an acceptance shall be made by notification, except where acceptance may be made

by an act on the basis of customary business practice or as expressed in the offer.

Based on the above, the 'battle of the forms' dispute is resolved under the Chinese Civil Code by a logic of either 'offer – substantial alternations – new offer – acceptance' or 'offer – non-substantial alternations – acceptance'.

Language requirements

3 | Is there a legal requirement to draft the contract in the local language?

There is no legal language requirement for drafting a contract under PRC law. In practice, parties may draft the contract in a bilingual form with both Chinese and another language, in particular if one of the parties is a foreign undertaking. And according to article 466 of the Chinese Civil Code, where a contract is concluded in two or more languages and it is agreed that all versions are equally authentic, the words and sentences in each version are presumed to have the same meaning. In the case of any discrepancy in the words and sentences used in different versions, they shall be interpreted in accordance with the relevant terms, nature and purpose of the contract as well as the principle of good faith.

Moreover, certain contracts are subject to approval or other procedures in accordance with laws and administrative regulations. In this circumstance, it is better to prepare a Chinese version contract for the competent authority to review.

Signatures and other execution formalities

4 | In what circumstances are signatures or any other formalities required to execute commercial contracts in your jurisdiction? Is it possible to agree a B2B contract online (eg, using a click-to-accept process)? Does the law recognise the validity of electronic and digital contract signatures? If so, how are they treated in comparison to wet-ink signatures?

In general, under PRC law, the parties can conclude a contract in written form or any other form. According to 490(2) of the Chinese Civil Code, the written form requirement of a contract is not mandatory, and does not affect the effect of the contract.

Under normal circumstances, a signature or seal is the proof of the establishing of the contract. According to article 490(1) of the Chinese Civil Code, when the parties conclude a contract in written form, the contract is established when both parties have signed it, affixed their seals thereon or have affixed their fingerprints thereon.

As for the signature and the stamp, in China, a stamp usually prioritises, and has external effect that can be regarded as agency authority. Under PRC law, the company stamp is the externalisation of the company's will and is legally binding, which is of great significance for commercial activities.

It is possible to conclude a contract online under the Chinese Civil Code and E-commerce Law of the PRC.

According to article 469 of the Chinese Civil Code, the parties may conclude a contract in writing, orally or in some other form. Any electronic data that can show, in material form, the contents that it specifies through electronic data exchange or email can be accessed for reference and used at any time and shall be regarded as a written form.

In particular, if the contract is an online sales contract, the click-to-accept process can be adopted. According to article 491(2) of the Chinese Civil Code, where the information of any commodity or service released by one party via the Internet or any other information network meets the conditions of offer, the contract shall be established when the other party selects such commodity or service and submits the order successfully, unless otherwise agreed by the parties. It is also stipulated in the E-commerce Law of the PRC (E-commerce Law), that e-commerce participants using an automated information system to conclude or perform contracts shall be legally binding on the parties using the said system (article 48(1)); and where the information on goods or services announced by an e-commerce business operator satisfies the criteria for making an offer, the contract shall be deemed established if the user selects the said goods or services and submits an order (article 49(1)).

In China, electronic and digital signatures have the same legal validity as a wet-inked signature or affixation of seal, according to the Electronic Signature Law of the PRC (Electronic Signature Law).

Electronic signature, in the Electronic Signature Law, refers to data contained in or attached to a data message in electronic form, which is used to identify the signatory and indicate the signatory's approval of the content therein (article 2(1)). For contracts or other documents and instruments in civil activities, the parties involved may agree to use electronic signature and data message, and shall not deny legal validity on the ground of electronic signature or data message being used (article 3).

However, certain conditions must be satisfied for the electronic signature to achieve legal effect. According to article 13 of the Electronic Signature Law, an electronic signature shall be deemed as reliable electronic signature if it satisfies all the following criteria:

- when the electronic signature creation data is used for electronic signature, it is exclusively proprietary to the electronic signatory;
- the electronic signature creation data is exclusively controlled by the electronic signatory at the time of signing;
- any subsequent alteration to the electronic signature after the signature can be detectable; and
- any subsequent alteration to the content and form of the data message after the signature can be detectable.

Reliable electronic signatures will have the same legal validity as a handwritten signature or affixation of seal.

STATUTORY CONTROLS AND IMPLIED TERMS

Controls on freedom to agree terms

5 | Are there any statutory or other controls on parties' freedom to agree terms in contracts between commercial parties in your jurisdiction?

In general, parties to a contract have the freedom to agree to terms in a contract under PRC law. It is stipulated in article 470 of the Chinese Civil Code, that the contents of a contract shall be agreed upon by the parties, and shall generally contain the following clauses:

- personal names or names and domiciles of the parties;
- subject matter;
- quantity;
- quality;

- price or remuneration;
- time limit, place and method of performance;
- liability for breach of contract; and
- dispute settlement method.

The parties may conclude a contract by reference to a model text of each type of contract.

However, this provision is a guidance on the terms of contract rather than a mandatory requirement. Parties are not necessary bind by those terms, and can adopt their own model text and agreed terms.

However, there are certain conditions that shall be satisfied for the contract to be effective. The previous Contract Law of PRC stipulated some situations in which the contract shall be null and void. The Chinese Civil Code deleted those provisions and combined them into the effect of civil juristic acts. According to articles 146, 153 and 154 of the Chinese Civil Code, the contract shall be null and void if it contains following terms:

- the terms are concluded by persons of civil conduct and counterparties under false manifestation;
- the terms violate the mandatory provisions of laws and administrative regulations; and
- the terms are concluded by a person colludes with his or her counterparty that impair others' legitimate rights and interests.

Besides, certain types of exception clauses in a contract shall be null and void, according to article 506 of the Chinese Civil Code:

- those that cause personal injury to the other party; or
- those involving property damage to the other party as a result of deliberate intent or gross negligence.

Standard form contracts

6 | Are standard form contracts treated differently?

The standard form contracts have legal effect, but the party providing the standard terms shall observe certain obligations stipulated by the Chinese Civil Code.

Standard terms are clauses that are prepared by one party in advance for repeated use and that are not subject to negotiation with the other party when concluding a contract (article 496(1), the Chinese Civil Code).

As the standard terms are drafted in advance by one party without negotiating with the other party, in order to achieve the principle of fairness and protect the legal rights of the other party, the Chinese Civil Code stipulates some specific obligations to the party providing the standard terms:

- shall observe the principle of fairness in determining the rights and obligations of the parties;
- remind the other party in a reasonable way of the provisions that greatly affect the other party, such as those that exclude or mitigate the liability of the party providing the standard terms, 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 reminding or explanation, causing the other party to fail to notice or understand the terms in which it has a material interest, the other party may claim that the terms do not form the contents of the contract.

Moreover, to better protect the other party, where there are two or more interpretations for standard terms, the interpretation unfavourable to the party providing such term shall prevail. Where a standard term is inconsistent with a non-standard term, the non-standard term shall prevail (article 498, the Chinese Civil Code).

Implied terms

7 | What terms are implied by law into the contract? Is it possible to exclude these in a commercial relationship?

In Chinese laws, the concept of 'implied terms' is not introduced as in the Anglo-American laws. According to article 470 of the Chinese Civil Code, the contents of a contract shall include terms of the contract parties, subject matters, quantities, quality requirements, price or remunerations, time limit, places and method of performance, etc.

Although the Chinese Civil Code does not provide which terms are implied by law, it respects the trading practices and recognises that the trading practices could fill in the blank space if there are no express terms. After the effectiveness of a contract, if there is no agreement on the terms regarding quality, price or remuneration or place of performance, or such agreement is unclear, the parties may enter into a supplementary agreement. If no supplementary agreement is reached, the relevant terms of the contract or trading practices shall govern.

Particularly in terms of any warranties on the quality of products, if quality requirements are unclear, the contract shall be performed according to the compulsory national standards. In the absence of compulsory national standards, the recommended national standards shall apply. In the absence of recommended national standards, the industry standards shall be followed; in the absence of national standards or industry standards, the contract shall be performed in accordance with customary standards or specific standards in conformity with the purpose of the contract.

Meanwhile, in some judicial precedents, the Chinese courts may agree that the requirements stipulated in the Product Quality Law should be deemed as an 'implied guarantee' for the quality requirements. Article 26 of the Product Quality Law was cited, which stipulates that product quality shall satisfy the requirements, as follows:

- no unreasonable danger to personal safety or the safety of property shall exist; where there are national or industry standards for protection of health, personal safety and the safety of property, such standards shall be complied with;
- products must possess the properties for use that should be possessed by such products, except for products where flaws in their properties for use are clearly indicated; and
- products must conform to the product standards carried on the product or its packaging, and conform to the quality indicated by such means as the product description and physical samples, etc.

For the requirements stipulated in the Product Quality Law, the provision also clarifies that the first requirement is compulsory and cannot be excluded, while the second is a non-compulsory requirement and could be excluded by agreement.

Vienna Convention

8 | Is your jurisdiction a signatory to the United Nations Convention on Contracts for the International Sale of Goods (the Vienna Convention)?

China signed the United Nations Convention on Contracts for the International Sale of Goods (CISG) in 1981 and approved it on 11 December 1986. China makes a reservation in relation to the application of article 1(1)(b) (ie, this Convention applies to contracts of sale of goods between parties whose places of business are in different states: when the rules of private international law lead to the application of the law of a contracting state, and only adopt CISG among contracting states).

Good faith in entering and performing

9 | Is there an obligation to use good faith when entering and performing a contract?

Good faith is established as a general principle for engaging in all civil actions under Chinese laws. When entering a contract, the Chinese Civil Code establishes that any party that violates the principle of good faith in negotiation shall bear the liabilities for negligence in contracting if losses are incurred by the other party.

Besides, a party shall not disclose or improperly use trade secrets or other confidential information known to it in the course of concluding a contract, no matter whether the contract is established or not; if it discloses or improperly uses such trade secrets or information and causes losses to the other party, it shall be liable for compensation.

When performing a contract, the Chinese Civil Code also establishes that contract parties shall observe the principle of good faith. Meanwhile, the parties shall, not only fully perform their respective obligations as agreed, but also, under the principle of good faith, perform such obligations as notification, rendering assistance and maintaining confidentiality according to the nature and purpose of the contract as well as trading practices.

LIMITING LIABILITY

Prohibition on exclusions and limitations

10 | What liabilities cannot be excluded or limited by a supplier in a contract?

Liabilities exemption or limitation clauses refer to the clause agreed by parties that aim at limiting one party or both parties' liabilities in the future, thus reducing the parties' risks of being claimed. In general, Chinese law allows parties to agree on exemption or limitation clauses, but cannot violate the good faith principle and public interest. According to the Chinese Civil Code, the following exception clauses in a contract shall be null and void:

- those that cause personal injury to the other party; or
- those involving property damage to the other party as a result of deliberate intent or gross negligence.

Furthermore, considering the essence of the exemption or limitation clause is to confirm and allocate perspective risks in advance, in particular to exempt the liabilities incurred by events emerging after the contract has been signed, the parties shall not conceal practical risks occurring before or during the signing of the contract. According to the Chinese Civil Code, where the parties agree to relieve or exempt the liability of the seller for the defects of the subject matter, and the seller fails to inform the purchaser of the defects of the subject matter intentionally or due to gross negligence, the seller shall have no right to claim for relief or exemption of its liability.

Besides, where the exemption or limitation clauses are standard terms, the party providing the standard terms shall observe more obligations. If the party providing the standard terms (1) unreasonably exempts or reduces its liability, increases the liability of the other party or (2) limits the major rights of the other party, or (3) excludes the main rights of the other party, the standard terms shall be null and void.

Financial caps

11 | Are there any statutory controls on using financial caps to limit liability for breach of contract?

Under Chinese laws, the liability for breach of contract is more of a compensation rather than a punishment or a penalty. The circumstances triggering liability for breach of contract are defined as a contracting

party fails to perform its obligations under the contract, or its performance fails to conform to the agreement, and thus causes losses to the other party.

Under such circumstances, the financial caps to limit liability for breach of contract shall be equal to the losses caused by the breach of contract, including the interest receivable after the performance of the contract, but shall not exceed the probable losses caused by the breach of contract that have been foreseen or ought to be foreseen by the breaching party when the contract is concluded. In a case where contract parties agree on liquidated damages, a People's Court or an arbitration tribunal is still entitled to adjust the amount of liquidated damages, if such amount is too inappropriate compared to the actual losses.

Indemnities

12 | Are there any statutory controls on indemnities used to cover liability risks in contracts?

The concept of indemnity does not exist in Chinese laws in relation to commercial contracts.

The indemnities used to cover liability risks in contracts, are concluded by a clause where the contracting party agreed to indemnify and hold harmless the other party from any obligations, liabilities, costs and expenses arising out of its performance of the contract. The indemnities could be unilateral or bilateral, or be triggered under certain circumstances. Once triggered, the indemnities shall become an independent debt in addition to the subject debt of the contract.

Under Chinese laws, there is no provision or stipulation to control indemnity clauses, while in principle, wherever the breach of contract occurs, the breaching party shall compensate for the actual losses due to the breach of contract. The 'inferred reliance' doctrine is rooted in Chinese laws and judicial practices in determining the burden of liabilities due to the occurrence of breach of contract.

Liquidated damages

13 | Are liquidated damages clauses enforceable and commonly used in your jurisdiction?

The liquidated damages are explicitly permitted under Chinese laws. According to Chinese Civil Code, the contract parties may agree on liquidated damages clauses, which could stipulate either a certain sum of liquidated damages in light of the circumstances of the breach or a method for the calculation of damage incurred as a result of breach.

However, the Chinese Civil Code also grants the People's Courts and the arbitration tribunals with the discretion to adjust the amount of liquidated damages. In the circumstances where the amount of liquidated damages agreed upon is lower than the losses incurred, the court or an arbitration tribunal may increase such amount upon the request of the parties based on the actual loss caused by the breach of contract. Where the amount of liquidated damages agreed upon is excessively higher than the losses incurred, the court or the arbitration tribunal may appropriately reduce such amount upon the request of the parties. The amount of liquidated damages can be regarded as 'excessively higher' if it exceeds 30 per cent of the losses caused.

PAYMENT TERMS

Statutory time limits on payments

14 | Are there statutory time limits for paying invoices? Is it possible to agree a different payment period?

There are no mandatory time limits for payment under Chinese laws, instead, the parties can agree on the payment date or period. The purchaser shall pay the purchase price at the agreed time.

Where the time for payment is not agreed or the agreement is not clear, the parties may enter into a supplementary agreement; if no supplementary agreement is reached, the relevant terms of the contract or trading practices shall govern. If the payment time still cannot be determined in accordance with the methods aforementioned, the obligor may perform, and the obligee may request performance, at any time, provided that the other party shall be given the time required for preparation.

Late payment interest

15 | Is statutory interest charged on late payments? Is it possible to agree a different rate of interest?

In a sales contract, the contract parties may agree on liquidated damages or a rate of interest for late payment.

If no agreement is made in the sales contract, when the purchaser delays the payment resulting in a breach of contract, the seller may initiate civil proceedings and claim damages of the late payment interest, where the rate of interest is stipulated by the Interpretation on Issues Relating to Application of Law in Hearing Cases of Disputes over Sales Contracts promulgated by the Supreme People's Court. Article 18 provides that if the breach of contract occurred before 19 August 2019, the Court may make a computation on the basis of the benchmark interest rate of the People's Bank of China for renminbi-denominated loans of the same type and period, and with reference to late penalty interest rate standards; where the breach of contract occurred after 20 August 2019, the Court may make a computation of losses incurred from late payment based on the one-year loan prime rate (LPR) announced by the National Interbank Funding Centre with authorisation of the People's Bank of China at the time of occurrence of the breach of contract, plus 30 per cent to 50 per cent.

Especially with regard to the LPR, the People's Bank of China (PBC) has authorised the National Interbank Funding Center (to release the benchmark loan prime rate (LPR) of the PBC at 9.30am on the 20th of each month (subject to postponement in case of holidays). To date, the latest LPR is 3.85 per cent for one-year loan.

Civil penalties

16 | What are the civil penalties for failing to comply with statutory interest rate or late payment of invoices?

For late payment, the obligee is entitled to request the obligor to continue performance as well as to compensate for the losses due to the late payment.

The interest rate for late payment stipulated in the interpretation fills in the blank space where no agreed rate of interest exists in the contract. Thus, when the obligor fails to comply with the interest rate either agreed by the contract parties or stipulated in the interpretation, the obligee may seek for legal remedies and request the court to order the obligor to undertake the interest for late payment. Once an effective judgment upholds the obligee's claims, the obligee may apply to enforce the obligor's properties by filing at the Enforcement Department of the Court.

TERMINATION

Implied terms

17 | Do special rules apply to termination of a supply contract that will be implied by law into a contract? Can these terms be excluded or limited by including appropriate language in the contract?

There is no special rule applying to termination of a supply contract implied by law. The termination of a contract, under Chinese laws, could be agreed by the contract parties or incur under statutory circumstances provided by law, which according to article 563 of Chinese Civil Code include:

- it is impossible to achieve the purpose of the contract due to force majeure;
- any party expressly states, or indicates through its conduct, that it will not perform its principle debts prior to the expiration of the performance period;
- any party delays in performing its principle debts and fails to perform the same within a reasonable period after being urged to do so;
- any party delays performance of its debts, or has other violations, rendering it impossible to achieve the purpose of the contract; or
- other circumstances stipulated by the law arise.

In addition to the above circumstances, it is also provided in the same article that, if an indefinite-term contract contains the continuing performance of obligations, any party may rescind the contract at any time, provided that it shall notify the other party before a reasonable time limit.

In terms of a supply contract, the performance could be one-time or continuing. For a supply contract of one-time performance, the termination shall follow the performance and if the time limit of performance is not expressly agreed in the contract, according to article 511 of Chinese Civil Code, the obligor may perform, and the obligee may request performance, at any time, provided that the other party shall be given the time required for preparation. Meanwhile, for a supply contract of continuing performance, if the time limit of performance is indefinite, the termination shall apply the rule in article 563, where any contracting party may terminate the contract and provide the other party with a notice period.

Notice period

18 | If a contract does not include a notice period to terminate a contract, how is it calculated?

Previously in the Chinese Civil Code, only several provisions in relation to specific types of contracts mentioned the 'notice period' in the Contract Law, including loan contracts, lease contracts, warehousing contracts, storage contracts, contracting contracts and commission contracts. The common characteristic of the above types of contracts is that the performance is usually continuing. Therefore, in the Civil Code, a new provision is introduced for the indefinite-term contracts with continuing performance: paragraph 2, article 563 provides that if an indefinite-term contract contains the continuing performance of obligations, any party may rescind the contract at any time, provided that it shall notify the other party before a reasonable time limit. According to this provision, the notice period refers to 'a reasonable time limit' from the moment the notice of termination has reached the other party and until the termination has taken effect.

Although 'a reasonable time limit' is a vague method for calculation of a notice period, it could be interpreted in combination with the purpose of the legislation. Generally, in the indefinite-term contracts with continuing performance, the contract parties rely on each other, and if one party terminates the contract at any time, this will cause a sudden attack on the other party and involve unexpected damages. This legislation arrangement of 'a reasonable time limit' acts as a buffer period, so as to protect the contract parties from sudden attacks and unexpected damages. Therefore, the party that wants to terminate the contract unilaterally should fully consider how to prevent itself from such damages when calculating the notice period.

With this concern, article 946 of the Civil Code provides a specific notice period for the contracts of property services, '... where a decision on dismissal is made, the property service provider shall be notified in writing 60 days in advance, unless the contract stipulates otherwise on the notice period.' This provision may be seen as a reference example of determining 'a reasonable time limit'.

Automatic termination on insolvency

19 | Will a commercial contract terminate automatically on insolvency of the other party?

Once the insolvency application of a company is accepted by a People's Court, an administrator will be designated to take over all business of the insolvent company. Those contracts, which were concluded between the insolvent company and other parties prior to acceptance of the insolvency application but are still pending completion by the parties, will not terminate automatically, and will be also handed over to the administrator. The administrator is entitled to decide whether those contracts shall be terminated or be continued and will notify the other contracting parties.

If the administrator, within two months upon the acceptance of insolvency application, has not notified the other contracting parties, or if the other contracting parties, within 30 days upon the receipt of the notification, has not replied to the administrator, the pending contract shall be deemed terminated.

When the administrator decides to continue the contract, the other contracting parties are entitled to request the administrator to provide security for the performance. Under such a request, if the administrator fails to provide security accordingly, the pending contract shall be deemed terminated as well.

For any damages arising from aforementioned termination of contracts, the other contracting parties may declare the credit rights in the insolvency procedures.

Termination for financial distress

20 | Are there restrictions on terminating a contract if the other party is in financial distress?

If a contracting party is in financial distress, it does not necessarily bring about termination of the contract. Under the Chinese Civil Code, if a contract party's business is seriously deteriorating, it shall grant the other party of the unsafe right of defence, which allows the other party to timely notify the party in financial distress and suspend performance of the contract. The resuming of the performance will be subject to a guarantee provided by the party in financial distress. If the party in financial distress fails to restore its capacity for performance or to provide a guarantee within a reasonable time limit, the other party may terminate the contract and request the other party to bear the liability for breach of contract.

Alternatively, in the case that the financial distress causes frustration to the performance of the contract, the principle of change of circumstances will be triggered.

In fact, the principle of change of circumstances had not been officially introduced into Chinese laws until the Chinese Civil Code established it, which provides that, after the conclusion of a contract, if there is a significant change that occurred to the basic conditions of the contract, which was unforeseeable at the time of contract conclusion and was not a commercial risk, causing obvious unjust to a contracting party if the contract is continued to perform, the adversely affected party may renegotiate the contract with the other party. If the renegotiation fails within a reasonable period of time, the contracting parties may seek legal remedies requesting to modify or terminate the contract concerned.

Force majeure

21 | Is force majeure recognised in your jurisdiction? What are the consequences of a force majeure event?

The Chinese Civil Code recognises force majeure and defines it as unforeseeable, unavoidable and insurmountable objective events. In general, if any obligation fails to be fulfilled due to force majeure, the obligor shall be partially or wholly exempted from liability in light of the impact of the force majeure

Where the force majeure causes a failure to perform a contract, the obligor shall notify the other party in time to reduce any possible losses, and shall provide proof within a reasonable time limit.

Furthermore, if the force majeure makes it impossible to achieve the purpose of the contract, the contracting parties may terminate the contract.

However, the exemption of liability under force majeure is not applicable if the force majeure occurs after any party has delayed its performance.

Interestingly, before the Chinese Civil Code, force majeure was excluded from the conditions of the change of circumstances, that is to say, the change of circumstances could not be invoked due to force majeure. The Chinese Civil Code, however, removes such distinction. Thus, the consequences of the change of circumstances, such as renegotiation on the contract, are also adaptable to the cases of force majeure.

SUBCONTRACTING, ASSIGNMENT AND THIRD-PARTY RIGHTS

Subcontracting without consent

22 | May a supplier subcontract its obligations under the contract without seeking consent from the other party?

Under Chinese laws, if the supplier subcontracts all or part of its obligations to a third party, the consent of the other party must be obtained. The supplier or the third party may urge the other party to give its consent within a reasonable period, where no reaction of the other party is deemed dissent.

On the other hand, the Chinese Civil Code also establishes that if the third party joins the supplier to perform the obligations, the consent of the other party is not necessary to be obtained. In this case, the third party or the supplier needs to notify the other party, and, as long as the other party does not explicitly reject within a reasonable period, the other party will be entitled to request the third party to perform the obligations.

Statutory rules

23 | Are there any statutory rules that apply to subcontracting in your jurisdiction?

The Chinese Civil Code provides several rules on general contract, and the party shall obtain the consent of the other party if it intends to subcontract all or part of its obligations to a third party.

With respect to construction contracts, there are specific statutory rules in the Chinese Civil Code, alongside with regulations on construction projects promulgated by State Council. If the construction projects involve bidding and tendering, the Bidding Law of the People's Republic of China shall also apply.

Although under the general rules, the supplier may subcontract all obligations with the consent by the other party, in a construction contract, the supplier is not allowed to subcontract the entire construction project to a third party, nor may it split the construction project into parts and subcontract each part respectively to a third party in the name of subcontracting.

After subcontracting, the third party will bear joint and several liabilities with the supplier on the subcontracted parts of the construction project.

In addition, the third parties who accept such subcontracts should be qualified in accordance with laws and regulations. If there is any illegal subcontracting, the other party to the construction contract may unilaterally terminate the contract.

Assignment of rights and obligations

24 | May a party assign its rights and obligations under the contract without seeking the other party's consent?

For assignment of obligations, as aforesaid, the assignor shall obtain consent from the other party, and no reaction of the other party is deemed dissent. In a case where the third party joins the assignor to perform the obligations, the assignor or the third party should notify the other party and unless the other party explicitly rejects, it is deemed that such join is recognised by the other party.

For assignment of rights, on the other, the consent of the other party to the contract is not required, but in the following circumstances, all or parts of the rights cannot be assigned:

- such rights may not be assigned in light of the nature thereof;
- such rights may not be assigned according to the agreement between the contract parties; or
- such rights may not be assigned according to the provisions of the laws.

In particular, in cases where the parties have agreed not to assign such rights, if such rights are non-monetary, the agreement shall not act against a bona fide third party; if such rights are monetary, the agreement shall not act against any third party.

Upon the assignment of rights, the assignor should notify the other party, and if the other party is not notified, such an assignment of rights is not binding to the other party. The notification is not revokable, unless the third party accepts the assignment and gives its consent.

In a case where the assignor assigns both rights and obligations, the consent of the other party is a must, but the other controls on the assignment of rights and the assignment of obligation shall apply respectively.

25 | What statutory controls apply to the assignment of rights or obligations under a supply contract?

In a supply contract, the assignment of rights or obligations are first subject to statutory control of general rules regarding the assignment of rights or obligations of a contract provided in the Chinese Civil Code.

In relation to the assignment of receivables of a supply contract, it usually involves a factoring contract signed between the supplier and a third party (called a factor) under Chinese laws.

If the third party is a commercial factoring enterprise, such transaction will be subject to the regulation and supervision of the China Banking and Insurance Regulatory Commission (CBIRC). According to the Notice of the General Office of the CBIRC on Strengthening Supervision and Administration of Commercial Factoring Enterprises, a commercial factoring enterprise should comply with certain regulatory requirements.

Enforcement by third party

26 | How may a third party enforce a term of the contract?

In principle, the Doctrine of Privity shall apply in the enforcement of a contract (ie, where the parties agree that the obligor shall perform the obligation for the benefit of a third party, or those obligations owed to the obligee shall be performed by a third party, and the obligor or the third party does not perform the obligation or does not perform in conformity with the parties' agreement, the obligor shall be liable to the obligee for breach of contract).

However, since the effectiveness of the Chinese Civil Code, the contract for a third party has been introduced and established under Chinese laws, where the third party is allowed to enforce the terms of a contract. Article 522 of the Chinese Civil Code provides if the contract

parties agree that the obligor performs obligations for a third party and that a third party may directly request the obligor to perform the obligations, as long as the third party does not specifically reject within a reasonable period, once 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 for breach of contract and the third party may request the obligor to bear liability for breach of contract; the obligor may, in respect of the third party, avail itself of any defence it has against the obligee.

Except for the aforementioned circumstances, in a case of subrogation, the third party may also enforce the terms of a contract upon the demand of the obligee. The subrogation refers to if the obligor is remiss in enforcing its contract rights or the accessory rights related to its claims, thereby affecting the realisation of the due claims of the obligee, the obligee claims to the People's Court to enforce the contract rights of the obligor against the counterparty in subrogation in its own name. However, the scope of subrogation shall be limited to the due claims of the obligee.

DISPUTES

Limitation periods

27 | What are the limitation periods for breach of contract claims? Is it possible to agree a shorter limitation period?

According to the Chinese Civil Code, the ordinary limitation period for breach of contract claims is three years. The limitation period for claims for disputes arising from an international contract for the sales of goods or a contract for the import and export of technology is four years.

The above limitation periods start from when the claimant knows or should have known the facts giving rise to his or her claim and who the accused is. In any event, if more than 20 years have passed since the date of the occurrence of facts giving rise to the claim, the court shall not offer any protection.

The law provides rules to suspend the limitation period if, within the final six months of the limitation period, the rights to 'demand' cannot be exercised because of any of the following statutory obstacles:

- force majeure;
- the person who has no or limited capacity for civil conduct has no statutory agent, or his or her statutory agent dies or loses the capacity for civil conduct or the power of agency;
- neither a successor nor a legacy caretaker has been determined after the commencement of succession;
- the obligee is controlled by the obligor or other persons; and
- other obstacles resulting in the failure of the obligee to exercise the right of claim.

The limitation period will be resumed after the causes of such suspension are eliminated.

In addition to suspension, the limitation period can be interrupted according to law. The limitation period is interrupted if legal proceedings are instituted or if a party demands or agrees to the fulfilment of its obligations. The limitation period commences anew from the time of interruption and can be interrupted repeatedly.

Article 197 of the Chinese Civil Code further regulates that the periods, calculation methods and reasons for a suspension or interruption in respect of the limitation of action shall be prescribed by law and those agreed by and between the parties shall be null and void. A party's prior waiver of the benefit of the limitation of action shall be null and void.

Choice-of-law clauses

28 | Do your courts recognise and respect choice-of-law clauses stipulating a foreign law?

Under PRC laws, parties to a contract with foreign elements are permitted to choose a foreign law as the governing law for their contract. The following factors are considered in determining whether a contract has foreign elements:

- whether any party is a foreign party or resides in a foreign country;
- whether the object of the contract is located in a foreign country;
- whether the contract is signed, performed, revised or transferred in a foreign country; or
- whether factors that affect the rights and obligations of the parties take place in a foreign country.

For some special contracts, such as Sino-foreign equity joint venture contracts, Sino-foreign cooperative joint venture contracts and Sino-foreign cooperative contracts for the exploitation and development of natural resources in China must be governed by PRC law. Choice of a non-PRC law for these contracts is not valid.

Besides, where a party intentionally creates a link to foreign elements to circumvent the mandatory provisions of PRC laws and regulations, the People's Court will hold that the foreign law cannot be applied.

29 | Do your courts recognise and respect choice-of-jurisdiction clauses stipulating a foreign jurisdiction?

With respect to foreign-related disputes over contracts or other property rights, Chinese courts recognise choice-of-jurisdiction clauses stipulating a foreign jurisdiction, though such choice of jurisdiction, according to article 531 of Interpretation of Supreme People's Court on the Application of the Civil Procedure Law of the People's Republic of China (Amended in 2020), shall satisfy the following conditions:

- The foreign jurisdiction should be actually associated with the disputes, such as the place where the defendant is domiciled, the place where a contract is performed, the place where a contract is signed, the place where the plaintiff is domiciled, the place where the subject matter is located, or the place where the infringing act is committed, etc.
- The choice of jurisdiction shall not violate the exclusive jurisdiction of Chinese courts stipulated in articles 33 and 266 of the Chinese Civil Procedure Law, for example, in the case of a real estate dispute lawsuit where the real estate is located in China, the Chinese court at the location of the real estate shall have the exclusive jurisdiction.

In practice, if one of the contract parties brings a lawsuit at a Chinese court while the contract in dispute includes a choice-of-jurisdiction clause of a foreign jurisdiction, the Chinese court will put its focus on whether such clause excludes jurisdiction of Chinese courts when determining the recognition of choice of jurisdiction. There have been precedents of recognising the choice of a foreign jurisdiction in recent years.

Efficiency of local legal system

30 | How efficient and cost-effective is the local legal system in dealing with commercial disputes?

Normally, a general procedure for a civil claim at first instance is concluded within six months from the commencement of the proceeding. If there is a need for an extension under special circumstances, an extension of six months may be granted, subject to the approval of the president of the court. If there is a need for a further extension, the approval of the higher-level court is required.

However, the period for trial of foreign-related civil cases by courts is not subject to the abovementioned time limits and restrictions. Therefore, in practice, the efficiency of the trial has a high degree of arbitrariness depending on the varied competency and capability of local judges from city to city.

New York Convention

- 31 | Is your jurisdiction a signatory to the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards? Which arbitration rules are commonly used in your jurisdiction?

China acceded to the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards on 22 January 1987.

In China, the leading arbitration institution handling foreign-related disputes is CIETAC and CIETAC procedural rules are the most commonly used arbitration rules in China. The most recent version of the CIETAC arbitration rules came into effect on 1 January 2015.

REMEDIES

Available remedies

- 32 | What remedies may a court or other adjudicator grant? Are punitive damages awarded for a breach of contract claim in your jurisdiction?

Depending on the nature of disputes, common substantive remedies include damages compensation, permanent injunctions and specific performance.

In civil litigation, remedies are mostly compensatory, with punitive damages as an exception. However, according to the opinions of the Supreme People's Court on strengthening the punishment of intellectual property infringement, in the field of intellectual property, if the circumstances are serious, the right holder's claims of punitive damages shall be supported according to law, and the deterrent effect of punitive damages on intentional infringement shall be fully exerted.

UPDATE AND TRENDS

Recent developments

- 33 | Are there any other current developments or emerging trends that should be noted?

Development of the Chinese Civil Code in China, replacing the Contract Law and other major Chinese laws

The Chinese Civil Code has been effective since 1 January 2021. In the contract law section of the Chinese Civil Code, several important modifications are made to the current Contract Law. These are:

- specific provisions are provided for conclusion and performance of electronic contracts;
- relevant rules for sales contract, contract preservation, loan contracts and financial leasing contracts have been improved; and
- the protection of creditors is strengthened; and
- the principle of changed circumstances is also included.

After the Chinese Civil Code became effective, it has repealed and replaced the prevailing effective Contract Law, Property Law, Securities Law, Marriage Law, Adoption Law, Inheritance Law and Tort Liability Law.

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Coronavirus

- 34 | What emergency legislation, relief programmes and other initiatives specific to your practice area has your state implemented to address the pandemic? Have any existing government programmes, laws or regulations been amended to address these concerns? What best practices are advisable for clients?

There is no major amendment or legislation, but there are some temporary regulations and notices (especially from local courts) to help China go through this crisis.

Improving regulations on force majeure, affirming that both the epidemic and epidemic prevention measures may constitute force majeure.

Legislative Affairs Commission of the Standing Committee of the National People's Congress clarified on 10 February 2020 that 'the current epidemic has occurred in China, and the government has taken corresponding epidemic prevention measures to protect public health. For the party who cannot perform the contract as a result, it is force majeure that cannot be foreseen, avoided and overcome.'

Many high courts have also made it clear in their guidance that parties may raise the defense of force majeure where the epidemic and epidemic prevention measures affect the performance of the contract. (See the notices made by the high courts in Zhejiang, Hubei, Jiangsu and Fujian provinces.)

Improve the provisions on changed circumstances, affirming that both epidemic conditions and epidemic prevention measures may constitute a changed circumstance.

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