Part I General Part

Chapter 1. Overview

Literature: *Bu Yuanshi* (ed.), Chinese Business Law, Munich/Oxford 2010. *Liang Huixing* (梁慧星), General Introduction to Civil Law (4. ed.) (民法总论), Beijing 2011. *Li Minghua* (李明华), Civil Legal Capacity of Partnership Business (论合伙企业的民事权利能力), Journal of Sichuan Normal University (Social Sciences) (四川师范大学学报(社会科学版)) 2000, No. 3, 30–35. *Liu Kaixiang* (刘凯湘), General Introduction to Civil Law (3. ed.) (民法总论), Beijing 2011. *Ran Hao* (冉昊)/*Du Lihong* (杜丽红), The Way to Rule of Law in New China: A Review of Civil Law in a History of 56 Years (新中国法治历程民法56年), Journal of Nanjing University (Philosophy, Humanities and Social Sciences) (南京大学学报(哲学.人文科学.社会科学版)) 2005, No. 4, 66–75. *Wang Liming* (王利明), The Personal Experience of the Legislating Process of the General Principles of Chinese Civil Law (关于民法通则的制定), Chinese People's Congress Journal (中国人大2011, No. 7, 26. *Yang Lixin* (杨立新)/*Wang Yi* (王轶)/*Wang Zhu* (王竹)/*Wang Tianfan* (王天凡)/*Zhao Ke* (赵可), The Thirty Years of Chinese Civil Law (中国民法学三十年), Beijing 2008. *Zhang Chi* (张驰), The Analysis of Legal Person's Ability (法人能力论), Journal of East China University of Political Science and Law (华东政法大学学报) 2009, No. 3, 43–52. *Zhang Xinbao* (张新宝), The Current Development and Future of Chinese Civil Law (中国民法和民法学的现状与展望), Law Review Journal (法学评论) 2011, No. 3.

I. Evolution of Chinese Civil Law

The equivalent Chinese word for civil law is "民法", which includes two characters: 民 and 法. The character 民 (*Min*) means "people" and the character 法 (*Fa*) means "law". Therefore, a simple way to translate civil law in Chinese is "the law of people". 1

In the current Chinese legal system, the Constitution[1] sets out (i) the fundamental rights and obligations of each citizen and (ii) the structure of the country. Following the general principles stated in the Constitution, civil law, criminal law, and administrative law are the three most important substantial law constituents[2] of the Chinese legal system, ranking beneath the Constitution and each covering a crucial and different area of legal relations. As described by art. 2 of the General Principles of Civil Law (GPCL)[3], civil law deals with property and personal relationships among citizens and legal persons. The focus of civil law is to regulate legal relations between equal counterparts. 2

However, unlike other civil law jurisdictions, the People's Republic of China (PRC) has not yet enacted one comprehensive modern civil code. Since 1949, there have been at least four rounds of drafting projects mandated by the National People's Congress (NPC) with the goal of creating a comprehensive Chinese civil code. The first round produced a draft in 1956, which was based on the Civil Code of the Soviet Union. The second code was drafted in 1964 and highlighted the 3

[1] 宪法, promulgated on and effective from 4th December, 1982.
[2] Together with the corresponding procedure laws.
[3] 民法通则, promulgated by the NPC on 12th April, 1986 and effective from 1st January, 1987.

characteristics of a planned economy. The start of China's reform and "open door" policy in 1978 triggered the establishment of a new civil law drafting committee. However, after the third attempt to prepare a complete civil code failed, due to various reasons[4], the GPCL[5], based on the principle of "only including well developed provisions"[6], was eventually enacted on 12th April, 1986. The GPCL is neither a comprehensive civil code nor a piece of legislation focusing on one particular civil law subject. Some scholars referred to it as a "quasi" civil code[7] and praised it for strengthening the protection of private rights and reducing the influence of the Civil Code of the Soviet Union[8]. Given the fast development of China's economy, the NPC formally started the fourth round of drafting a thorough civil code in 2002. This consisted of a clear, initial plan to separately complete the legislation of all-important subjects of civil law, especially contract law and property law, and then to assemble a comprehensive civil code.

4 Although the majority of Chinese legal scholars agree that China should have a unified civil code, there has not been a universally accepted opinion on its general structure. The most popular of these schools of thought include: (i) the open and loose structure, (ii) the classical Roman/French civil law structure following *Institutiones*, and (iii) the classical German Civil Code structure following *Pandektae*.[9] Furthermore, some experts have preferred to have a separate code for private international law rather than to include it in the civil code.[10] It has also been argued that intellectual property law should be added to the civil code.[11] The 2002 draft of the civil code consists of nine parts: (1) general provisions, (2) law of real rights, (3) law of contract, (4) law of personality rights, (5) law of marriage, (6) law of adoption, (7) law of succession, (8) law of tort liability, and (9) private international law.[12]

II. Sources of Civil Law

5 As mentioned above, the PRC has not yet enacted its comprehensive civil code. However, this does not imply there is no well-developed civil law in China. Following continuous efforts made by Chinese legislators and legal scholars over the last 30 years, civil law has already become the most developed and heavily legislated subject in China. Currently, apart from the fundamental rules set out in the constitution, there are roughly six different categories of sources of civil law listed below, which cover most areas expected to be included in a comprehensive civil code.[13]

[4] *Yang Linxin/Wang Yi/Wang Zhu/Wang Tianfan/Zhao Ke*, 99. The most important debate during that period was between the development of civil law and economic law. It was argued by some scholars that it is unnecessary to have civil law since the relevant rules are already covered under the wider concept of economic law. *Ran Hao/Du Lihong*, 68.

[5] It was regarded as a mini version of the civil code. *Zhang Xinbao*, 103.

[6] 成熟一条制定一条, *Wang Liming*, 26.

[7] *Liu Kaixiang*, 2.

[8] *Liang Huixing*, 22.

[9] *Yang Lixin*, 101.

[10] *Liu Kaixiang*, 18.

[11] Ibid.

[12] *Liu Kaixiang*, 17–18.

[13] Some scholars argue that there are three general sources of law: legislations, state policies and customs. *Liu Kaixiang*, 30–34.

(1) Main statutes in relation to civil law enacted by the NPC and its Standing 6
Committee: GPCL, Contract Law (CL)[14], Real Rights Law[15], Security Law[16], Law on Tort Liability[17], Succession Law[18], Marriage Law[19] and Adoption Law[20].

(2) Administrative regulations issued by the State Council or the relevant 7
ministries: Regulations for the Registration of Enterprises as Legal Persons[21], Interim Regulations on Registration and Administration of Institutions[22], Regulations on Registration and Administration of Associations[23], Provisional Regulations for the Registration and Administration of Privatly-Run Non-Enterprise Institutions[24], Regulations on Foundation Administration[25], and Implementation Rules for Regulations on the Registration of Enterprises as Legal Persons[26].

(3) Judiciary interpretations issued by the Supreme People's Court (SPC). 8
Although China has a codified legal system and an earlier court judgement does not automatically bind future court proceedings, in practice, the official interpretation issued by the SPC does have binding authority and is followed by legal practitioners in order to clarify difficult civil law related issues. Important judiciary interpretations issued by the SPC in respect of the civil law issues include: Opinions of the SPC on Several Issues Concerning the Implementation of General Principles of Civil Law of the People's Republic of China (Trial)[27], the SPC Rules on Certain Issues concerning the Implementation of a Period of Limitations in Civil Litigation[28], the Opinions of the SPC on Certain Issues Regarding the Implementation of the Civil Procedure Law of the People's Republic of China[29], SPC Interpretation on Several Issues Concerning the Application of the Contract Law of the People's Republic of China (Part I)[30], Interpretation of the SPC on Several Issues Concerning the Application of the

[14] 合同法, promulgated by the SCNPC on 15th March, 1999 and effective from 1st October, 1999.

[15] 物权法, promulgated by the NPC on 16th March, 2007 and effective from 1st October, 2007.

[16] 担保法, promulgated by the SCNPC on 30th June, 1995 and effective from 1st October, 1995.

[17] 侵权责任法, promulgated by the SCNPC on 26th December, 2009 and effective from 1st July, 2010.

[18] 继承法, promulgated by the NPC on 4th October, 1985 and effective from 1st October, 1985.

[19] 婚姻法, promulgated by the NPC on 10th September, 1980 and effective from 1st January, 1981.

[20] 收养法, promulgated by the NPC on 29th December, 1991 and effective from 1st April, 1992.

[21] 企业法人登记管理条例, promulgated by the State Council on 3rd June, 1988 and effective from 1st July, 1988.

[22] 事业单位登记管理暂行条例, promulgated by the State Council on effective from 25th October, 1998.

[23] 社会团体登记管理条例, promulgated by the State Council on 25th October, 1998 and effective from 25th October, 1998.

[24] 民办非企业单位登记管理暂行条例, promulgated by the State Council on 25th October, 1998 and effective from 25th October, 1998.

[25] 基金会管理条例, promulgated by the State Council on 8th March, 2004 and effective from 1st June, 2004.

[26] 企业法人登记管理条例施行细则, promulgated by SAIC on 3th November, 1988 and effective from 1st December, 1988.

[27] 最高人民法院关于贯彻执行《中华人民共和国民法通则》若干问题的意见(试行), promulgated on 26th January, 1988 (hereinafter: Opinions on the GPCL).

[28] 最高人民法院关于审理民事案件适用诉讼时效制度若干问题的规定, promulgated on 21st August, 2008 and effective from 1st September, 2008.

[29] 最高人民法院关于适用《中华人民共和国民事诉讼法》若干问题的意见, promulgated on 14th July, 1992.

[30] 最高人民法院关于适用《中华人民共和国合同法》若干问题的解释(一), promulgated on 19th December, 1999 and effective from 29th December, 1999.

Contract Law of the People's Republic of China (Part II)[31]; and Interpretation of the SPC on Several Issues Concerning the Application of the Security Law of the People's Republic of China[32].

9 (4) Regulations enacted by a provincial congress which sets out specific implementation rules applicable in the relevant province.

10 (5) State policies. Art. 6 of the GPCL states that if there is no applicable rule expressly provided by law, the relevant civil activity should comply with state policies. This seems to be a part of the remains from the transitional period between the earlier planned economy and the current market-oriented economy. It is worth repeating that the GPCL was enacted in 1986, an early stage of China's economic reform.

11 (6) Local customs. The GPCL does not expressly refer to local customs. However, some leading scholars hold the view that local customs should be included as a source of civil law rules and quote art. 85 Real Rights Law as an example.[33] In accordance with art. 85 Real Rights Law, unless there are relevant rules set out by law or regulation, the neighbouring relations should be dealt with pursuant to local customs.

III. General Principles

12 The Chinese legal system is a codified one, and unlike common law jurisdictions, previous court judgements do not have an automatically binding effect. Meanwhile, legal practitioners cannot expect the SPC to issue judicial interpretations to clarify every point. As a result, almost every major piece of legislation in China sets out a series of its general principles. If there is any ambiguity in understanding an issue in a statute and that point is not covered by the judicial interpretation previously issued by the SPC, the relevant general principles will be used to infer an appropriate interpretation.

13 In this regard, there is no exception to the Chinese civil law. It is generally agreed among Chinese legal scholars that the basic principles of civil law should apply throughout the civil law legislative process, judicial determination, and relevant civil activities.[34] Therefore, before analysing any specific concept, it is important to understand the general principles of Chinese civil law.

14 At present, the GPCL is the fundamental statute which sets forth all the basic principles and concepts in the Chinese civil law family. However, the details regarding the basic principles of civil law remain a heatedly debated subject among Chinese legal academics.[35] Five general principles, as arranged below, are commonly referred to by legal scholars: legal protection of civil rights, equal status, freedom of contract, good faith, and public policy.[36]

[31] 最高人民法院关于适用《中华人民共和国合同法》若干问题的解释(二), promulgated on 24th April, 2009 and effective from 13th May, 2009.

[32] 最高人民法院关于适用《中华人民共和国担保法》若干问题的解释, promulgated on 8th December, 2000 and effective from 13th December, 2000.

[33] *Liang Huixing*, 27–28.

[34] *Yang Lixin*, 102.

[35] Ibid. Some scholars believe that there are five general principles while others list six, *Liu Kaixiang*, 26–30; *Liang Huixing*, 46–52.

[36] *Liu Kaixiang*, 26–30.

1. Principle of Legal Protection of Civil Rights

The essence of this principle is straightforward: any natural person or legal person's legal civil rights are protected by law and are not allowed to be infringed by any other organisation or individual.[37] In contrast, with emphasis on protecting the assets of the state and the power of the government, the focus on protecting civil rights of each individual or legal person is widely regarded as the direction of Chinese civil law development. Many Chinese scholars either rank this principle as the first general principle or categorise it as the fundamental principle and purpose of Chinese civil law.[38] 15

2. Principle of Equal Status and Principle of Freedom Of Contract

Art. 3 GPCL makes it clear that each party has equal status in any civil activity. Even if one party is a public authority, when dealing with civil issues, such as entering into a contract with subjects governed by civil law, it is prohibited from enforcing the relevant counterpart to agree to any terms against their free will. This logically links with the Principle of Freedom of Contract. Unless otherwise restricted by law, the parties are free to negotiate the terms of civil activity between them. 16

The Principle of Equal Status is particularly important in a jurisdiction which has experienced the transition from a planned economy to a market-oriented economy, since in a planned economy a contractual party may be forced to enter into an unfair agreement following the supply and demand plan set out in advance by the state.[39] 17

3. Principle of Good Faith

Pursuant to art. 4 GPCL, civil activities should follow the Principle of Good Faith. This principle requires parties (i) to ensure fairness and equality of each civil activity, (ii) to respect counterparties' rights, and (iii) to avoid abusing his/her own civil rights.[40] This is the moral standard in a market-oriented economy.[41] Art. 6 CL also expressly requires contractual parties to carry out their rights and perform their obligations in accordance with the Principle of Good Faith. 18

For example, in the case of *Changsha Xianfeng Branch of the Agricultural Bank of China v Hunan Golden Sail Investment Management Co., Ltd. and Changsha Jinxia Construction & Development Co., Ltd.* in respect to a dispute regarding a loan agreement and corresponding security agreement,[42] the purpose of the loan, as manually written in the original loan agreement provided by the bank, is to be used as "working capital and for the repayment of a pre-existing loan". However, the purpose of the loan, as manually written in the original loan agreement provided by the mortgagor, is only to be used as "working capital". The mortgagor refused to perform its obligations as the mortgagor when the borrower used the new loan to repay pre-existing debt and consequently failed to repay the new loan on the basis 19

[37] Art. 5 GPCL.

[38] *Liu Kaixiang*, 26–37; *Liang Huixing*, 42–44.

[39] *Liang Huixing*, 46.

[40] *Liu Kaixiang*, 29.

[41] *Liang Huixing* 269.

[42] 中国农业银行长沙市先锋支行与湖南金帆投资管理有限公司长沙金霞开发建设有限公司借款担保合同纠纷案, judgement of the SPC dated 28th April, 2008.

exercised either within one year from the date the creditor knows or should have known of the improper act or within five years from the occurence of the improper act.[82]

3. Legal Effect of Right of Invalidation

62 If the court invalidates the obligor's act, then the act will be invalid *ab initio*.[83] Where the disposal of the property is declared void, any property recovered from a third party would become the obligor's property again. The creditor who excerises the right of invalidation has no priority in satisfaction.[84] The creditor is not allowed to use the property recovered initially for settling debts owed by the obligor. On the contrary, all creditors have equal rank for demanding satisfaction of their debt.

[82] Art. 75 CL.
[83] Art. 25 of the Interpretation of the CL (Part I).
[84] *Han Shiyuan*, 418; *Wang Liming* (2003), 519.

Chapter 7. Liability for Breach of Contract

Literature: *Cheng Xiao* (程啸), Breach of Contract and Non-pecuniary Damage (违约与非财产损害赔偿), Civil and Commercial Law View Vol. 25 (民商法论丛第25卷) 2002, 70–116. *Cui Jianyuan* (崔建远), On the Nature and Status of Guarantee Liability against Defects of Goods (物的瑕疵担保责任的定性与定位), China Legal Science (中国法学) 2006, No. 6, 32–43. *Cui Jianyuan* (崔建远), Contract Law (合同法), Beijing 2010. *Gu Angran* (顾昂然), Lectures on the Contract law of the People's Republic of China (中华人民共和国合同法讲话), Beijing 1999. *Han Shiyuan* (韩世远), Non-Pecuniary Damage and Contract Liability (非财产上损害与合同责任), Law Science (法学) 1998, No. 6, 27–30. *Han Shiyuan* (韩世远), Pandect of Contract Law (合同法总论), Beijing 2004. *Han Shiyuan* (韩世远), Seller's Guarantee Liability against Defects of Goods and Chinese Contract Law (出卖人的物的瑕疵担保责任与我国合同法), China Legal Science (中国法学) 2007, No. 3, 170–190. *Li Guohui* (李国慧), An Interview with Song Xiaoming, the Presiding Judge of the No. 2 Civil Division of the Supreme People's Court, on the Issues on Contract Law Practice (就合同法司法实务相关问题访最高人民法院民二庭庭长宋晓明), Journal of Law Application (法律适用) 2009, No. 11, 10–13. *Li Yongjun* (李永军), Contractual Remedy for Non-Pecuniary Damage and its Legitimacy (非财产性损害的契约救济及其正当性), Journal of Comparative Law (比较法研究) 2003, No. 6, 47–62. *Ning Hongli* (宁红丽), Study on Travel Contract (旅游合同研究), Civil and Commercial Law View Vol.22 (民商法论丛第22卷) 2002, 19–67. *Qi Yingyang* (齐鹰扬)/*Wu Hong* (伍红), Issues on the Application of Law in Concurrence between Liability for Breach of Contract and Tort, Legal Analysis on the Case between Zhang and Bus Company 2nd Branch (违约责任与侵权责任竞合案件审理中的法律适用问题——张某与公交总公司二分公司赔偿纠纷案法律分析), (ed.) Beijing High People's Court (北京人民高级法院), Studies on Difficult Cases (疑难案例实务研究), Beijing 2002, 195–202. *Wang Chuang* (王闯), Issues on the Application of Law in Hearings concerning Commercial Contract Disputes by the People's Court (当前人民法院审理商事合同案件适用法律若干问题), Journal of Law Application (法律适用) 2009, No. 9, 3–8. *Wang Hongliang* (王洪亮), On the Risk Allocation Rule on Impediments in Performance, Comments on the Objective Liability System in Chinese Contract Law (试论履行障碍风险分配规则——兼评我国<合同法>上的客观责任体系), China Legal Science (中国法学) 2007, No. 2, 85–95. *Wang Hongliang* (王洪亮), On Guarantee Liability of Flaws of Things, Leistungsstörungsrecht and Culpa in Contrahendo (物上瑕疵担保责任履行障碍法与缔约过失责任), Science of Law (法律科学) 2005, No. 4, 64–74. *Wang Liming* (王利明), A Comparative Study on Chinese and German Sales and Purchase Contracts (中德买卖合同制度的比较), Journal of Comparative Law (比较法研究) 2001, No. 1, 21–37. *Wang Liming* (王利明), Study on the Contract Law Vol. 2 (合同法研究第二卷) Beijing 2003. *Wang Liming* (王利明), On Liability for Breach of Contracts (违约责任论), Beijing 1996. *Wang Liming* (王利明)/*Cui Jianyuan* (崔建远), Restatement on Pandect of the Contract Law (合同法新论· 总则), Beijing 2000. *Xiao Xun* (肖峋)/*Wei Yaorong* (魏耀荣)/*Zheng Shuna* (郑淑娜), Interpretation of the Contract Law of the People's Republic of China (Pandect) ((中华人民共和国合同法释论(总则)), Beijing 1999. *Yang Lixin* (杨立新), The Influence of Earthquakes as and Event of Force Majeure in Civil Law (地震作为民法不可抗力事由的一般影响), Political Science and Law (政治与法律) 2008, No. 8, 2–9.

I. Overview

1. Definition of Breach of Contract

Chinese contract law provides several types of remedies for the aggrieved party in 1
cases of an obligee's breach of a contract duty, including specific performances, the cure of non-conforming performances, and damages. A breach of contract is defined in Chinese contract law as the failure of a party to completely perform its

duties under contract. A breach of contract may be actual or anticipatory. The latter refers to the situation in which one party expressly states or indicates by its conduct that it will not perform its obligations under contract. Therefore, the other party may hold it liable for a breach of contract even before the obligation is due. It is generally believed that the relevant provision, as stated in art. 108 CL, is borrowed from the common law system.[1]

2. Attribution Principle of Liability

2 According to art. 107 CL, the non-performing party bears the liability for a breach of contract in cases of any default, irrespective of his actual fault. Thus, it is inferred from this provision that Chinese contract law adopts the principle of no-fault liability or strict liability for a breach of contract.[2] This follows the model of the common law system, the CISG and the PICC.[3] Art. 107 CL is indeed an excellent example of the influence of the CISG and the PICC on the CL. Although the concept of strict liability is obviously different from that of fault-based liability, in practice no fundamental difference may be identified between the two for the following three reasons:[4]

3 Firstly, both attribution principles of liability recognize force majeure as a defence for the breach. Even under the principle of strict liability, force majeure serves as a defence to excuse the non-performing party from the liability for breach. Art. 117 para. 1 CL provides that a party unable to perform a contract, due to force majeure, is exempted from liability in part or in whole according to the impact of the event of force majeure, except where otherwise provided by law. Certainly, where an event of force majeure occurred after the party's delay in performance, it is not exempted from liability. Force majeure is defined by art. 117 para. 2 CL as an objective unforeseeable, unavoidable, and insurmountable circumstance. This definition is the same as the one in the PICC. The term "unforeseeable" means that even an objectivly reasonable person would not take the objective circumstance into consideration when the contract was concluded. The terms "unavoidable" and "insurmountable" mean the circumstance or its consequences may neither be avoided nor overcome.

4 As to the scope of force majeure, according to the mainstream scholarly view, force majeure includes three situations: (1) natural disasters, such as floods, tsunamis, earthquakes, volcanic erruptions, etc. (these events may be described with the term "acts of God" in other legal systems); (2) social abnormal events, such as a war, strike, or riot; (3) acts of the government.[5] For example, the government enacts a new law which bans a contracting party from performing the contractual duty after the contract is concluded.

5 Although the events listed above are usually deemed to fall within the scope of force majeure, the final criterion to judge the existence of force majeure remains to be "unforeseeable, unavoidable, and insurmountable", as stipulated by art. 117

[1] *Wang Liming* (2003), 494, 498.
[2] *Gu Angran*, 44–45; *Xiao Xun/Wei Yaorong/Zheng Shuna*, 341–342; *Wang Liming/Cui Jianyuan*, 580.
[3] *Fansworth*, Legal Remedies for a Breach of Contract. 70 Columbia Law Review 1147 (1970), see *Wang Liming* (2003), 415; Art. 45 CISG; Art. 7.4.1 PICC.
[4] *Wang Hongliang* (2007), 85–95.
[5] *Han Shiyuan* (2004), 429–432.

para. 2 CL. Whether or not the specific event can be considered force majeure is to be examined based on the circumstances of a concrete case.

For example, in the case of *Zhongji Tongyong Imports & Exports Company v The Second Port Company of Tianjin Harbor*, the plaintiff's goods suffered loss, due to a windstorm, when those goods were in the custody of the defendant. In this case, the national oceanic forecast service had warned of the windstorm, but failed to point out that the windstorm would meet with the astronomical tide. Due to a 7-grade wind, the tide level was in the end 160–193 centimeters higher than usual. Waves were up one meter within the pool of the port and two meters outside the pool of the port, both exceeding the levels previous claimed by the national oceanic forecast service. The court ruled that the seawater had engulfed the wharf, ruining the plaintiff's goods, because the natural disaster was aggravated by the combination of the windstorm, the astronomical tide, and high sea waves. The court ruled that this outcome was beyond the port company's ability to foresee. Thus, the port company's defence of force majeure was accepted.[6] 6

Not all earthquakes amount to force majeure.[7] Although earthquakes may be predicted by today's technology, they may reach different scales of magnitude. The ones that are not large enough to cause damage would obviously not be considered force majeure. With regard to an earthquake, a contracting party in the hard-hit areas may be allowed to raise the defence of force majeure, while a party in the light-hit areas may be barred from doing so. Since parties in seismically active areas are able to invest in resources in order to fend off earthquakes, such as deploying earthquake-oriented designs or strengthening the standards of buildings, earthquakes that could have been fended off by such measures do not qualify as force majeure. 7

If a party is unable to perform a contract due to force majeure, it will have the duty to notify the other party in a timely manner for the purpose of mitigation of loss and to provide proof of force majeure within a reasonable amount of time.[8] 8

Secondly, a breach of contract due to a third party is usually barred from operating as a defence in both attribution principles of liability. Even though a party's breach is attributable to the conduct of a third party, that party is nevertheless liable to the other party for breach. Any dispute between the party and a third party is to be resolved between them in accordance with art. 121 CL. For example, the vendor will be unable to deliver the goods to the buyer if his own supplier defaults or if the work to be completed by a sub-contractor does not pass the acceptable tests. In these cases, the vendor or the primary contractor may still be found in breach. In *Qin Zhangqun v Zhang Jinshui*, the defendant leased land from one villagers' group (村民小组) and subleased parts of the land to the plaintiff with the permission of the villagers' group. The plaintiff paid the total rental fee for the whole duration of the lease contract to the defendant while the defendant annually forwarded the rent to the villagers' group. One year after the contract has been concluded, the villagers' group decided to withdraw the land and designated the land as the villagers' housing site. The plaintiff made a request for the refund of the 9

[6] *Zhongji Tongyong Import and Export Company Co., Ltd. v Tianjin Harbour Second Stevedoring Co., Ltd.* (中机通用进出口公司诉天津港第二港埠有限公司港口作业合同纠纷案), judgement of the Tianjin High People's Court dated 13th February, 2000.
[7] *Yang Lixin*, 2–9.
[8] Art. 118 CL.

rent, which was upheld by the court, by arguing that the defendant was also in a breach of contract because he also suffered a loss as the result of the termination of the contract. However, the defendant would be able to recover the loss by filing a suit against the owner of the land.[9]

10 Thirdly, under the principle of fault-based liability, the mere fact of non-performance already suffices to indicate the existence of fault unless the debtor has a legitimate defence so that the plaintiff does not need to prove the element of fault, which is exactly the same in cases of no-fault liability.

3. Election of Remedy in Tort or in Contract

11 A breach of contract may trigger liability in contract and in tort simultaneously. In such a situation, art. 122 CL allows the plaintiff to choose between the two as the legal basis for his actions. In other words, the plaintiff is not allowed to sue concurrently. The plaintiff may modify a choice already made before the first instance trial commences.[10]

II. Main issues

1. Specific Performance

12 The CL distinguishes between monetary specific performance and non-monetary specific performance. With regard to monetary specific performance, there is no exception. The party who fails to pay the price or remuneration is barred from raising any defence.[11] As to non-monetary specific performance, there are three exceptions:[12]

13 (1) If the performance is impossible in law or in fact, the obligee will not be permitted to require specific performance. The performance being impossible in fact means that it is impossible for the obligor or for anyone else to perform, and as a result the claim for performance is not actionable. For example, if the owner of a house sells it to multiple buyers and the house has already been transferred to one buyer, it is impossible for the owner to perform the other contracts in fact.

14 (2) If the subject matter of the obligation is not suitable for enforcement or the cost of performance is excessive, the obligor can refuse to perform. For instance, a publishing contract or a performance contract is not suitable for enforcement because such type of obligations is usually exclusively personal to the obligor. Enforcement of these obligations may invade the personal liberty of the obligor. The obligor may also refuse to perform so far as the performance requires excessive expenditure. The legislator codifies this exception in consideration of balancing both parties' interests.

15 (3) The obligee will be prohibited from requiring specific performance if he fails to do so within a reasonable period of time.

[9] *Qin Zhangqun v Zhang Jinshui, Institute of Applied Legal Studies of the SPC (2005)*, Selected Cases of People's Court, Special on Commercial and Intellectual Property Rights Cases of 2004 (人民法院案例选(2004年商事• 知识产权专辑)), 237–242.
[10] Art. 30 of the Interpretations of the CL (Part I).
[11] Art. 109 CL; *Wang Liming* (2003), 574.
[12] Art. 110 CL.

2. Defect Warranty

According to art. 111 CL, in cases of non-compliance in quality, the aggrieved 16 party may, by reasonable election based on the nature of the subject matter and the degree of loss, require the other party to repair, replace, remake, return the goods, reduce the price, or remuneration.

Art. 111 CL is construed by some scholars to the effect that Chinese contract law 17 has adopted the rule of defect warranty, which is independent from the normal rule regarding the liability for a breach of contract.[13] Other scholars deny this way of interpreting art. 111 CL. In their opinion, there is no room for a separate rule of defect warranty. Liability for the defect of goods has been integrated into the provision of liability for a breach of contract.[14] Scholars in favor of the independence of defect warranty insist that there are three main differences between defect warranty and ordinary liability for a breach of contract. Firstly, under the rule of defect liability, the buyer has the duty to inform the seller of the defect of the goods. If the buyer fails to inform the seller, he will be barred from asserting his rights on the basis of the seller's defect warranty. The ordinary rule on liability for a breach of contract has no comparable requirement. Secondly, defect warranty exists only for a limited period of time. A buyer is not allowed to assert warranty liability beyond a set time limit. Thirdly, types of remedy are different. Usually, ordinary types of liability for a breach include specific performance, payment of damages, or liquidated damages, while defect warranty includes the repair, replacement, remake, or return of the goods, a reduction in price, or remuneration.[15]

The above arguments are not sufficiently convincing. Even the CL has a set time 18 limit for the inspection of goods and requires the buyer to raise an objection within that period of time. No compulsory conclusion can be drawn that defect warranty constitutes a separate rule outside the general rule on liability for a breach. It can be construed that this is a special rule for sales contracts just like the law also sets an inspection period with respect to a cargo carriage contract.[16] "Repair, replace, and remake" are methods of specific performances. Return of the goods is in fact the buyer's right to rescind the contract, which is not an extraordinary relief for the non-breaching party. "A reduction in price or remuneration" can be seen as a combination and variation of traditional remedies, in which the non-breaching party abandons the right to specific performance and accepts the actual performance, but requests to recover the loss between the agreed performance and the actual performance. In whole, the rule of defect warranty may be an independent rule of contract law in other jurisdictions; however, it is unnecessary to interpret Chinese contract law in the same way.

3. Liability for Damages

a) Basic Principles

(1) Full Compensation. The purpose of liability for damages is to recover the 19 innocent party's entire loss. Chinese contract law takes the position that the party

[13] *Cui Jianyuan* (2006), 36–43; *Wang Hongliang* (2005), 72–74.
[14] *Wang Liming* (2001), 21–37; *Han Shiyuan* (2007), 170–190.
[15] *Cui Jianyuan* (2006), 32–43.
[16] Art. 310 CL.

Chapter 14. Acquisition of Ownership

Literature: *Bu Yuanshi* (卜元石), Introduction to Chinese Law (Einführung in das Recht Chinas), Munich 2009. *Cheng Xiao* (程啸), On the Constitutive Conditions of Bona Fide Acquisition of Immovable Property (论不动产善意取得之构成要件), Studies in Law and Business (法商研究) 2010, No. 5, 74–84, cited as *Cheng Xiao* (2010a). *Cheng Xiao* (程啸), On the Differentiation Between Public Reliance on the Land Register and Bona Fide Acquisition of Movable Property (论不动产登记簿公信力与动产善意取得的区分), Peking University Law Journal (中外法学) 2010, No. 4, 524–539, cited as *Cheng Xiao* (2010b). *Dong Xueli* (董学立), On the New Mode of Real Right Transaction Established by the Chinese Real Rights Law (论《物权法》确立的物权变动新模式), Legal Forum (法学论坛) 2011, No. 4, 54–64. *Jia Lianjun* (贾连君), The Impact of the Principle of Separation in Real Right Transactions on Notarization (物权变动区分原则对公证业务的影响), China Notary (中国公证) 2009, No. 8, 42–44. *Li Yongjun* (李永军), Reflections on the First Part of the Real Rights Law (对《物权法》第一编的反思), Contemporary Law Review (当代法学) 2010, No. 2, 7–20. *Liu Baoyu* (刘保玉), The Achievements and Shortcomings of China's Real Rights Law (中国物权法的成就与不足), Legal Forum (法学论坛) 2008, No. 5, 21–28. *Lu Chunya* (鲁春雅), On Moment of Bona Fide in Bona Fide Acquisiton of Real Estate (论不动产善意取得制度中善意判断的时点), Legal Forum (法学论坛) 2011, No. 3, 130–135. *Lurger/Faber*, Principles of European Law – Acquisition and Loss of Ownership of Goods, Munich/Berne 2011. *Stürner*, The New Chinese Real Rights Law from a German Perspective (Das neue chinesische Sachenrecht aus deutscher Sicht), in: *Bu Yuanshi* (卜元石) (ed.), Chinese Civil and Commercial Law from a German Perspective (Chinesisches Zivil- und Wirtschaftsrecht aus deutscher Sicht), Tübingen 2008, 3–17. *Sui Pengsheng* (隋彭生), On the Right of Possession (论占有之本权), Studies in Law and Business (法商研究) 2011, No. 2, 86–95. *Tang Dehua* (唐德华)/*Gao Shengping* (高圣平) (ed.), New Commentary on the General Principles of Civil Law and Additional Provisions (民法通则及配套规定新释新解), 2nd edition, Beijing 2003. *Tu Changfeng* (涂长风), Secured Transactions, in: *Bu Yuanshi* (卜元石) (ed.), Chinese Business Law, Munich 2010, 183–219. *Wang Rongzhen* (王荣珍), On Bona Fide Acquisition of Priority Notice Registration (论预告登记的善意取得), Law Science Magazine (法学杂志) 2011, No. 3, 10–13. *Wang Yi* (王轶), On Chinese Elements in China's Civil Legislations (论中国民事立法中的"中国元素"), Law Science Magazine (法学杂志) 2011, No. 4, 27–32. *Zhang Yuxin* (张喻忻), On the Possession System of Property Law in the Traditional Legal Culture (传统法律文化中的物权法占有制度探析), Hebei Law Science (河北法学) 2010, No. 3, 116–120. *Zheng Hui* (郑辉), Bankruptcy, in: *Bu Yuanshi* (卜元石) (ed.), Chinese Business Law, Munich 2010, 221–268.

Acquisition of ownership occurs in form of original acquisition and derivative acquisition. While original acquisition refers to the acquisition of ownership over an asset which was not owned by anybody at the time of acquisition, derivative acquisition means acquisition from a predecessor in title. It should be noted that the object of acquisition is the ownership right over an asset rather than the asset itself.[1] 1

According to art. 115 RRL, ownership over an accessory is transferred along with ownership over the principal thing, whereas (in cases of derivative acquisition) the parties may stipulate otherwise. The RRL does not define the term "accessory". Under German law, accessories are movable things that, without being parts of the principal thing, are intended to serve the economic purpose of the main thing and 2

[1] Cf. *Dong Xueli*, 54, note 5. A contrary approach (transfer of the asset itself) is taken by French law, under which the transfer of ownership takes place by extinction of the transferor's right and creation of a new right in favour of the acquirer (*Lurger/Faber*, 490).

are in a spatial relationship to it that corresponds to this intention.[2] There is good cause to believe that under Chinese law a similar concept applies.

I. Conveyance of Title

3 Conveyance of title, as addressed in this section, exclusively refers to derivative acquisition of ownership by virtue of contracts. Derivative acquisition of ownership by other means (such as acquisition by way of succession or as a result of continuous possession), as well as original acquisition (e.g. of fruits) will be dealt with in section III of this Chapter (*infra* at 61 *et seqq.*).

1. Transfer by a Single Legal Act

4 The parties to a transaction can accomplish conveyance of title by a single legal act. Typically, this will be a sales and purchase contract, which, pursuant to art. 130 CL, is a contract whereby the seller transfers his ownership over the targeted matter to the buyer and the buyer pays the price therefor.[3] When the RRL sets out additional requirements such as delivery or registration (for details see *infra* at 8 *et seqq.*), such an additional act is of a factual nature (i.e. it is a "real act" as opposed to a legal act).[4]

5 The German approach has not found its way into the RRL although Chinese scholars had discussed it for many years before the enactment of the RRL.[5] Under the German model, a sales and purchase contract only creates an obligation to a title transfer and will on no account bring about a transfer of title by itself, whereas the transfer of title can only be effected by a second legal act, the so-called "real agreement" (物权行为)[6]. The two legal acts exist separately from one another (principle of separation), and the legal validity of the real agreement is independent of the validity of the underlying sale and purchase contract (principle of abstraction). If such underlying contract is void or avoided, ownership will not be re-vested automatically, but the transferee has a duty to retransfer his ownership right over the property under the rules of unjust enrichment.[7]

[2] Art. 97 para. 1 of the German Civil Code (*Bürgerliches Gesetzbuch*).

[3] This shows that under Chinese law there is one single contract containing an agreement on mutual obligations as well as an agreement on the actual transfer of both the targeted matter and the purchase price, cf. *Stürner*, 7.

[4] *Stürner*, 8; *Bu Yuanshi*, 134 at 23. By contrast, *Dong Xueli*, 54 (left column), seems to be of the opinion that there must be a real agreement, or declaration of a "real right will" (物权意思) because art. 15 RRL sets out the "principle of separation" (区分原则), which *Dong* obviously associates with the "real agreement" under German law (for details on the German approach see the next paragraph). However, there is in fact no such close link between the Chinese principle of separation and the German approach (for the differences between Chinese and German law in this respect, see *infra* at 5–7). *Jia Lianjun*, 42, is under a similar misapprehension.

[5] *Bu Yuanshi*, 134 at 23.

[6] Cf. *Dong Xueli*, 55 (left column).

[7] For a detailed description of the German model with respect to movable property, see *Lurger/Faber*, 409, 482–484. The distinctive feature of the German model is typically referred to as the "principle of separation and abstraction of the real agreement", in Chinese: 物权行为与债权行为区分与无因原则 (cf. *Li Yongjun*, 18, note 1).

Although Chinese law does not follow the German approach, there is a certain degree of separation of the conclusion of a sales and purchase contract on the one hand from the actual transfer of ownership on the other hand. For immovable property, art. 15 RRL states that a contract with respect to the creation, alteration, transfer, or extinction of a real right takes effect immediately upon execution, irrespective of whether the property right has already been registered. For sales and purchase contracts, i.e. the transfer of ownership of immovable as well as movable property, art. 135 CL stipulates that the seller is obliged to deliver and transfer ownership over the targeted matter. These provisions show that a contractual obligation to transfer ownership can be validly created without the need for immediate transfer. It is not even necessary that the seller is the owner of the targeted matter at the time of the conclusion of the sales and purchase contract.[8] 6

This separation of the contractual obligation from the completion of the transfer itself is merely a chronological one. While the RRL permits a delay in time between "signing" and "closing", these two elements are closely linked to each other legally. If there is no valid contract, delivery alone will not make for a transfer of title. Some Chinese scholars refer to art. 15 RRL as containing the "principle of separation"[9] or the "principle of separation of the validity of an obligatory contract and the transfer of a title"[10]. This is correct as far as the chronological separation is concerned. However, one must bear in mind that the same term has a different meaning under German law (*supra*), so the use of this term in the context of Chinese law can be somewhat misleading.[11] 7

2. General Remarks on Publicity Requirements

Following the principle of publicity of real rights (*supra* Chapter 13 at 38), under Chinese law the transfer of ownership (as well as the establishment and transfer of any other real right) requires an act of publicity. Usually the transfer of ownership of movable property only takes effect upon delivery, and the transfer of ownership of immovable property does not become valid before registration.[12] This shows that Chinese law has not adopted the model of transfer by mere consent[13] as its basic model. Exceptions will be discussed below (at 10 *et seqq.*). 8

[8] Art. 3 para. 1 of the Interpretation of the SPC on Issues Concerning the Application of Law in the Trials of Cases about Disputes over Sales and Purchase Contracts. This provision shows that arts. 132, 51 CL do not refer to the validity of the sale and purchase contract ifself but rather to the validity of the transfer of title effected under such contract.

[9] *Dong Xueli*, 54 (left column); *Jia Lianjun*, 42.

[10] *Liu Baoyu*, 22 left column.

[11] Cf. *supra* note 4 for examples. It certainly contributes to the risk of confusion that the German principle of separation, just as the principle of separation under Chinese law, allows for a chronological separation of the obligatory contract from the actual transfer of title. However, this is not the key point under German law. The meaning of the principle of separation under German law is rather that the transfer in title requires a separate legal act (not just a "real act") the legal validity of which, according to the principle of abstraction, has to be assessed irrespective of the legal validity of the underlying obligatory contract.

[12] Arts. 6, 9 para. 1, and 23 RRL. This model is referred to as 债权形式主义 in Chinese (cf. *Wang Yi*, 29 (right column)).

[13] In Chinese this model is referred to as 意思主义 (cf. *Wang Yi*, 30 (right column)). French law is a textbook example of transfer by mere consent. Under French law, the ownership of movable property passes on from the transferor to the transferee in the moment in which the contract, e.g. a

9 As mentioned above (*supra* at 4), the act of publicity is of a factual nature. The act of publicity itself never causes the transfer of ownership; the validity of the transfer always depends on the existence of a valid contract, e.g. a sales and purchase contract.[14]

3. Publicity Requirements Regarding Movable Property

a) Delivery

10 Pursuant to art. 23 RRL, conveyance of title in movable property requires the delivery of the movable property, unless the law provides otherwise. Such other provisions are contained in arts. 25–27 RRL. When a transferee has already lawfully possessed the movable, e.g. as a lessee, prior to the conclusion of the contract that is targeted at the transfer of ownership, ownership validly passes on to the transferee at the time when such a contract becomes effective;[15] no delivery is required (*brevi manu traditio* 简易交付[16]).

11 Under arts. 26 and 27 RRL, actual delivery (实际交付)[17] (or physical delivery) can be substituted by notional delivery (观念交付)[18]. This means that direct (or actual) possession of the movable property remains with the same person, while a change only takes place on the level of indirect (or constructive) possession. As a result, the principle of publicity is attenuated in very much the same way as in German law.[19]

12 When a third party possesses the property, the transferor may discharge his obligation to deliver the property by transferring to the transferee the right to request the third party to return the property.[20] The transfer of ownership is complete as soon as the transfer of the right to request a return of the property becomes effective.[21] It is noteworthy that such a right to request a return must be the result of lawful possession by the third party, so a claim arising from unjust enrichment will not be sufficient.

13 When the transferor possesses the movable property, the transferee may agree that the property remains in possession of the transferor after the transfer of

sales and purchase contract, is validly concluded, and from such point in time a transferor who still holds the asset does so on account of the transferee (*Lurger/Faber*, 488).

[14] *Stürner*, 7.

[15] Art. 25 RRL. The beginning of this provision ("*The establishment and transfer of real rights in movable property (…)*") addresses both the transfer of ownership and the establishment of other real rights (such as a pledge). However, its last part ("*(…) the real right shall become effective as of (…)*") strictly speaking, only fits the establishment of real rights, cf. *Liu Baoyu*, 26 (right column).

[16] Cf. *Sui Pengsheng*, 91.

[17] Cf. *Sui Pengsheng*, 91.

[18] Cf. *Liu Baoyu*, 26 (left column); *Sui Pengsheng*, 91.

[19] *Stürner*, 11.

[20] Art. 26 RRL. This kind of substitution of actual delivery is termed 指示交付 in Chinese, cf. *Liu Baoyu*, 26 (left column); *Sui Pengsheng*, 91.

[21] Where the right to request return of the property is transferred by way of transfer of a delivery order (提货单), the transfer does not become effective before the third party possessor has been notified of the transfer. See *Concordia Agricultural Products (Shanghai) Ltd. v Guangdong Fuhong Oil Products Ltd and Zhanhong Branch of China Construction Bank Co., Ltd.* as third party in respect of a dispute over the confirmation of ownership (肯考帝亚农产品贸易(上海)有限公司与广东富虹油品有限公司第三人中国建设银行股份有限公司湛江市分行所有权确认纠纷案), judgement of the SPC dated 25th February, 2011. Unlike a bill of lading (提单, see art. 71 of the Maritime Code (*infra* note 28)), a delivery order is not a document of title.

ownership of the property (*constitutum possessorium* 占有改定[22]).[23] The parties have to make an explicit agreement to this effect, e.g. a lease agreement between the transferee as lessor and the transferor as lessee; the agreement on the transfer of ownership itself, e.g. a sale and purchase contract, is not sufficient.[24] Ownership passes on to the transferee upon conclusion of both agreements.

b) Registration

Registration is not only available for real rights over immovable property (see *infra* at 18 *et seqq.* for registration of immovable property) but also for certain types of movable assets. Pursuant to art. 24 RRL, the establishment, modification, transfer and lapse of real rights in respect of vessels, aircraft vehicles, and motor vehicles does not affect a *bona fide* third party before such establishment, modification, transfer, or lapse of a real right has been registered.[25] 14

It is clear that after the delivery of a vessel, aircraft vehicle, or motor vehicle, the transfer of title needs to be registered in order to be effective as against a *bona fide* third party.[26] However, the question arises whether delivery is still required to complete the transfer of ownership when the transfer has already been registered. Given that the purpose of any act of publicity is to make the transfer visible to the public one could argue that registration serves this purpose as well as, or even better than, delivery can do;[27] therefore, no delivery should be required in this case. In addition, the transfer of ownership of immovable property solely requires registration as an act of publicity. Therefore, one could take the view that art. 24 RRL is a "law that provides otherwise" within the meaning of art. 23 RRL. 15

On the other hand, art. 6 RRL clearly states that the establishment and transfer of real rights over movable property require delivery of the property. Art. 16 RRL, according to which registration is the basis for the attribution of real rights, only applies for immovable property. In addition, it would be odd if the generic reference to the possibility of exceptions in art. 23 RRL were directly followed by a provision containing such an exception without art. 23 pointing to it in a more specific way. More importantly, arts. 25 and 27 RRL give an example of how the RRL is worded when transfer can take full effect in the absence of actual delivery ("the real right shall become effective"). By contrast, art. 24 RRL only refers to opposability as an option against a *bona fide* third party. 16

[22] Cf. *Liu Baoyu*, 26 (left column); *Sui Pengsheng*, 91.

[23] Art. 27 RRL. Similar to art. 25, the wording of art. 27 is imperfect in that the Law addresses the transfer of a real right but states that such real right "shall become effective", cf. *Liu Baoyu*, 26 (right column).

[24] *Qingdao Yuanhongxiang Textile Co., Ltd. v Gangrun (Liaocheng) Printing and Dyeing Co., Ltd.* in respect of a dispute over the confirmation of a recall right (青岛源宏祥纺织有限公司诉港润聊城印染有限公司取回权确认纠纷案), judgement of the High People's Court of Shandong Province dated 5th May, 2011.

[25] There are separate registers for the different types of assets. For example, the registration of real rights with respect to vessels is subject to the Regulations on Vessel Registration (船舶登记条例) promulgated on 2nd June, 1994 and effective from 1st January, 1995. Registers are run by the local offices of the Maritime Safety Administration (海事局); a central register does not exist.

[26] For details regarding the concept of opposability against a *bona fide* third party, see *infra* at 20.

[27] This idea seems to be at the basis of art. 106 para. 1 (3) RRL according to which good faith acquisition does not require delivery where a real right that requires registration has been duly registered.

57 Strictly speaking, China has not established a sound legal system of estates management.[21] The SL contains some provisions dealing with the management of estates, which may be applied to both foreign-related and domestic successions. In brief, art. 24 SL provides that anyone who possesses the estate of the decedent shall carefully maintain it and that no one is to misappropriate or contend for it. Further, art. 29 SL provides that the allocation of the estates should be conductive to production and livelihood (of the heirs). Art. 33 SL provides that the applicable tax or debts of the decedent should be satisfied prior to the allocation of the estates.

58 According to art. 34 LAL, on the law applicable to the management of estates in foreign-related succession, the governing law should be that of the place where such estates are located. Here, Chinese law does not distinguish real estates and movable estates. Besides, it should be noted that some Sino-foreign consular treaties also contain provisions on the management of estates, such as the Consular Treaty between the People's Republic of China and the Republic of Mongolia.[22] In such cases, according to art. 142 GPCL (*supra* at Chapter 18 at 19), treaty provisions prevail over the SL.

4. Succession of Heirless Estates

59 In reality, it is possible that no heirs can be identified to inherit the decedent's estates. A typical reason could be that the decedent has no statutory heirs and makes no testament to dispose of his estates, or that all heirs lose their rights to succession. It is thus necessary to first discuss how to identify whether certain estates should be deemed as heirless estates and follow up with who should inherit such heirless estates.

60 Concerning the first issue, it is widely accepted that the applicable law of succession should be applied to decide whether certain estates are to be deemed as heirless estates. In practice, such a law could refer to either the national law of the decedent (the law of his nationality or domicile) or the *lex loci rei sitae*. On this issue, Chinese law does not contain an express provision. Therefore, the general rule on conflict of laws governing foreign-related succession, namely art. 149 GPCL, applies. Under this provision, when the decedent dies, the law of his domicile should govern whether his movable estates are heirless estates, while the *lex loci rei sitae* should govern whether his real estates are heirless estates.

61 Concerning the second issue, art. 35 LAL provides that the applicable law should be that of the place where the decedent's estates are located when he dies. It should be noted that this provision does not distinguish real estates and movable estates; thus, it should be applied to both types of estates. In cases where this rule refers to the substantive law of China, the SL comes into play. With regard to heirless estates, art. 32 SL provides that heirless estates are generally inherited by the state of China. Such a provision is different from many state laws and reflects China's long-rooted orientation towards the state's interests in lawmaking. Furthermore, as mentioned earlier, some Sino-foreign consular treaties also deal with succession issues. Therefore, according to art. 142 GPCL, if these relevant treaties contain different rules, such rules shall prevail (*supra* at Chapter 18 at 19).

[21] *Wan E'xiang*, 255.
[22] See *Zhang Bozhong*, 438–439.

Chapter 21. Property Rights, Obligations and Intellectual Property Rights

Literature: *Chi Manjiao* (池漫郊), "The Iceberg Beneath the Water": The Hidden Discrimination against the *Lex Mercatoria* in Chinese Arbitration, Journal Private International Law 2011, Vol. 7 (2), 351–352. *Huang Jin* et al (黄进), Chinese Judicial Practice in Private International Law: 2006, Chinese Journal of International Law 2009, Vol. 8 (3), 715–740. *Huang Jin* (黄进), Private International Law (国际私法)(2 ed.), Beijing 2005. *Huo Zhengxin* (霍政欣), On the Applicable Law to Compensation in Foreign-Related Tort (涉外侵权之债的法律适用), Studies in Law and Business (法商研究) 2011, No. 6, 11–16. *Liang Huixing* (梁慧星), Comments on China's Civil Legislations: Civil Code, Real Rights Law and Tort Law (中国民事立法评说民法典物权法侵权责任法), Beijing 2010. *Ministry of Labor and Social Welfare* (劳动和社会保障部), Publicity Guideline of the Labor Contract Law of The People's Republic of China (《中华人民共和国劳动合同法》宣传提纲) (29th June, 2007). *Vogenauer/Kleinheisterkamp* (eds.), Commentary on the UNIDROIT Principles of International Commercial Contracts, Oxford 2009. *Wan E'xiang* (ed.) (万鄂湘编著), Understanding and Applying the Law of the Application of Law for Foreign-related Civil Relations (涉外民事关系法律适用法条文理解与适用), Beijing 2011. *Xiao Yongping* (肖永平), Principles of Private International Law (国际私法原理), 2nd ed., Beijing 2007. *Xiao Yongping* (肖永平)/*Long Weidi* (龙威狄), Contractual Party Autonomy in Chinese Private International Law, Yearbook of Private International Law 2009, No. 11, 194–209. *Yang Lixin* (杨立新), Guidelines on Application of Law Concerning Chinese Media Tort Cases (中国媒体侵权责任案件法律适用指引), Journal of Henan University of Economics and Law (河南财经政法大学学报) 2012, No. 1, 15–31. *Yu Ying* (余莹), Comment on Art. 42 of the Law of the Application of Law for Foreign-Related Civil Relations (评涉外民事关系法律适用法第42条), Law Review (法学评论) 2011, No. 2, 65–66.

I. Introduction

This Chapter deals with several types of civil relations that probably carry the most practical significance in people's daily life. It touches upon various fields of law, such as property law, contract law, intellectual property law, and tort law. As mentioned in previous chapters, in China, property rights (real rights) and obligations are governed principally by the Real Rights Law (RRL)[1], the Contract Law, and the Law on Tort Liability[2]. The main sources of intellectual property (IP) rights include the Patent Law[3], the Copyright Law[4], and the Trademark Law[5]. Most of these laws are either newly adopted or recently amended in order to keep pace with the country's rapid economic development in recent decades. In addition to these laws, there are also a large number of relevant SPC judicial interpretations and administrative regulations. China is also a contracting state to various international conventions in the above areas, such as the 1980 United Nations Convention on Contracts for the International Sale of Goods (CISG). 1

[1] 物权法, promulgated on 16th March, 2007 and effective from 1st October, 2007.
[2] 侵权责任法, promulgated on 26th December, 2009 and effective from 1st July, 2010.
[3] 专利法, promulgated on 12th March, 1984 and effective from 1st April, 1985; last revision effective from 1st October, 2009.
[4] 著作权法, promulgated on 9th July, 1990 and effective from 1st June, 1991; last revision effective from 1st April, 2010.
[5] 商标法, promulgated on 23rd August, 1982 and effective from 1st March, 1983; last revision effective from 1st December, 2001.

2 It should be noted that, although the laws of contract, tort, property rights, and IP rights are quite numerous and fragmented, the importance of the rules on conflict of laws in these fields has been somehow diluted in recent years. One reason is the enhanced unification of laws in these areas at the international level, particularly in the field of contract law. Another reason is that nowadays the national legal systems tend to recognize the broadened party autonomy principle, which governs a wider scope of issues than merely contractual disputes.

II. Property Rights (Real Rights)

3 In modern society, real rights carry fundamental significance. Almost all state laws contain concrete rules governing various types of real rights, and such rights are deemed as an important aspect of citizen rights. Under Chinese Law, though real rights have a broad coverage, they are divided by art. 2 RRL into movables, immovables, and certain rights as prescribed by law. The term "real rights" means the exclusive right of direct control over a property enjoyed by the holder in accordance with law, including ownership, usufractuary rights, and real rights for security.

4 That the law should protect citizens' real rights is a well-established principle. This principle is partly recognized and codified by the RRL. As discussed in Chapter 13, leading Chinese civil law experts opine that art. 66 RRL actually denies the equal protection of private property and state property because it obviously prioritizes the protection of state property.[6]

5 It is interesting to note that the RRL does not contain rules on conflict of laws. According to its art. 8, in cases where other laws contain special provisions regarding real rights, such laws shall apply. Therefore, the LAL will be applied to determine the applicable law of foreign-related real rights issues, according to which different types of real rights are governed by different rules on conflict of laws. Although real rights issues are among the most important and complicated legal issues, the rules on applicable laws, with regard to real rights issues, are not always so complicated thanks to various well-established principles.

1. Immovables

6 Generally, it is necessary and a general practice to distinguish immovables from movables in law. Such a distinction is not only relevant to the jurisdictional issue of real rights disputes, but is also connected to the disposal of such rights. It has been well established that the law applicable to immovables is the law of the place where such estates are located (*lex rei sitae*).

7 This rule was formerly recognized by art. 144 GPCL and later codified by art. 36 LAL. Art. 36 LAL does not distinguish the different aspects of immovables; thus, it should be understood that the *lex rei sitae* governs all aspects of immovables, unless otherwise provided, including the ownership, sale, lease, use, establishment, modification, assignment, extinction, and legal protection of such immovables. Given

[6] See generally *Liang Huixing*, 114–128.

such a broad coverage of this provision, it is even suggested that this LAL provision does not contain any exceptions.[7]

2. Movables

An important implication of distinguishing immovables from movables lies in 8
that they are subject to different applicable laws. Compared with immovables, the law applicable to movables has undergone substantial changes in the past centuries. Formerly, movables were governed by the *lex personalis* of their owners. Since the 19th century, this rule gradually became obsolete due to the frequent cross-border movements of persons and the development of international commercial transactions. Following such a trend, some states began to apply the *lex rei sitae* rule to movables. More recently, with the rapid economic development, various states began to adopt the party autonomy principle in order to determine the law applicable to movables.

In China, the GPCL and its relevant judicial interpretations do not contain any 9
express rules regarding the law applicable to the movables. This vacuum is filled by the LAL, following recent international legislative trends. According to art. 37 LAL, parties may reach an agreement regarding the law applicable to the movables; absent such agreement, the *lex rei sitae* (where the legal relations occurred) is applied. This provision is applied to a broad range of aspects of foreign-related civil relations relating to movables, including the ownership, use, type, contents, establishment, modification, assignment, termination as well as legal protection of such movables.

Under Chinese law, there are a few exceptions to art. 37 LAL. For instance, 10
movables in transit are a typical exception. Generally, it is almost practically impossible to determine a certain location of movables in transit as such location is constantly changing. Therefore, art. 38 LAL provides that the law applicable to such estates is subject to the parties' agreement; and absent such agreement, the applicable law is the law of the destination of the transportation.

3. Securities

There is no unified definition of the term securities as different states have 11
different legal systems and commercial practices. However, it is generally agreed that securities as such should possess certain elements: they should be negotiable, carry certain value, and represent certain rights independent from its holder.

In practice, there might be many ways to classify securities. For instance, 12
according to art. 2 Securities Law[8], securities include corporate bonds, stocks, or others types of securities as approved by the State Council. Art. 71 Maritime Law deals with commonly seen types of securities, for instance, bill of lading. Similarly, art. 2 Negotiable Instruments Law provides that negotiable instruments may refer to money orders, checks, and/or promissory notes. Besides, as previously mentioned, Chapter 5 Negotiable Instruments Law also provides for several rules on conflict of laws for foreign-related securities.

[7] *Wan E'xiang*, 270.

[8] 证券法, promulgated on 29th December, 1998 and effective from 1st July, 1999; last revision effective from 1st January, 2006.

13 In contrast, the LAL fails to expressly provide what types of securities it governs. Thus, it is at the discretion of the court to decide whether a certain type of securities falls under the scope of application of the LAL. This is to say, the LAL is supplementary to the above securities laws. In other words, the LAL shall be applied if the previous laws are not applicable or do not contain rules on conflict of laws. According to art. 39 LAL, securities are governed either by the law of the place where the rights in respect of securities are to be exercised, or by any other law to which the securities are most closely connected. Since the LAL is unclear on the connecting factors which are needed to decide on the law most closely connected, it is subject to the discretion of the courts.

4. Pledge of Rights

14 According to art. 223 RRL, at the outset, there are various types of rights on which a pledge can be established, including (1) money orders, checks, and promissory checks; (2) bonds and deposit receipts; (3) warehouse receipts and bills of lading; (4) transferable fund units and stock rights; (5) assignable property rights of trademark rights, patent rights, copyrights, etc; (6) receivables; and (7) other property rights that can be pledged as prescribed by law.

15 With regard to the law applicable to a pledge of rights, the RRL is silent. Again, the LAL fills the gap. According to art. 40 LAL, a pledge of rights is governed by the law of the place where the pledge is established. As the LAL is silent as to what place is deemed as the place the pledge is established, one must resort to the respective substantive laws. On this issue, arts. 224–228 RRL provide guidance. According to these provisions, the place of establishment of the pledge is generally the registration place of such pledge. Such rules on conflict of laws echo the compulsory requirement of registering a pledge of rights as prescribed in these provisions.

III. Contract

16 Given the practical importance of contracts, contract law is deemed a key instrument in almost all state legal systems. In nature, a contract is an agreement between two or more parties that dispose of their civil rights and thereby create certain obligations to one another. Art. 2 Contract Law (CL) clearly recognizes that a contract is an agreement created to establish, modify or terminate the civil rights or obligations between equal natural persons, legal persons, and organizations. Contracts are divided into a number of major types, such as sales contracts, lease contracts, and transportation contracts. Contract law regime is a complicated one, touching upon various aspects of legal issues, such as formation, legal effects, modification, termination, performance, breach, and remedy of a contract. The applicable law issues relating to foreign-related contracts are mainly embodied in a special chapter of the GPCL, art. 126 CL, the LAL, and various SPC judicial interpretations.

1. The Party Autonomy Principle

17 Since the mid-20th century, party autonomy has been widely recognized as a fundamental principle of private international law. Under Chinese law, subject to a few exceptions, this principle is applied to settle applicable law issues in various types of legal disputes, including both international disputes and inter-regional disputes.[9]

18 The applicability of the party autonomy principle to foreign-related contractual disputes has long been confirmed in Chinese law. It was first provided by art. 145 GPCL and later in art. 126 CL. The relevant parts of both provisions provide that parties to a foreign-related contract may choose which law to apply to their contractual disputes, except when the law has other provisions. Absent such a choice, the law that bears the closest connection with the contract is applicable.

19 The same position was recently codified in art. 41 LAL. According to this provision, parties may agree to choose the law applicable to their contract. Absent such a choice, the law of the place where the party, who is required to effect the characteristic performance of the contract, has its habitual residence or any other law to which the contract is most closely connected is applicable. In practice, parties are only allowed to choose substantive law instead of procedural law. Besides, parties may choose a law to govern their contract that bears no connection with the contract, unless such a choice violates the mandatory rules of Chinese law.[10]

20 Despite China's explicit recognition of the party autonomy principle, it is still necessary to further discuss several operational aspects of this principle, such as the time for parties to conclude their agreement on the choice of law, the formal requirements of the parties' choice as well as the restrictions and exceptions of this principle.

21 First, the LAL is silent as to the time frame for parties to make an agreement on the choice of law. In general, it is accepted that parties may choose the law applicable to their contract either before or after the conclusion of the contract or before a dispute arises. Some state laws also allow parties to modify their original choice of law. In this regard, the Rules of the SPC on the Relevant Issues Concerning the Application of Law in Hearings on Foreign-Related Contractual Disputes in Civil and Commercial Matters (SPC Judicial Interpretation No. 2007–14)[11] contains clear guidance. According to art. 4 of the SPC Judicial Interpretation No. 2007–14, if the parties conclude an agreement on the choice of law before the end of the first instance court hearing, the agreement will be allowed. In *Guangzhou Xianyuan Real Estate Co. Ltd v Guangdong Zhongdazhongxin Investment Planning Co. Ltd, Guangzhou Yuanxing Real Estate Co. Ltd, and China Investment Group International Finance Ltd*[12] concerning a contract for the transfer of company shares, the SPC, based on this provision, ruled that Chinese contract law should be applied because all of the parties had agreed to it during the court hearing. There are other cases where the parties make their agreement on the choice of law during the court hearings, some even during the hearing of the second instance.[13] Though scholars

[9] *Xiao Yongping/Long Weidi*, 195.
[10] *Wan E'xiang*, 297.
[11] 最高人民法院关于审理涉外民事或商事合同纠纷案件法律适用若干问题的规定, promulgated on 11th June, 2007 and effective from 8th August, 2007.
[12] 广州市仙源房地产股份有限公司与广东中大中鑫投资策划有限公司广州远兴房产有限公司中国投资集团国际理财有限公司股权转让纠纷案, judgement of the SPC dated 30th December, 2009.
[13] See *Xiao Yongping/Long Weidi*, 199–200.