‘Rule of Law’ in China: The Confrontation of Formal Law with Cultural Norms

Larry A. DiMatteo*

I. Introduction
   A. China as a Civil Law Country
   B. Modern Chinese Contract Law

II. Contract Law of the People’s Republic of China (CCL)
   A. Sources and Coverage
   B. General Principles of the CCL

III. General Rules of the Civil Law of the People’s Republic of China
   A. General Structure
   B. General Principles
      1. Normative Tension
      2. Rule of Persons and Rule of Law
   C. Specific Provisions
      1. Capacity
      2. Expression of Intention
   D. Comparing the General Principles of CCL with the General Rules

IV. Modern Contract Law with “Chinese Characteristics”
   A. Confucian Values and Norms
   B. Communism and Socialistic Principles
   C. Contract Law with ‘Chinese Characteristics’
   D. Purpose of General Principles
   E. Good Faith as Meta-Principle?
      1. Good Faith as Culturally Dependent Principle
      2. Good Faith in the Chinese Cultural and Legal Context
      3. Good Faith in Chinese Legal Practice

V. Paradigm of Hard-Soft Law
   A. Chinese Contract Law as a Hard and Soft Law System
   B. Towards a General Civil Code

Conclusion

Word Count: 27,154

*Huber Hurst Professor of Contract Law, University of Florida, JD Cornell University, LLM Harvard University, PhD Monash University. I am grateful for the invaluable help of Justin W. Evans in providing numerous sources and citations to support many of the article’s assertions.
ABSTRACT

This Article will be the first to fully examine the adoption of the first part of China’s long-term quest to enact a grand civil code. It is primarily an examination of the interaction between law and culture—this interaction is most visible when law is transplanted from one legal tradition (Western) into a country of a different legal tradition (Eastern). The General Rules of the Civil Law of the People’s Republic of China took effect on October 1, 2017. This enactment of general principles is the first step in what is expected to take up to five years to create a European-style civil code. There are multiple, interlocking themes to this article. First it focuses on the general principles of contract law, comparing the current Chinese Contract Law of 1999 with the General Rules of 2017. This analysis of general principles is not merely confined to contract law, but reflects the values and goals of Chinese society.

A second theme explores the effectiveness and inherent problems of legal transplantation from one legal system to another. China is a unique example given the great mass of laws adopted in its transition to a socialist-market economy. The review of general principles and analysis of the effectiveness of China’s transplantation of Western-style laws provides the basis for examination of the status of the “rule of law” in present day China. The rule of law is generally associated with public law, such as criminal and constitutional law, and concepts such as due process. This article demonstrates the importance of rule of law in the more mundane area of private law, in this case, the law of contracts. The examination of the rule of law in Chinese private law also has different dimensions. First, the article examines the pivotal role that Chinese cultural norms—Confucian and socialist principles—has had in diminishing the rule of law in China. Second, the continued influence of government agencies and the low quality of the Chinese judiciary has also held back the implementation of a rule of law system in the private law realm. The article concludes with the use of a hard-soft law paradigm to best understand the interaction of formal law and cultural norms in modern China.
‘Rule of Law’ in China: The Confrontation of Formal Law with Cultural Norms

I. INTRODUCTION

[The political and civil laws of each nation must be proper for the people for whom they are made, so much so that it is a very great accident if those of one nation can fit another.... [The laws] must agree ... with the customs [of the people].
- Montesquieu

This article examines two divergences in the evolution of modern, market-oriented law in the People’s Republic of China (China). The first divergence pertains to the difference between the intended meanings of transplanted law in the country of origin to the borrowing country. The second divergence relates to the rule of law—the difference between the objectivity of law as enacted and partiality of law as applied. The first divergence relates to China’s massive transplanting Western-style law into an Eastern cultural and legal tradition. This transplantation was broad in scale and implemented with lightening speed given the broad sweep of legal evolution. Not surprisingly, the divergence between implementation and understanding was great, leading to wholesale confusion and contradiction in the laws’ interpretation. This divergence did not come as a surprise given China’s Confucianist-Communist-Socialistic history. Related to this divergence of law on the books and law in interpretation, was another divergence. Assuming away the first divergence (assuming uniformity of interpretation) divergences has appeared between the meaning of the borrowed in the country of origin and the meaning appropriated through the lens of Chinese cultural and socialistic norms. This divergence has been problematic

in the application of individual legal rules and concepts as part of a body of holistic law. However, such cultural tainted meanings should not be considered as a failure of transplantation, but as the necessary intermixing of formal law with cultural, social, and legal norms of the accepted country.

At one level, the mass transplantation of Western-style law can be measured as a major success given the rapid expansion of China’s market-export economy. However, this shrouds the weakness of the Chinese court system and its inability to comply with the rule of law. This has been a result of impartiality and bias in the application of private law and the general lack of objective legal reasoning due to the low quality of the Chinese judiciary. The movement of the law of the person based on the omnipotence of the Communist party and the hierarchical nature of roles in Confucianism to the rule of law still needs further development. Regarding the low quality of the judiciary in Western legal reasoning, the Chinese government, mostly through the work of the Supreme People’s Court (SPC), steps have been implemented to improve the qualifications of judges and to obtain a more uniform application of law through the Chinese court system.

The theme of this article is that although the rule of law is generally applied to areas of law, such as constitutional, criminal, and human rights, and the application of concepts such as fairness, justice, and due process, the rule of law is just as vital to the more “mundane” area of private law. China and Chinese contract law provide an excellent case study of country trying to adopt the rule of law in one area (private law), while limiting its application in the public sphere controlled by a Communist dictatorship. This schizophrenic splitting of the rule of law is unique and perplexing.
A. China as a Civil Law Country

China’s gradualism in introducing formal (Western) law and recognizing contract and private property rights was best equipped to handle its dramatic shift from a socialist-relational perspective of law’s role in society to a private rights and formal law approach to managing legal relationships.\(^3\) After the destruction unleashed by the Cultural Revolution it is understandable that the legal reforms begun by the Deng Xiaoping’s government in the late 1970’s and those that followed have been “so cautious and gradual.”\(^4\)

Just as the Chinese economy has accelerated in unprecedented fashion over the last thirty-five years, the Chinese government has implemented a massive expansion of Chinese law, most of which related to the creation of a market economy. Almost the entire Chinese legal system has been created over this period of time, whereas for western countries it took centuries.\(^5\) A major part of this legal revolution is yet to be created—a grand or general Chinese Civil Code. This article will examine the recently promulgated first part of the Code project.

On March 15 2015, The Twelfth National People's Congress of the People's Republic of China promulgated the first part of what is intended to become China’s first comprehensive

---


4 *Id* at 396.

5 It is important to understand the difference between substance and praxis as it relates to Chinese law. The massive amount of legislative activity was set in the context of a Chinese judicial system ill equipped to understand and apply Western-style law. For example it was not until 2002 that judges were required to pass a national bar exam. See Stanley Lubman, *Looking for Law in China*, 20 COLUM. J. ASIAN L. 1, 29 (2006). Thus, a divergence remains between the substantive law and its functional use, as well as uncertainty in its application. The independence and quality of the Chinese courts still remains an issue and until that issue is solved the legal system will remain less than fully functional.
General Civil Code,\(^6\) entitled *General Rules of the Civil Law of the People’s Republic of China* (*General Rules*).\(^7\) The law goes into effect on October 1, 2017. The idea of a comprehensive Chinese Civil Code is not a new one, as tentative steps towards its creation can be seen in various eras of Modern China including the late Qing Dynasty’s (1902–1911) production of a Draft Civil Code, the enactment of the first Chinese Civil Code in 1930 by the Kuomintang (Republican Government), and again in the early 1950s a civil code contemplated by the new Chinese communist government.\(^8\) The Kuomintang Civil Code was much influenced by Chinese natural law theory, which focused on social harmony—the “we” over the “I” that favored conciliation and compromise in social (contractual) relationships. Thus, the Kuomintang Code is “characterised by a concern for social order rather than unbridled individual interests.”\(^9\) This same communitarian theme persists in current Chinese contract law and in the *General Rules*, which will be reviewed in this article.

The selection of a civil law system, rather than a common law system, by Chinese leaders was due to the fact that it was a better fit given the civil law’s reliance on general principles or general clauses, which can be found in the code-like precepts of Confucius, “while the individualistic common law approach did not fit into a Chinese communitarian society.”\(^10\) The Chinese government resurrected the idea of a civil code in the early 1980s, but this effort was ultimately rejected. Although in 1986 the National People’s Congress adopted a short instrument

---

\(^6\) The Chinese government has committed itself to the adoption of a comprehensive Civil Code over the next four years. See TOWARDS A CHINESE CIVIL CODE: COMPARATIVE AND HISTORICAL PERSPECTIVES (Lie Chen & C.H. van Rhee eds. 2012).

\(^7\) General Rules of the Civil Law of the People's Republic of China have been adopted at the Fifth Session of the 12th National People's Congress of the People's Republic of China on March 15, 2017 and are hereby promulgated, effective from October 1, 2017.


\(^9\) *Id.* at 169, citing CHEN JIANFU, FROM ADMINISTRATIVE AUTHORIZATION TO PRIVATE LAW 14 (The Hague 1994).

of a mere 156 articles entitled the General Principles of the Civil Law (GPCL).\(^\text{11}\) The GPCL was a milestone in a sense since it moved China toward a market economy, but it was not a great leap forward in crafting a civil code because it retained the ideas of public ownership of property and a “planned socialist commodity economy.”\(^\text{12}\)

Oddly, there is strong evidence of a common-law type of legal system, based upon *panwen* (written legal documents) judgments or decisions, dating back to at least before the pre-Qin dynasty (before 221 B.C.).\(^\text{13}\) In this context we see that although subsequently Chinese law evolved through the use of civil-like codes,\(^\text{14}\) elements of the common law’s principle of precedent or *stare decisis* had been firmly entrenched. This is important in that it shows that the Chinese legal tradition moved beyond the “law of persons” or status based on Confucian principles; *panwen* recognizing the importance of the rule of law that similar decisions and punishments should be prescribed for similar fact situations (also based upon Confucian principles).\(^\text{15}\) Later, in the early nineteenth century, predictability in the case law was demonstrated in partnership law, where the ability of partnerships to contract and the survivorship

\(^{11}\) General Principles of Civil Law, Fourth Session of the Sixth NPC, April 12 1986 (effective January 1, 1987).

\(^{12}\) Chen, *supra* note 8 at 176-77.

\(^{13}\) Norman P. Ho, *Confucian Jurisprudence in Practice: Pre-Tang Dynasty Panwen (Written Legal Judgments)*, 22 PAC. RIM L. & POL’Y J. 48, 55 (2013). See also, Jialue “Charles” Li, Note, *China, A Sui Generis Case for the Western Rule-of-Law Model*, 41 GEO. J. INT’L L.711, 737-38 (2010) (discussing precedent in the Han and subsequent dynasties, and noting that Western scholars often neglect the role of precedent in ancient China). However, it is important to not that the ancient Chinese legal system pre-dated the Western common and civil law systems. *See generally*, JOHN W. HEAD & YANPING WANG, LAW CODES IN DYNASTIC CHINA 3-4 (2005) (noting that Chinese law predates and is distinguishable from the civil and common law traditions); *id.* at 135 (discussing the role of codification in civil and common law jurisdictions, and distinguishing imperial China from both).

\(^{14}\) Chen, *supra* note 8. See also, R. Randle Edwards, *The Role of Case Precedent in the Qing Judicial Process as Reflected in Appellate Rulings*, in UNDERSTANDING CHINA’S LEGAL SYSTEM 180, 180-81 (C. Stephen Hsu ed., 2003) (describing the ancient system in which rarely-changed “statutes” were adopted verbatim by subsequent dynasties, but “sub-statutes” evolved “in response to changing social needs”).

\(^{15}\) It was in the second century B.C. that the Emperor Wu official adopted Confucianism as the guiding principles of government and society. It remained official state doctrine until 1911. *Id.* at 75.
of the partnership after the death of a partner were universally accepted in some areas of China. The *panwen* system, which came into full force during the Han dynasty (206 B.C.-208 A.D.), was based on the application of principles to fact scenarios; analysis of context; and analogical reasoning from previously espoused *panwen* judgments. During the Han dynasty different types of *panwen* were developed using various types of reasoning. Dong Zhongshu was a key figure in developing the *panwen* system during the Han Dynasty. He used the Confucian text known as the *Spring and Autumn Annals* to derive general principles to be used in legal decisions. Dong also created hypothetical or model *panwen*, which can be seen as the precursor of the current practice of the Chinese SPC issuing of *Guiding Opinions*. The use of principles derived from the *Spring and Autumn Annals* and the application of model *panwen*, known as

---

16 Mark Allee found that in at least one Chinese locality in the early 1800s, courts treated *partnerships* as being capable of retaining or alienating contractual rights that survived the individual natural persons constituting the partnership. This arrangement almost certainly “had important implications for the rationality and predictability of economic transactions.” Mark A. Allee, *The Status of Contracts in Nineteenth-Century Chinese Courts*, in *CONTRACT AND PROPERTY IN EARLY MODERN CHINA* 159, 167 (Madeleine Zelin, Jonathan K. Ocko & Robert Gardella eds., 2004). Interestingly, the development of these contract principles predated the transplantation (or imposition) of any Western legal concepts beginning with the Opium War era in the early 1840s. The role of judicial precedent, Allee concludes, was central to these contractual principles: “[these] cases suggest that, although the statutes of codified law may appear indifferent at best, precedents established through the findings of local courts were far from inimical to economic growth.” Id. at 167.

17 Chen, *supra* note 8 at 78.

*Chunqiu Jueyu* practice,\(^1^9\) were used to decide real cases. This was a way of bringing more consistency and objectivity to the legal system, which can be compared to the current Chinese courts current inconsistent application of modern, Western-style laws. In sum, like other legal traditions there was no linear progression from a status-based law to a rule of law (freedom of contract), but, instead, Chinese history shows various mixtures of the two with one type being more dominant at a given time.\(^2^0\)

**B. Modern Chinese Contract Law**

The evolution and codification of a general contract code, culminated in the 1999 enactment of the Contract Law of the People’s Republic of China or Chinese Contract Law (CCL)\(^2^1\) and by subsequent “interpretations” of the SPC.\(^2^2\) These instruments (CCL and SPC Interpretations) can be seen as the first steps toward a general civil code. The new civil code if completed as expected over the next five years will hopefully include a new and improved law of contracts.

Movement toward a grand Chinese Civil Code is the culmination of the evolution of Western-style law in China since its shift to a partially free-market, capitalistic economy beginning in the early 1980s, but also from antecedents before the opening up of the Chinese

---

\(^{1^9}\) Chen, *supra* note 8 at 78-79.


\(^{2^2}\) The Supreme People's Court supervises the work of the local people's courts by issuing “Interpretations” on various areas of law. See, e.g., Supreme People's Court, Interpretations of the SPC on Certain Issues Concerning the Application of the Contract Law of the PRC (II) (effective May 13, 2009); Interpretation of the Supreme People's Court on Issues Concerning the Application of Law for the Trial of Cases of Disputes over Sales Contracts, adopted at the 1545th session of the Judicial Committee of the Supreme People's Court on March 31, 2012 (effective July 1, 2012).
economy. It was at the end of the Qing Dynasty (1644-1912) that the Chinese started to learn from Western laws to broaden and tailor Chinese contract codes. The first generation of modern Chinese contract law evolved through a piecemeal approach with the enactment of specialized bodies of contract law including a domestic Economic Contract Law, Foreign Economic Contract Law, Technology Contract Law, Joint Venture Contract Law, and so forth. A major event that would lead the Chinese government to embrace a more harmonized approach was its adoption of the United Nations Convention on Contracts for the International Sale of Goods (CISG) in 1988. The CISG represented China’s first experience with an international harmonizing private law instrument. It also led to the development of a higher level of expertise in the Chinese court system, and especially in Chinese arbitration tribunals. For example, the China International Economic and Trade Arbitration Commission (CIETAC), China’s premier international arbitration association, has demonstrated a somewhat astonishing grasp of the CISG and has proven its ability to interpret and apply Western-style laws in a non-biased manner.

The CISG and its application in China provided a model for constructing a harmonized Chinese law of contracts. Eleven years after the adoption of the CISG, the Chinese government

23 Chen, supra note 7 at 160-62.
24 Economic Contract Law (promulgated by the Nat'l People's Cong., Dec. 13, 1981, effective July 1, 1982)
adopted the CCL, which became effective on October 1, 1999. The law repealed the former specialized laws of contract, such as the Chinese domestic contract law and the Foreign Economic Contract Law, and replaced them with a single law that covered both domestic and international contract transactions.\(^3\) The CCL is the second generation of modern Chinese contract law. Hopefully, the new civil code will incorporate a third generation contract law that will solve the gaps and inconsistencies found in the CCL.

Part II will review the 1999 CCL including a brief look at its sources and coverage, before focusing on its general principles espoused in Articles 1-9, which will then be compared in Part V with the general principles enunciated in the General Rules. Part III examines the general principles of the General Rules, along with its specific provisions dealing with capacity and expressions of intent, as well as comparing the general principles of the 1999 CCL and the 2017 General Rules. Part IV sets the context for evaluating the place of general principles in modern Chinese contract law by examining the role of Confucian and socialistic values on how the rule of law is viewed by Chinese society. Part V also provides an extended analysis of how the Western concept of good faith has been applied in the context of Chinese cultural norms. Part VI offers the construct of hard and soft law as a way to better understand the application of transplanted Western-style law in the Chinese legal system. This view of Chinese law as a mix of hard and soft law shows that China as a rule of law society remains somewhere in the future.

II. CONTRACT LAW OF THE PEOPLE’S REPUBLIC OF CHINA (CCL)

The enactment of the CCL was a milestone in Chinese legal development in relation to

\(^3\) The CISG remains China’s international sales law, but in non-sales international transactions the CCL is the applicable law.
establishing a market economy. It acted to harmonize a piecemeal set of contract laws into a thick, comprehensive set of rules based upon the Western legal tradition.

A. Sources and Coverage

The CCL represented an improvement over the earlier nascent contract laws since it harmonizes Chinese contract law in a single instrument, is a more modern law, and is a relatively comprehensive instrument with four hundred twenty-eight articles. The CCL provides a general law of contract, like the common law, but also specialized rules applicable to different contract-types, more aligned to the nominate contracts in Roman and modern civil law.31 Its “general provisions” follow the Western-style template of rules covering the formation, performance, termination, and remedies related to breach of contract. The “specific provisions” parts provide particularized rules for different types of contracts including: sale of goods (domestically), gift (charitable subscriptions), leasing, lending, financial, services, construction, carriage of goods, technology transfer, deposit, bailment, agency, and brokerage contracts. This can be seen as following a civil law approach in contrast to the common law of contracts, which applies directly to many of the listed contracts in the Chinese law’s specific provisions. Similarly, in the United States legal system, the passage of the Uniform Commercial Code (UCC) provided specialized rules for commercial contracts involving the sale of goods, leasing of goods, negotiable instruments, secured transactions (financing), wire transfers, documents of title, letters of credit,

31 A nominate contract is a standardized contractual relationship that has a special designation attached to it, such as purchase and sale, lease, loan, and insurance contracts. For example, Justinian identified four types of real contracts including contracts in re (in a thing), mutuum (loan for consumption), commodatum (loan for use), depositum (deposit), and pignus (pledge). BARRY NICHOLS, AN INTRODUCTION TO ROMAN LAW 167 (1962).
and bulk transfers.\textsuperscript{32}

The drafters of the CCL in their quest to enunciate a truly Western-style, modern free market contract law borrowed from a host of different sources including, the CISG, UNIDROIT Principles of International Commercial Contracts (PICC),\textsuperscript{33} Principles of European Contract Law (PECL),\textsuperscript{34} German Civil Code (BGB),\textsuperscript{35} American UCC, and the common law, among others.

The problem with the use of so many different sources is that it led to numerous gaps and inconsistencies in the CCL.\textsuperscript{36} For example, the CCL borrowed many of the formation rules found in the CISG, but failed to adopt the full set of acceptance rules, leading to a gap subject to different interpretations of it and when a late acceptance leads to a conclusion of a contract.\textsuperscript{37} In the area of insecurity of performance, the CCL adopts two types of protections with different sets of rules—defense of insecurity, taken form German law, and anticipatory breach, taken from the CISG and the common law. The result is if not redundancy, at least overlapping systems of rules dealing with similar real world situations, leading to a great deal of inconsistencies in the law and in its application.\textsuperscript{38}

\textsuperscript{32}The Articles of the UCC include: General Provisions (Art. 1), Sale of Goods (Art. 2), Lease of Goods (Art 2A), Negotiable Instruments (Art. 3), Bank Deposits and Collections (Art.4), Wire Transfers (Art. 4A), Letters of Credit (Art. 5), Bulk Sales (Art. 6), Documents of Title (Art. 7), Investment Securities (Art 8), and Secured Transactions (Art. 9), available at https://www.law.cornell.edu/ucc.


\textsuperscript{34}Ole Lando & Hugh Beale, PRINCIPLES OF EUROPEAN CONTRACT LAW, PARTS I AND II, prepared by the Commission on European Contract Law (2000), available at https://www.trans-lex.org/400200/pecl.


\textsuperscript{36}See LARRY A. DIMATTEO & LEI CHEN, CHINESE CONTRACT LAW: COMPARATIVE PERSPECTIVES (Cambridge University Press 2017).

\textsuperscript{37}Jingen Wang & Larry A. DiMatteo, Western Reception and Transplantation of Western Contract Law, 34 BERKELEY J. INT’L L. 44 (2016).

\textsuperscript{38}For example, the CCL adopted both the common law concept of anticipatory repudiation (breach) and the civil law concept of defense of security. These doctrines serve similar purposes, but diverge in the area of application. See CCL Articles 68, 69, 94 and 108.
B. General Principles of the CCL

The CCL has three key objectives set out in Article 1 CCL: (i) to protect the lawful rights and interest of the contracting parties; (ii) to maintain social and economic order; and (iii) to promote socialist modernisation. The principles set out in subsequent articles serve two functions: (i) to guide the interpretation of specific substantive provisions of the CCL and (ii) to be used as a basis on which gaps in the CCL could be bridged when adjudicating a particular matter.\(^{39}\)

The first general principle underpinning all contractual agreements is that of “equality” as found in Article 2’s recognition that the parties are equal and Article 3’s obligation that no party may impose its will upon the other party. This suggests that no coercion in the process of contract formation or contract performance is permissible. However, this general assumption leaves unclear as to what should happen if there are clear instances of an inequality in the position of the parties: “The one thing that is perhaps missing from the CCL’s agreement-based definition of the nature of the contract is that it is not specified that the agreement must be intended by the parties to have the force of law, or – to put it another way – that in making the agreement the parties are demonstrating consent to be bound at law.”\(^{40}\) The importance of intention in the bindingness of contractual obligations is clearly implied in the General Rules.\(^{41}\)


\(^{40}\) Martin Hogg, “General Principles of Chinese Contract Law: A Scottish Perspective” (manuscript on file with author).

\(^{41}\) See General Rules Articles: 133 (“civil juristic acts . . . [include] the establishment, alteration, and termination of civil legal relations through an expression of intention”); 137 (“expression of intention, which is made by dialogue, takes effect when the person knows the content”); and 140 (“persons of civil conduct may make an expression of intention by express or implied ways”).
The second principle is that of “voluntariness”, or party autonomy,\textsuperscript{42} found in Article 4 CCL, according to which parties have “the right to voluntarily conclude contracts”. This concept includes the prohibition that “no unit or individual may illegally intervene therein”, which still leaves open the possibility for restrictions imposed by law on the exercise of the right to conclude a contract. It seems that the principle of “voluntariness” should not be equated too readily with the notion of freedom of contract which is the hallmark of the common law of contract (and, indeed, of all Western legal systems);\textsuperscript{43} rather, it might better be understood as freedom to contract. This is more than just semantics – as the discussion of the common law approach will show, freedom of contract is about much more than just enabling parties to enter into legally binding agreements.

Article 3 may be read in different ways. It can be seen as a further emphasis on the importance of freedom of contract as articulated in Article 2. Or, it can be interpreted as focusing on any abuse of bargaining power. It states that “parties are equal in their legal status, and no party may impose his own will upon the other party.” The phrase “equal in their status” may be a simple recognition that all civil parties have the freedom to enter into contracts. However, the phrase “no party may impose his own will upon the other part” is vague. It could be viewed narrowly as simply encompassing cases of fraud or coercion (duress) found elsewhere in the CCL. Or, it could be broadly construed as preventing a party with superior bargaining power of overreaching by negotiating a highly one-sided contract. The broader interpretation would recognize a principle not seen in other legal systems.

Article 4 can also be seen as ancillary to the principle of freedom of contract. It states that everyone has the “right to voluntarily conclude contracts.” Freedom of contract is further reinforced by Article 8, which states “contracts concluded according to law are legally binding on the parties.”

The behaviour of the parties to a contract is then regulated by the third and fourth general principles: first, in determining their respective rights and duties, the parties must observe the “principle of fairness” (Article 5); secondly, in exercising their rights and performing their duties, parties must observe the principle of “good faith” (Article 6). Unfortunately, the CCL fails to provide factors directly relevant to application of Articles 5 and 6, leaving it for the courts to specify the factors, which will be relevant in establishing whether both parties have complied with the threshold requirements of fairness and good faith. There are other provisions in the CCL, particularly on good faith, which provide greater detail: Article 42 CCL holds a party liable for (i) negotiating in bad faith; (ii) intentionally concealing a fact or providing wrong information; and (iii) any other instance which violates the principle of good faith. This suggests that two of the key aspects of “good faith” are honesty and transparency. Moreover, Article 60 requires that the parties observe the principle of good faith in performing their obligations.

The fifth general principle can be summarized as the “compliance with public interest”. “Although China has moved towards a rule of law system, public policy still plays an important role.”44 Since fairness is singled out as a public policy concern, the “Chinese courts work more like a court of equity rather than a court of law in an effort to promote fairness.”45 Thus, Article 7 specifies that parties must act in accordance with relevant laws when concluding and performing a contract, respect public morals, and not disturb the social and economic order nor harm the

45 Id.
public interest. What seems like a reasonable obligation imposed on the parties could potentially form the basis for far-reaching intervention into the contracting process—from negotiation to content to performance.

Professors Wang Liming and Xu Chuanxi have argued that the general principles of the CCL can be categorized as serving three fundamental values—“freedom of contract (hetong ziyou), good faith (chengxin), and the fostering of transactions (guli jiaoyi).” The principles of freedom of contract and good faith are contractual bedrock. All contract laws are premised on the freedom of parties to create their own private law (contract). Almost all contract law systems, recognize the principle of good faith as a means of facilitating contractual exchange (filling gaps and interpreting contracts) and as a policing mechanism to regulate abuse of freedom of contract.

The more interesting principle flagged by Wang and Xu is the principle of the fostering of transactions. This principle must be placed in the context of the first generation of contract laws, such as the Economic Contract Law and the Foreign Economic Contract Law, and their shortcomings and the advancement of a more modern unified contract by the enactment of the 1999 CCL. They argue that the earlier contract laws too often invalidated contracts by only recognizing the remedy of voidness and not voidability, as well as invalidating contracts due to ambiguity. In contrast, provisions of the CCL foster contractual exchange, when the parties indicate a general intent to enter a contract, as well as giving the victim of an invalidating act the right to reaffirm the contract (voidability).

A brief review of the main differences between the CCL and its predecessor laws will illustrate the contract friendly nature of the CCL. First, Article 58 of the GPCL renders void all contracts where there is evidence of duress, fraud, or exploitation of a party’s vulnerability.

---

Under the CCL, the victim of such conduct has the right to enforce or seek termination. Thus, more contracts deemed to be invalid *per se* under the previous law are now fully enforceable. Second, the previous contract laws automatically terminated contracts if they violate a law or regulatory provision. The CCL requires that such termination only apply to national-level laws and regulations.\(^{47}\) Third, since the previous laws did not provide rules of interpretation, if courts were faced with a contractual ambiguity they commonly held the contract to be invalid due to the ambiguity (lack of mutual assent). In contrast, the CCL provides a number of rules of interpretation, which essentially force the courts to fill in the gaps of an otherwise viable contract.\(^{48}\) Article 38 requires that standard terms shall comply with the principle of fairness. Article 41 provides that: (1) standard terms “shall be interpreted in accordance with the usual understanding of the term”; (2) the term is to be interpreted in a way least favorable to the drafter if there is more than one reasonable interpretation; and (3) if in conflict, a non-standard term prevails over a standard term. Article 62 provides a number of gap fillers including, a quality term\(^{49}\) (“contract shall be performed in accordance with the state standard or industry standard”); price term\(^{50}\) (“market price prevailing in the place of performance at the time of the conclusion of the contract”); performance\(^{51}\) (“obligation to pay money shall be performed at the place where the party receiving the money resides” and “in regard to other subject matters, the obligation shall be performed at the place where the party performing the obligation resides”), and time of

\(^{47}\) See CCL Art. 52.

\(^{48}\) See CCL Articles 38 (standard terms), 41 (standard terms), 53 (exemption clauses), 62 (gap-fillers) & 63 (price), and 66 (sequence of performance).

\(^{49}\) CCL, Article 62(1).

\(^{50}\) CCL, Article 62(2).

\(^{51}\) CCL, Article 62(3).
performance\textsuperscript{52} (“debtor may perform the contract at any time and the creditor may demand performance at any time, but the other party shall be given the necessary time for preparation”).

It is important to note that even though the CCL was a major advancement in the development of a Western-style contract law it, as the contract laws that came before, should be viewed as transitional in nature, to be replaced by a third-generation law, one that hopefully fixes the ambiguities, gaps and inconsistencies that have become apparent in the nearly twenty years of experience in the application of the CCL.\textsuperscript{53}

III. **GENERAL RULES OF THE CIVIL LAW OF THE PEOPLE’S REPUBLIC OF CHINA**

This part reviews the *General Rules* of Civil Law beginning with the structure and coverage of its six chapters: General Principles, Legal Capacity, Legal Persons, Non-Incorporated Organizations, Civil Rights, and Civil Juristic Acts. It then focuses on the ten substantive principles found in Articles 1-10, before briefly discussing the provisions on capacity and expression of intention.

*A. General Structure*

This initial part of what is intended to be the enactment of a grand general civil code consists of two hundred and six articles. It is important to note that the title to this 2017 law begins as “General Rules.” It will thus play a crucial role in the framing of the rest of the code. Initial interpretation of its articles will be vitally important in setting the tone for the entire code. As

\textsuperscript{52} CCL, Article 62(4).

\textsuperscript{53} See, e.g., Wang & DiMatteo, *supra* note 35 (gaps in late acceptance rules and right to cure’ overlap between defense of insecurity and anticipatory breach).
with the CCL, *General Rules* include potentially conflicting principles and articles due to the remaining influence of Chinese customary law and socialist principles. The first twelve articles making up Chapter I, much like what is found in the CCL, provide the general principles to be used in the interpretation and application of the specific rules enunciated in the *General Rules*, and parts of the civil code to be promulgated in the future. A detailed analysis of the general principles will be undertaken below.

Chapter II covers the areas of legal capacity including the rights of minors to enter into contracts;\(^54\) guardianship;\(^55\) declarations relating to death and missing persons;\(^56\) the status of business organizations and leased farm owners.\(^57\)

Chapter III is entitled “Legal Persons” and consists of some forty-five articles\(^58\) and covers not only natural persons, but also an assortment of business organizations including, for-profit and not for-profit businesses or organizations, along with “special persons.” Special persons cover an array of government, quasi-government, and communal organizations. The continuing existence of collective farms, a holdover from the previous communist-socialist view of property, means that farming land is based upon contract rights and not real property rights. The title to the land is held in the collective and not the individual farmers. Article 99 states that: “The rural collective economic organisations shall obtain the legal personality according to law.” This type of system is a product of historical creation of the communist system in China before its movement to a market economy. Farm cooperatives exist in the United States, but mainly serve purposes of the marketing and selling goods of small to medium sized farms, which are privately owned.

\(^{54}\) *General Rules*, Articles 13-25.  
\(^{56}\) *General Rules*, Articles 40-53.  
\(^{57}\) *General Rules*, Articles 54-56.  
Chapter IV regulates “non-incorporated organizations,” which are defined as “organizations that have no legal personality but may lawfully engage in civil activities under their own names.” These types of entities can be seen as variants of Western business organizations, such as partnerships, limited liability companies, and professional associations. But, under American law the limited partnership (LP), limited liability company (LLC), limited liability partnership (LLP), and the professional association (PA) all provide limited liability protection for its partners and members. However, Chapter IV provides that: “If the property of the non-incorporated organization is insufficient to pay off the debts, investors or the founders shall bear unlimited liability.”

Chapter V is a wide-ranging section covering “Civil Rights.” But the notion of civil rights is broadly construed to include property rights and is not a listing of fundamental human rights as is found in the American Bill of Rights or the United Nation Universal Declaration on Human Rights of 1948. Instead its focus is on individual property rights. Again, this is a product of the continuing transition from public to private ownership of property. Chapter V covers such areas as property rights, contract rights, privacy rights, intellectual property rights, as well as the right to bring actions for breach of contract, tort, and unjust enrichment. Other provisions provide for fundamental human rights but are couched in vague, general, and abstract.

---

60 *General Rules*, Article 104.
62 U.S. Constitution, Amendments 1-10.
64 *General Rules*, Articles 115-117.
65 *General Rules*, Article 119.
67 *General Rules*, Article 123.
68 *General Rules*, Article 120.
69 *General Rules*, Article 122.
Chapter VI entitled “Civil Juristic Acts” provides a brief framework of contract law. It covers the areas of requirements of contract and contract formation; conditions; defenses or validity relating to breach of contract, such as “fake expression of intent,” mistake, fraud, duress, and unfairness; limitation periods (statute of limitations); termination; contract interpretation; and restitution. Although this litany of provisions covers many areas of contract law it is vastly short of being a comprehensive contract law. It is strange that the drafters placed substantive contract law rules in the General Rules. One explanation is this cursory review of contract law rules serves as a preamble to the necessary more comprehensive bodies of rules and principles, laid out in independent parts, such as the law of persons and the law of obligations—of general civil codes to be enacted in the future. This must be the intent of the drafters since the General Rules do not repeal the CCL; that will only come if the law of obligations is later added to the General Rules. This begs the question of why it was felt necessary to place a hodge-podge set of rules on contract law in the first part of what is to become a general civil code? Also, how are these contract rules to be applied vis-à-vis the CCL? These questions will be discussed in a later section. The General Rules conclude with a chapter.

---

70 See General Rules, Article 109 (“personal freedom and personal dignity”); Article 110 (“right to life, health rights, physical rights,” as well as the “right of honour”); Article 132 (“civil subjects shall not abuse civil rights and damage the national interests”).
71 General Rules, Articles 158-159.
72 General Rules, Article 146.
73 General Rules, Article 147.
74 General Rules, Articles 148-149.
75 General Rules, Article 150.
76 General Rules, Article 151.
77 General Rules, Article 152.
78 General Rules, Article 156.
79 General Rules, Article 142.
80 General Rules, Article 157.
on agency law,\textsuperscript{81} civil liability,\textsuperscript{82} and general limitation periods.\textsuperscript{83}

\textit{B. General Principles}

This part will examine the general principles enunciated in the first ten articles of the \textit{General Rules}. More specifically, the analysis will focus on the general principles and their application to contract law—interpretation of contract law rules and the interpretation of contracts. This focused analysis is due to two factors. Much of the \textit{General Rules}, as discussed above, are directly related to contract law (rules on intention to be bound, capacity, defenses and validity of contracts, limitation period, and agency law). Second, the principles in the \textit{General Rules} can be compared to the general provisions found in the CCL. In the later case, this will allow a longitudinal analysis of changes to the values advanced in the 1999 CCL with the 2017 \textit{General Rules}.

1. Rule of Persons and Rule of Law

The ten general principles provided in the \textit{General Rules} include a mix of freedom of contract and freedom of contract-restricting values. A blend of Western capitalistic with Confucian-socialistic norms are represented in Article 1, which call for the new law to be “adapt[ed] to the requirements of the development of socialism with Chinese characteristics, and carrying forward socialist core values.” The phrase “Chinese characteristics” can be traced to Deng Xiaoping who was the supreme leader of China from 1978 to 1997, and was the force behind China’s opening

\textsuperscript{81} \textit{General Rules}, Articles 161-175.  
\textsuperscript{82} \textit{General Rules}, Articles 176-187.  
\textsuperscript{83} \textit{General Rules}, Articles 188-205.
up to Western trade and investment, as well as beginning the transition to a market economy. Prior to Deng, China’s Communist-Socialist system was based substantially on the Soviet model. 84 That model was based on a centralized planned economy. Deng declared that it was important that China move away from the Soviet model and create a model of socialism (including, a socialistic economy) based upon “Chinese characteristics.” 85 At this time, the idea of a socialist market economy was still viewed in the context of the law as being instrumental to advancing the policies of the State.

At the same time, Deng’s major contributions were advancing the view that all citizens were equal before the law—shifting the Mao mindset that viewed the law as the “rule of persons” (instrumental to government-control of the people) to “rule of law” in which the government is subservient to the law. 86 In the end, Deng’s view of rule of law was not one that would diminish the power of the State and the Communist Party. Instead, he advanced the notion that law should be a vehicle for the creation of individual wealth and, thus, the use of the legal system and the application of law should be aimed at improving the material well-being of the people. 87 Thus, even though the State and the Communist Party remain the dominant forces in China, the


86 Id. at 469, 475-478.

87 Id. at 475. See also, Deng viewed the formal law as a means to facilitate wealth creation, but not a Western-style rule of law. JUNE TEUFEL DREYER, CHINA’S POLITICAL SYSTEM 5 (9th ed. 2014) (Deng’s view of the rule of law was not of democratic, civil libertarianism but as purely instrumental; it was “necessary to resolve disputes … before the wheels of production could turn smoothly [wealth creation]”).
broadening of the rule of law has reduced the role of these entities in economic life. More importantly, under rule of law, the judiciary becomes superior to the Party. This is clearly not the case at present, but the idea remains robust and should influence legal development in the future.

2. Normative Tension

All contract law systems demonstrate underlying tensions between the dominant value of freedom of contract and an assorted number of principles aimed at curtailing abuse of that freedom. For example, the principle of good faith is recognized by almost all national legal systems, whether civil or common law. At one end, of the spectrum, German law places an extraordinary emphasis on the principle of good faith in the interpretation and enforcement of contracts.\(^88\) At the other end, English law continues to reject an implied duty of good faith in contracts.\(^89\) It has become an outlier as other common law systems such as Australia,\(^90\) Canada,\(^91\) New Zealand,\(^92\) and the United States\(^93\) recognize the principle as an implied term in all contracts. However, the common and civil laws continue to diverge in the area of whether there is a duty of good faith negotiations and the consequences of bad faith conduct in the pre-contract stage. Most civil law countries recognize pre-contractual liability for bad faith negotiations including a tort

---

\(^88\) See German Civil Code (BGB) § 242.
\(^89\) But, see, *Yam Seng v International Trade Corporation*, [2013] EWHC 111 (QB) (recognizes that the duty of good faith can be recognized as a contract term implied-in-fact).
\(^90\) See *Renard Constructions (ME) Pty v Minister for Public Works* (1992) 44 NSWLR 349.
\(^92\) See *Bobux Marketing Ltd v Raynor Marketing Ltd* [2002] 1 NZLR 506, 517 (dissent).
\(^93\) See Restatement (Second) of Contracts § 205.
claim of *contra in contrahendo*.\(^9^4\) The common law continues to reject the duty of good faith in pre-contractual negotiations. Although, the United States has recognized the claim of promissory estoppel that allows for the recovery of reliance damages in certain cases involving pre-contractual promises.\(^9^5\)

The other major counterpoise to unferreted freedom of contract is the notion of fairness of contract, or what James Gordley referred to as “fairness in the exchange.”\(^9^6\) Unlike, the duty of good faith, the principle of fairness has been more problematic to incorporate into contract law. Good faith can be seen as an implied term because it is a common assumption that business parties expect each other to act in good faith. This assumption is often based on good faith as a trade usage or of mutual benefit to both parties in encouraging the completion of contractual performance. In contrast, the value of fairness is a direct assault on freedom of contract. In a capitalistic system, as long as a contract is based upon mutual consent, harsh or one-sided bargains should be strictly enforced as a product of private autonomy.

Nonetheless, most legal systems are uneasy in enforcing contracts that are a product of overreaching, often due to severe bargaining power and informational asymmetries. In the Nineteenth century, the law of contracts was still anchored in the value of the fairness of the exchange.\(^9^7\) Thus, the consideration to be exchanged had to be both legally sufficient (something of value) and adequate (relatively equal value). In equity law the importance of adequacy in the

---


\(^9^5\) Restatement (Second) of Contracts § 90 (1981).


exchange was protected by the principle of equitable unconscionability. By the end of the 19th century, the equitable holdover of adequacy of consideration was expunged from the law of contracts. Thus, as long as there was some consideration—even a “peppercorn” is legally sufficient consideration—the courts were now placed under a negative obligation not to assess the relative value of the consideration being exchanged. This fundamental shift was recognized in Lon Fuller’s seminal 1941 article Consideration and Form. In this article, Fuller asserts that consideration no longer should be construed as a substantive law doctrine, but only served as a formality, much like the Statute of Frauds’ requirement that some types of contracts needed to be in written form. Interestingly, Karl Llewellyn, highly influenced by German law, reinserted the concept of unconscionability into contract law, not as an equitable principle, but as a doctrine of contract law in writing Article 2 of the American UCC. However, English law continues to reject a formal doctrine of unconscionability although the term unconscionable is commonly seen in English court decisions.

In reality, under Section 2-615 of the UCC, the doctrine of unconscionability, which applies to both business and consumer contracts but in practice is not heavily used. It has rarely

---


See Chappell & Co Ltd v Nestle Co Ltd [1960] AC 47 (“peppercorn does not cease to be good consideration if it is established that the promisee does not like pepper and will throw away the corn”). See also, Edmund Polubinski Jr., The Peppercorn Theory and the Restatement of Contracts, 10 WILL. & MARY L. REV 201 (1968) (discusses peppercorn theory and nominal consideration).

100 Lon L. Fuller, Consideration and Form, 41 COLUM. L. REV. 799 (1941).


102 See UCC §2-615.

103 See, e.g., Cavendish Square Holding BV v Makdessi & ParkingEye Limited v Beavis, [2015] UKSC 67. Lord Mance in discussing penalty clauses used this terminology: “the ultimate question as being whether the shipbuilders had shown that the clause was exorbitant, extravagant or unconscionable.” Id. at 63 (emphasis added).
been used to save business entities from heavily one-sided or unconscionable contracts.\textsuperscript{104} It main use has been in voiding specific terms in consumer contracts—such as cross-collateral security clauses in rental agreements\textsuperscript{105} and choice of forum clauses, where the agreed upon venue is deemed to be inconvenient or prohibitively costly for the consumer to bring an action.\textsuperscript{106} In these cases, a specific clause may be deemed to be unconscionable, but not the contract as a whole. American courts have not recognized the fact that a consumer contract may be highly one-sided from a valuation sense (substantive unfairness) as a case of unconscionability.\textsuperscript{107} In contrast, German law possesses strong concepts of change of circumstances (harmshifp) and contractual equilibrium as rationales for terminating contracts.

The importance of freedom of contract is found in a number of the general principles. Article 3 espouses that personal and property rights “are protected by the law; no organisation or individual may infringe upon such rights and interests.” The notions of individual free will and private autonomy are found in the phrase “equal status” used in a number of the general principles.\textsuperscript{108} The idea of freedom of contract and its basis in mutual consent is made clear in Article 5’s phrase that: “civil activities shall follow the principles of voluntariness” and that engaging in civil activities, such as entering or terminating a contract, would be recognized “according to the [parties] own intentions.” This view of civil relations as based upon voluntary

\begin{footnotesize}
\textsuperscript{104} Mallor, supra note 95 at 1088 (“danger is that courts will withhold the doctrine from deserving commercial parties”).

\textsuperscript{105} Williams v. Walker-Thomas Furniture Co., 350 F.2d 445 (D.C. Cir. 1965).


\textsuperscript{108} See General Rules, Article 2 (“legal persons and nonincorporated organisations as subjects with equal status”); Article 4 (“all civil subjects have equal status in civil activities”).
\end{footnotesize}
consent is re-emphasized in more specific provisions of the *General Rules*,\(^{109}\) which will be discussed below.

The remaining principles place constraints on the absoluteness of freedom of contract. They can be viewed both from the perspectives of Confucian-socialist values and Western legal norms. Communitarian and fairness norms are found in all legal systems—the differences being more a matter of degree than in kind. Article 6 requires contracting parties to “follow the principles of fairness in determining reasonably the rights and obligations of all parties concerned,” while Article 7 recognizes that each party “shall follow the principles of good faith, adhere to honesty and keep their commitments.”

The customary nature of Chinese law is evidenced in Article 8’s call that civil activities shall not “go against the public order and good customs.” Article 10 again notes that when the rule of law fails to resolve a dispute then “usual practice may be followed, but the public order and good customs shall not be infringed upon.” Finally, a new principle is introduced in the *General Rules*, not found in the CCL or the earlier contract law. Article 9 states that it is the duty of all legal persons to conduct business in a way that protects the environment. The communal harm caused by China’s rapid industrialization is now recognized as a core concern of Chinese society\(^{110}\).

*C. Specific Provisions*

The two areas selected for additional coverage in the *General Rules* are those of legal capacity and intention to enter into legal obligations.

\(^{109}\) See, *General Rules*, Section 2 on “Expression of Intention.”

\(^{110}\) “Any civil activity conducted by civil subjects shall be conducive to saving resources and protecting the ecological environment.” *General Rules*, Article 9.
1. Capacity

The above general principles also need to be read in relationship to the articles on capacity and consent. One uniquely Chinese or Eastern value reflected in the area of capacity is the “legal” duty of children to tend to the needs of incapacitated parents. Article 26 in the section of “Guardianship” states that: “Adult offspring have the obligation to provide for, support and protection of their parents.” The genesis of this obligation can be seen in numerous sources including the Confucian virtues of respect for the role of parent and the importance of preserving family relationships; socialist values see the family as the core unit of a collective; and economic need, exacerbated by China’s one-child policy111 and the lack of sufficient government funding of elderly care.

The age of contracting capacity is multi-faceted. While the general rule recognizes the age of eighteen as the age of majority,112 giving persons full capacity to enter into contracts as is found in most Western legal systems. However, the General Rules provide more nuanced ancillary rules that expand capacity unlike what is the norm in the West. Article 18 of the General Rules provides that a minor over sixteen years of age has “full capacity” when its main source of income derives from a job. This is an expanded version of the common law’s necessities and emancipation doctrines that give a minor who has left the care of its parents to obtain implied in fact capacity in order to make a livelihood. In contrast, Article 18 gives full capacity to enter into any and all contracts even those not related to necessities or making a

111 The one-child policy limited many Chinese couples to one-child. This was aimed at limiting population growth but had the unintended demographic consequence of leading to the aging of the population.
112 General Rules, Article 17.
Finally, an expansive form of capacity is found in Article 19 of the *General Rules*, which provides limited capacity to a minor as young as the age of eight: “such minor may independently perform any civil juristic act that has a nature of pure profit or the performance of which is compatible with his/her age and intelligence.” This contextual determination of capacity for someone of such early age is not seen in Western legal systems. The key word being that the minor has “independent” capacity.

2. Expression of Intention

The *General Rules* devotes an entire section on expression of intention. First, it supplies a specific rule for contracting by electronic means so, an offer or an acceptance becomes effective when it enters the receiving party’s electronic system (e-mail; voice message) and not when the receiving party has knowledge of its existence or opens the message. This is the consensus view in most formal laws that deal with the issue. The rationale being that parties that do

---

113 In the common law, the necessities doctrine provides capacity to minors in contracts for necessities, traditionally defined as food, shelter, and clothing. The emancipation doctrine can be seen as an expansion of the necessities doctrine when the minor is self-supporting (such as, entering contracts to run a business).

114 There are exceptions in Western laws, for example in the case of child entertainers, to grant capacity to minor through guardianship or court order. See New York State Labor Law Labor Law §186-3.1 (effective April 1, 2013), available at https://labor.ny.gov/legal/child-performer-regulations.shtm (guardian of minor must obtain Temporary Child Performer Permit from the Office of the Commissioner of Labor).

115 *General Rules*, Article 137.

business through electronic means have a duty to monitor their electronic systems for incoming messages. Article 139 uses the vague term of “announcement” as an expression of intention possibly allowing for a broad interpretation of general advertisements as legal offers and not just invitations to offer.  

The General Rules provide a broad contextual approach to the interpretation of expressions of intent (contracts). Article 142 provides that the meaning of words shall be determined based upon “the use of the words, in combination with the relevant terms, the nature and purpose of the conduct, the habits and the principle of good faith” in order “to determine the genuine meaning of the persons of the civil conduct.” Article 151 provides that “if one party uses the state of danger or lack of judgment of the other party resulting in the unfairness in the establishment of the civil juristic acts” that other party may apply to a court or arbitration association to revoke the contract. The remedies for breach of contract found in General Rules Article 179 include: “eliminate the impact or restore the reputation” and “Apologise.” The importance of status and reputation embedded in Confucian values is at work here—a proper apology or a restoration of reputation being recognized as independent remedies than that of mere payment of damages.

The socialist history of China is seen at work in Article 185, which allows for civil liability against any person who infringes on the “reputation and honour of heroic martyrs and public interests are damaged.” It is through such provisions that the Communist Party acts as the gatekeeper to the past. In the context of Article 185, the Party guards its legitimacy through such provisions that provide civil liability against anyone infringing on the reputation and honor of martyrs. History is itself a source of political legitimacy in China and as such has long been

http://www.uniformlaws.org/shared/docs/computer_information_transactions/ucita_final_02.pdf, § 214: “Receipt of an electronic message is effective when received even if no individual is aware of its receipt”.  

117 General Rules, Article 139: “The expression of intention made in the form of an announcement shall enter into force at the time of issue of the announcement.”
contested politically. Robert Bickers states that: “We cannot understand the resurgence of China now, and its sometimes quiet, sometimes raucous and foul-mouthed anger at the world, unless we understand the traumatic century which followed the first opium war … For mere history matters in modern China, and the past is unfinished business.” Finally, Article 186 provides that in cases of breach of contract a party may sue in contract or tort.

In the end, one characteristic of the General Rules, as well as the CCL, is the vagueness of many of its provisions including the general principles and more specific provisions. Vagueness in law, especially contract law, can be positive in providing flexibility for courts to deal with novel cases and to render justice, when strict rule application would cause an injustice:

Vagueness in the law gives judges the power and latitude to construe laws in ways that serve the public interest. The Chinese courts seem to work more like courts of equity and try to ultimately deliver fairness. The inherent problem with vagueness is that it leads to inconsistency and may serve as a vehicle for corruption.

As intimated in the above quote, the negative consequence in the use of vague principles or standards, as opposed to fixed rules, is uncertainty in law application. This is why common law

---


119 General Rules, Article 186: Article 186 “If the personal rights and property rights of one party have been infringed due to the breach of contract of the other party, the injured party has the right to choose to claim the liability for breach of contract or tort liability.”


121 Matheson, supra note 42 at 378.
systems generally expunge principles of fairness from their contract law. The rationale being that businesses’ distaste uncertainty and prefer hard and fast rules that are clear and applied uniformly.  

D. Comparing the General Principles of CCL with the General Rules

The General Rules and CCL possess a mix of principles that from the perspectives of the civil, and especially the common law, seem confusing and conflictive, with the potential danger of diminishing the certainty and predictability of contract law. The general principles of the CCL can be divided into two different groups based on their primary functions, namely “private autonomy” and “public regulation”. While private autonomy—the right of private parties to create their own law though contract—is fundamental in the Western and Chinese contract law systems, judicial activism or intervention is more likely in the Chinese courts. This is, as explained extensively above, due to cultural norms. The CCL as applied seems to subject contracting parties to greater judicial control. Although both systems use comparable labels that set limits to the operation of freedom of contract, there is a clear difference in how widely or restrictively these are applied. English common law generally has a very restrictive approach, and courts are reluctant to interfere in the bargain reached between the parties.”

The CCL includes comparable restrictions to those of the General Rules, but are more broadly restrictive in some instances. Exhibit 2 compares the general principles of the CCL with

---


123 Christian Twigg-Flesner, supra note 37 at 20.
those of the *General Rules*.

Comparative Analysis of General Principles

<table>
<thead>
<tr>
<th>Chinese Contract Law 1999</th>
<th>General Rules of the Civil Law 2017</th>
</tr>
</thead>
<tbody>
<tr>
<td>“maintaining social and economic order and promoting socialist modernisation” (Article 1)</td>
<td>“maintaining social and economic orders, adapting to the requirements of the development of socialism with Chinese characteristics, and carrying forward socialist core values” (Article 1)</td>
</tr>
<tr>
<td>“contract, as referred to in this law, is an agreement whereby natural persons, legal persons or other organisations, as equal parties” (Article 2)</td>
<td>“civil laws adjust personal relationships and property relationships between natural persons, legal persons and nonincorporated organisations as subjects with equal status” (Article 2)</td>
</tr>
<tr>
<td>“contracting parties are equal in their legal status, and no party may impose his own will upon the other party” (Article 3)</td>
<td>“All civil subjects have equal status in civil activities.” (Article 4)</td>
</tr>
<tr>
<td>“parties enjoy, according to law, the right to voluntarily conclude contracts” (Article 4)</td>
<td>“civil subjects engaging in civil activities shall follow the principles of voluntariness” (Article 5)</td>
</tr>
<tr>
<td>“parties shall observe the principle of fairness” (Article 5)</td>
<td>“shall follow the principles of fairness in determining reasonably the rights and obligations of all parties concerned” (Article 6)</td>
</tr>
<tr>
<td>“parties shall observe the principle of good faith in the exercise of their rights and performance of their duties” (Article 6)</td>
<td>“shall follow the principles of good faith, adhere to honesty and keep their commitments” (Article 7)</td>
</tr>
<tr>
<td>“respect public morals, and they shall not disturb the social and economic order or harm the public interest” (Article 7)</td>
<td>“civil activities may [not] violate laws or go against the public order and good customs” (Article 8)</td>
</tr>
<tr>
<td></td>
<td>“any civil dispute shall be resolved in accordance with the law . . . but the public order and good customs shall not be infringed upon”</td>
</tr>
</tbody>
</table>
First, it should be noted that freedom of contract does not appear in either the CCL or the General Rules. The issue of incorporating the language of freedom of contract was highly debated during the drafting process. Instead, the concept of voluntariness is used in Article 4 of the CCL and Article 5 of the General Rules. This was primarily due to the fear that using the word “freedom” would have political consequences. Also, there existed a fear of abuse of freedom of contract by a party to a contract. However, in most Chinese commentaries voluntariness is equated to freedom of contract and is now a commonly accepted principle of its contract law with limitations based upon Chinese characteristics. An example of cultural spillover to the law is the emphasis placed in Chinese law on the mediation of disputes: “People’s mediation is a Chinese way of resolving contradictions and settling disputes without resorting to legal proceedings.” Mediation is seen playing an “important role in preventing and reducing civil disputes, resolving social conflicts, and maintaining social harmony and

---

125 Id. at 244.
126 Id. at 244-46.
stability.” The problem is that Chinese courts have been known to pressure parties into protracted periods of mediation in order to avoid making a decision on the merits.

Article 3 of the CCL is problematic since it broadly states that: “no party may impose his own will upon the other party.” In the hard negotiations of the free market a battle of wills is often the means of obtaining the most efficient contract. Thus, if this provision is broadly construed it could inhibit the free bargaining need to create efficient markets. If, however, the imposition of will merely refers to cases of duress or fraud, then the phrase does not pose such a threat. Since, the CCL contains specific provisions dealing with duress, fraud and exploitation; the idea of overcoming a party’s will, may simply be a reflection of these common policing doctrines.

The most troublesome of the principles from a free market perspective is the fairness principle found in Article 5 of the CCL and Article 6 of the General Rules. The idea of a counterpoise to freedom of contract based upon contractual imbalance is an old concept. In the English common law the equitable principle of unconscionability allowed the equity courts to withhold equitable remedies based upon the unfairness of contract. German law has recognized hardship in which a contract that was fair upon conclusion becomes imbalanced subsequently, due to a change of circumstances. In American law, the doctrine of unconscionability is a principle of law. But, in most cases, Western law requires something much more than simple one-sidedness to intervene, especially in commercial contracts. In fact, the doctrine of unconscionability in Article 2 of the American Uniform Commercial Codes legally applies to consumer and commercial sale of goods, but in practice is rarely ever used to police one-sided

---

128 Zhang, supra note 126 (there are more than 820,000 people’s mediation organizations in China, and 4.67 million people’s mediators).
commercial contracts. Thus, the CCL’s mandate that the parties follow the principle of fairness and the *General Rules* call for courts to “follow the principles of fairness in determining reasonably the rights and obligations of all parties” provides an avenue for the courts to abuse their discretion in intervening in merely one-sided contracts. Fortunately, as will be seen in the later discussion of the principle of good faith, the courts often use the principles of fairness and good faith in tandem. This indicates that the courts will require something more than simple one-sidedness before they overturn the express terms of a contract.

### IV. Modern Contract Law with “Chinese Characteristics”

The concept of law with “Chinese characteristics” will be explored to provide insight on how the Western-style CCL and *General Rules* may be interpreted and applied by Chinese courts. These laws are placed in the cultural context of Chinese society including, the role of Confucian values, socialistic principles instilled since the Communist revolution of 1949, as well as the notion of Chinese characteristics as espoused by the State and the Communist Party. An analysis of the purposes and importance of general principles within a legal system will be offered. Finally, a section is devoted to the assertion that the principle of good faith acts as a meta-principle in Chinese contract law. The duty of good faith is a Western concept, especially in civil law systems, imported into Chinese law. It is this principle and its application that reflect the true

---

meaning of law with Chinese characteristics. The notion of good faith contracting is closely aligned with the Confucian concept of virtue and the communitarian perspective of socialism. The result of these influences is a broader role of good faith in Chinese law than is found in Western law.

Chinese contract law can be considered a mixed-jurisdiction-type of law in a number of ways. First, the drafters of the modern contracts laws—CCL and expectantly in the drafting of a new civil code—have borrowed from the legal systems of the civil and common laws. In the rules of both Chinese and Scots contract law one sees the mark of the civilian and the common law traditions. In civilian terms, one finds in the CCL the principle of good faith (Article 6, and elsewhere), the exceptio non adimpleti contractus (Articles 66–69), culpa in contrahendo (Articles 42–43), third party rights (Article 64), and the actio pauliana (Articles 74–75), among others, and one does not find any requirement of consideration in order to validate a contract. In common law terms, the CCL has rules on anticipatory breach (Article 94(2)), fundamental or material breach (Article 94(4)), and foreseeability of loss as a limitation on recoverable damages (Article 113).

Second, the influence of the predecessor communist-socialist system of law persists. The communitarian-collective themes attendant to socialistic systems is found in the general principles of the CCL and the new General Rules. Third, China has a long history of non-formal customary law that still play a role in business practice, as well as how contracts are viewed as a private ordering instrument. Confucian norms also deter resorting to the court system as a method of resolving contract disputes. Instead, compromise, negotiations and informal mediation

---

have been the longstanding means of resolving disputes.\textsuperscript{132} This type of resolution is done within the context of the parties’ relationship, informal third-party persuasion, and the fear of negative reputational effects.\textsuperscript{133} In this type of extra-legal system the party that has been injured is often persuaded to “give way”—that is not to enforce contract rights with the hope that it can recoup its losses in future dealings.\textsuperscript{134} Thus, relational and social norms play an out-sized role in the negotiation, performance, and enforcement of contracts than is the case in Western legal systems. The normative context in which business operates in China continues to be influenced by traditional values represented by Confucianism and socialist principles.

\textit{A. Confucian Values and Norms}

Confucianism has dominated Chinese culture for millennia. It is an anti-individualistic ideology that view relationships and collective values to be more important than individual freedom.\textsuperscript{135} A concrete example of the influence of Confucian values and socialistic principles on Chinese contract law is the expansive use by the courts of the principle of good faith. The use of good


\textsuperscript{133} Cohen notes even during the Ching Dynasty where local magistrates were given the authority to rule on local disputes that: “the law in action provided a more accurate index of the Chinese predisposition to compromise.” \textit{Id.} at 1210. There are patches of such extra-legal, extra-judicial customary law systems in more formal rule of law countries. These types of social or self-help systems are generally trade-related. See Lisa Bernstein, \textit{Opting Out of the Legal System: Extralegal Contractual Relations in the Diamond Industry}, 21 J. LEGAL STUD. 115 (1992) (exploring how diamond traders use extracontractual relations to enforce promises); Lisa Bernstein, \textit{Private Commercial Law in the Cotton Industry: Creating Cooperation, through Rules, Norms, and Institutions}, 99 MICH. L. REV. 1724 (2001) (associations—one representing mill owners and another representing cotton merchants—have colluded to create a private resolution system within the cotton industry where reputational effects is a major persuasive force in resolving disputes).

\textsuperscript{134} Jerome phrases it as follows: “Moral [persons] did not insist on their ‘rights’ or on the exclusive correctness of their own position, but settled a dispute through mutual concessions that permitted each to save face.” \textit{Supra} note 125 at 1207-08.

faith comports with traditional values of the common good and mutually beneficial relationships, as opposed to the more individualistic nature of American contract law where enforcing the parties contract as written is deemed to be the courts’ primary role. In contrast, Chinese courts have been more willing to intervene in a contract that they deem as being “immoral” (unfair).\textsuperscript{136}

Confucianism values morality based upon respect of social status and relational norms over formal law.\textsuperscript{137} One commentator has linked the principle of good faith to the duty of care in fiduciary duties, which is closer to the Chinese view of good faith.\textsuperscript{138} The parties, under the good faith principle, owe a duty of care to one another and to society. Thus, courts may see the strict enforcement of a particular contract as antithetical to the Chinese cultural view of good faith. Thus, the principle of good faith through the lens of Chinese culture is as much a moral principal as it is a legal one. The principle of good faith helps to maintain China's traditional mores and commercial ethics. By embracing the principle of good faith, the Chinese courts are aligning the principle with China's traditional morality and business ethics, which is also consistent with the norms of international commercial practice. With its strong moral force, the principle of good faith can be expected to contribute much to the establishment of a normative transactional order in China.\textsuperscript{139}

Wang and Xu provide a framework for understanding the duties implied under the principle of good faith. In the area of contract negotiations, it requires: duty of loyalty in forming contracts, duty of honesty and non-deception, duty to keep promises and duty of

\begin{flushleft}
\textsuperscript{136} Id. at 326.
\textsuperscript{137} As one commentator has noted: “From the Confucian perspective, law is considered secondary and supplementary.” Id. Thus, Confucian values and traditions continue to influence how the Chinese view contracts. See MING-JER CHEN, INSIDE CHINESE BUSINESS 80, 142-43 (2001) (Chinese traditionally viewed formal written contracts as unnecessary as an insult to the reputations and integrity of the parties).
\textsuperscript{138} Leonhard, supra note 135 at 326.
\textsuperscript{139} Liming & Xu Chuanxi, supra note 44 at 13.
\end{flushleft}
confidentiality.\textsuperscript{140} After formation of the contract, parties have a good faith duty to diligently prepare for performance.\textsuperscript{141} During the performance phase a number of ancillary duties are linked to good faith performance including, duty of loyalty, duty to disclose defects, duty to notify of change in circumstances that may impact performance, duty to cooperate, and duty to provide instructions.\textsuperscript{142} At the termination of the contract, the parties have a duty to give advanced notice, especially in cases of long-term contracts, duty not to terminate unless a delay or defect in performance amounts to a frustration of the purpose of the contract, and the duty to not terminate a contract if defects in an installment “comprise but an insignificant part of the entire order.”\textsuperscript{143} Good faith also requires the honoring of the post-contractual duties of confidentiality and loyalty.

Finally, the principle of good faith also plays a major role in the interpretation of contracts. This use essentially dictates a contextual approach to interpretation where courts are expected to consider “the nature and purpose of the contract, the business customs at the location of the contract's formation, and so on, so as to arrive at the parties' true intention and meaning” and “balance the parties' interests and determine the terms of the contract fairly and reasonably.”\textsuperscript{144} Unfortunately, in the broader sense, the contextual approach in Chinese law may refer to a context that is unrelated to the particular parties and their contracts. This broader contextual approach is based on extralegal considerations such as advancing the mandates of the Communist Party and the policies of the Chinese government.

Confucianism’s worldview that each person has a certain role to play in the creation of a harmonious society, and that personal relationships, or \textit{guanxi} remains a key feature of Chinese

\textsuperscript{140} \textit{Id.} at 17-19.
\textsuperscript{141} \textit{Id.} at 18.
\textsuperscript{142} \textit{Id.} at 20.
\textsuperscript{143} \textit{Id.} at 20-21.
\textsuperscript{144} \textit{Id.} at 22.
society. Guanxi suggests relationships that include mutual obligation, reciprocity, and goodwill. This type of view sees contracts as minor reflections of a contractual relationship—instead of seeing breach of contract as triggering a legal right it sees breach or “adjustment” of the contract as triggering a moral right: “Once guanxi is established between two people, each can ask a favor of the other with the expectation that the debt incurred will be repaid sometime in the future.”

Thus, Westerners negotiating contracts in China should be aware of how constructs like guanxi impact the Chinese view of the lesser role of formal contracts compared to the importance of the relationship in drafting the contract, and the normalcy of requests for subsequent changes to the contract.

Guanxi is just one example that shows the lack of importance of formal law in the long history of China:

The concept and doctrines of legality, unlike the precepts of Confucianism, have never occupied a central role in traditional imperial China. There has not existed a legal culture with elements like officials' fidelity to law or citizens' consciousness of their legal rights, which provide the necessary conditions for the effective operation of a modem Western-

---


The concept of guanxi networking, which includes a heightened loyalty to immediate family, affects the business and contract climate in ways Westerners do not expect. It creates an aversion to conflict and litigation. This changes the structure of negotiations; post-ratification changes are expected and encouraged if it helps avoid a breach and results in a fulfilled contract.

Stanley Lubman has noted that the relationship between informal normative concepts like *guanxi* is not necessarily adversarial in nature to the drafting of formal contracts or to formal legal rules. In fact he argues that they may be complimentary in nature. Formal contracts and contract rules serve the primary functions that they do elsewhere in the world—they provide a framework for economic relationships, a blueprint of the parties’ obligations, and allow parties to plan for the future. The difference is between the formal view of written contracts as static instruments and the sanctity of contractual rights (Western view) versus the view that formal contracts are starting points meant to be flexible and subject to adjustment. Thus, where a Western party sees a Chinese request to re-negotiate terms in the contract as an act of bad faith, the Chinese party sees it as a natural phenomenon of the essence of cooperation and mutual interests embedded in the business relationship.

There is evidence, however, that the introduction of formal contract law has begun to loosen the grip of cultural norms on contract relationships. The rise of commercial and contract litigation in the Chinese courts demonstrates that business and ordinary persons now see the law and litigation as a means of protecting their interests. The rise of contract litigation also shows

---

149 Lubman, *supra* note 4 at 73-74.
150 “Although Westerners view contract formation (signing) as the culmination of the process, this is just the beginning of the process for the Chinese.” Matheson, *supra* note 42 at 382.
151 Lubman, *supra* note 4 at 73.
152 See generally Timothy Lau, Kyle Niemi, & Lanna Wu, Note, *Protecting Trademark Rights in China Through Litigation*, 47 STAN. J INT’L L. 441 (2011) (urging that litigation may be a productive means to protect one’s trademark rights in China). See also Benjamin L. Liebman, *Legal Aid and Public Interest Law in China*, 34 TEX. INT’L L.J. 211, 282 (1999) (acknowledging that while the wide-scale protection of individuals is still uncertain, “China’s experience with both legal aid and class action litigation demonstrates that, in many cases, governmental policy goals may be consistent with expanding access to the legal system and the vindication of individual rights”).
that even though contracting relationships remain influenced by cultural norms and customary law, the institution of formal contract law has expanded the level of impersonal contracting that has undercut the influence of extra-contract practices and cultural norms on economic relationships.\textsuperscript{153}

\textit{B. Communism and Socialistic Principles}

Between 1958 and 1978, the Chinese economic system was based on a planned economic model with all allocation decisions made by government authorities: “The rights and obligations of the parties and dispute resolution arising in these contractual exchanges were, to a large extent, based on custom and relations. There did not exist a comprehensive contract law system, or any formal application of contract law.”\textsuperscript{154} Communist ideology and socialist principles reinforced the collectivist values of Confucianism. Under the latter, social roles and values were more important than individual interests. The former did not recognize private ownership of property, and therefor had little use for private contract law. In essence, all property was owned by the State, and in all contracts at least one of the parties was the state.

In fact, the remnants of a primitive, functional legal system, including contract law, was destroyed during the era of the Cultural Revolution from 1966 to 1976.\textsuperscript{155} In 1978, the Communist Party lead by Deng Xiaoping made a radical change in policy, to transition from a


\textsuperscript{155} See Wang Chenguang, \textit{Introduction: An Emerging Legal System}, in INTRODUCTION TO CHINESE LAW 1, 5-7 (Wang Chenguang & Zhang Xianchu eds. 1997); JONATHAN D. SPENCE, \textit{The Search for Modern China} 704-05 (1990); YUHUA WANG, TYING THE AUTOCRAT’S HANDS 51 (2015).
planned economy to a market-oriented economy, which began in 1993. As reliance on the centrally controlled economy began to wane, the importance of private contractual exchanges increased, leading to the need for a more formal contract law. But, such a law needed to be in sync with a quasi-capitalistic, quasi-socialistic market economy. Thus, the focus needed to move away from the common good and public interest model of exchange, based upon Confucian and communistic-socialistic principles, to one focused on economic self-interest and private autonomy. Thus, the notion of freedom of contract in which private parties determine the content of their contracts without government interference, was made the guiding principle in the drafting of the CCL. However, as will be seen, the meaning of “freedom” and “without government interference”, was not known or well understood in Chinese law and culture. In reality, especially in the beginning of the free contract era, government interference into private ordering remained commonplace.

Also, the CCL included numerous general principles that limit or police the exercise of freedom of contract. The CCL further incorporated numerous and exceedingly vague specific provisions stating, that free contract was “subject to” other government laws, policies, and authorities. Such provisions are found in CCL Articles 10, 38, 44, 77, 126, 129, 132 133, 137, 142, and 150. Furthermore, the CCL voids contracts in cases where there are negative third-party externalities on private parties, the public or state interests. “Although China has moved towards a rule of law system, public policy [as stated by the government and government agencies or interpreted by the courts] still plays an important role.” Nonetheless, the recognition of freedom of contract as a fundamental principle of contract law served an important first step in the development of a separate private law regime in China:

156 Id. at 4.
157 CCL Article 52 (1) & (2).
158 Matheson, supra note 42 at 380.
Although China has moved to a market economy, administrative institutions still have the inclination to interfere with enterprises, particularly state-owned enterprises, in their business decisions. The freedom of contract provision provides legal means to resist such intervention.\(^{159}\)

Despite the cultivation of a private ordering system, communism, as represented by the Communist Party, continues to influence Chinese culture with its emphasis on the common good and the importance of communal, group or personal relationships, and obedience to superiors in the governmental and societal hierarchy.\(^{160}\)

A major problem for rule of law and certainty in law application is the out-sized power of local governments in the Chinese system to interpret the law to advance local needs, as well as to protect local corruption; at times at the expense of national laws and regulations. Despite the rhetoric of rule of law and equality before the law, the reality is that courts are not viewed as superior to state agencies: “In the bureaucratic hierarchy, courts are only parallel to, rather than superior to, other units of the Chinese bureaucracy. When courts seek to enforce judgments, agencies whose actions are required to assist the courts sometimes refuse to cooperate.”\(^{161}\)

\(^{159}\) Progress and Problems, supra note 146 at 9.

\(^{160}\) Pattison and Heron, supra note 140 at 486. See also, Teema Ruskola, Law Without Law, Or is "Chinese Law" an Oxymoron?, 11 WM. & MARY BILL RTS. J. 655, 659-60 (2003) (Chinese society based upon obedience to superiors).

\(^{161}\) Lubman, supra note 4 at 29. The influence of government and state agencies in judicial proceedings illustrates that the courts are not considered as independent, but as a quasi-state agency. This is partly due to constitutional shortcomings and the dictatorial rule of Imperial and then Communist China. Thus, “separation of powers is not a concept put to use in the Chinese government.” Matheson, supra note 42 at 376. In his review of the CCL upon its adoption in 1999, James Hitchingham stated that the governmental agencies continue to regulate contractual relations [and] newly borrowed contract standards are still undefined. . . . Consequently, in the near term, contracting parties may continue to find contractual justice elusive.” James Hitchingham, Steeping up to the Needs of the International Marketplace: An Analysis of the 1999 Uniform Contract Law of the People’s Republic of China, 8
legal localism is reinforced by the fact that local judges are hired and paid by the local
government and Communist Party apparatus.

C. Contract Law with 'Chinese Characteristics'

As discussed above, social practices and cultural norms stemming from a long-history of extra-
legal mechanisms for dealing with business relationships, influenced by Confucian and
socialistic values, has by necessity been vital in the creation of modern contract law. Or, putting
it in more concrete terms, the meaning of legal terms, such as good faith, must be determined not
from the Western perspective, but from the context of Confucian-socialistic norms. Good faith is
a powerful example; its use and application quickly became a robust part of Chinese contract law
because it is a core value of Confucian thought. Thus, these “embedded structures” (traditions,
customs, principles) shaped the understanding of Western legal concepts by the drafters of
Chinese contract law, and despite the similarity of terminology between Chinese and Western
contract law, these embedded structures continue to guide interpretation and application of
Chinese contract law. The same can also be said of embedded structures of equity law, which
continue to influence the application of the common law.

Article 1 of the General Rules gives as one of its purposes the advancement of a private

\footnotesize

\begin{itemize}
    \item \textsuperscript{162} Lucie Cheng and Arthur Rosett noted that: “A practice's compatibility with familiar social patterns is a
factor that will influence the ease of its adoption and use.” Lucie Cheng & Arthur Rosett, \textit{Contract with a Chinese Face: Socially
    \item \textsuperscript{163} See T. Leigh Anenson, “Studies in Equity: The Fusion of Unclean Hands in America” (unpublished
    doctoral thesis; on file with author); Larry A. DiMatteo, \textit{The History of Natural Law Theory: Transforming Embedded
    Influences into a Fuller Understanding of Modern Contract Law}, 60 University of Pittsburgh Law Review 839 (1999)
\end{itemize}
law that: “adapt[s] to the requirements of the development of socialism with Chinese characteristics, and carrying forward socialist core values.” Again, what is meant by the notion of law with Chinese characteristics? At its most abstract level this notion’s goal is to blend Eastern and Western cultural and business values. Chinese cultural values are represented by customary law, which has evolved over many centuries and was briefly discussed in the previous section’s review of the Confucian value system. More recently, the 1949 transition to Communism began the enculturation of Chinese society with communist-socialist principles including the ideas of complete subservience to the State and collectivism. Some of these principles had long been within the Chinese cultural belief structure stemming from its ancient imperial and feudal systems. Socialism reinforced some of these longstanding values, as well as emphasizing new variations of these communitarian norms.

In 2015, the Chinese State Council issued a document entitled “The Socialist System of Laws with Chinese Characteristics (Socialist System of Laws).” The surprising thing about this document is the recentness of its issuance after three decades of the opening of Chinese markets to international trade and towards a market economy. The forward in the document states: “We need to bring into being a socialist system of laws with Chinese characteristics so as to ensure there are laws to abide by for the carrying on of state affairs and social life.” It is important to note that the document is not referring to socialism as an appendage to Communism, but as it relates to a “social democracy.” But, how can such a term be reconciled with the dictatorial nature of the system (dictatorship by consensus of the most elite)?


---


165 Id.
economy,” “exercises the rule of law, building a socialist country governed according to law,” and “respects and protects human rights,” that “citizens’ lawful private property is inviolable,” and that “the system of multi-party cooperation and political consultation led by the Communist Party of China will exist and develop in China for a long time to come.”166 In the end, the crucial definition is what is the meaning in Chinese culture and law of the creation of a “socialist market economy”? One answer can be seen in the Socialist System of Laws’ description of the role of the Constitution:

China’s Constitution defines the basic system and basic tasks of the state. It affirms the leadership of the CPC, establishes the guiding role of Marxism-Leninism, Mao Zedong Thought, Deng Xiaoping Theory and the important thought of the ‘Three Represents,’ which determines the state system as a people’s democratic dictatorship led by the working class and based on the alliance of workers and peasants. It also takes the system of people’s congresses as the form of administration.167

This understanding of the dominance of the Chinese Communist Party, explains the inherent contradictions caused by the intermeshing of autocracy and free markets, and between public and private property. For example, despite the General Rules recognition of private property, the spirit behind the law is that such property should be used to advance social interests. Private parties cannot own fee title in real estate but can “buy” real estate based upon long-term leases of 50 to 70 years.168 Another facet of the Chinese market system, as noted earlier, is the

---

166 Id. at 3.
167 Id. at 6.
decentralized nature of government regulation where local governments are given substantial power to regulate businesses “in the light of the specific local conditions and needs.”169

Another example of a convergence of long held cultural norms and modern contract law is the Chinese concept of *heli* or reasonableness, which is a major feature of the common law and is especially robust in Article 2 of the American Uniform Commercial Code. The CCL makes numerous references to reasonableness,170 but again the cultural meaning of *heli* influences the application of such a standard. Thus, it is important to note that the concept of *heli* is much more textured then that of mere reasonableness. In Chinese culture, reasonableness or *heli* is linked with notions of fairness or justice.171 This linkage has two major consequences. First, Chinese courts, much like arbitral panels,172 balance the interests of the parties, as well as society and the State, to render fair and equitable decisions, thus, avoiding the strict enforcement of contract rights and contract law rules. Second, such a view of contracts requires a broad contextual approach to contract interpretation including taking into account the background relationship of the parties, the circumstances relating to the formation and performance of the contract, and customary practices in a trade or business. Professor Timoteo explains that judges bring a tripartite framework in the interpretation of law and contracts: *heqing* (feelings, relationship, circumstances), *heli* (reason), and *hefa* (legal rules). Thus, courts are placed in the position of

---

169 Socialist System with Chinese Characteristics,” supra note 164 at 8. It should be noted that China is a diverse country that includes 155 ethnic autonomous areas, five autonomous regions, 30 autonomous prefectures and 120 autonomous counties.

170 See, e.g., CCL Articles 24 (reasonable time), 39 (reasonable manner), 69 (reasonable time), 74 (unreasonably low), 94(3) (reasonable time), 95 (reasonable time), 110(3) (reasonable time), 111 (choose reasonably), 118 (reasonable time), 119 (reasonable expenses), 158 (reasonable time), 426 (determined reasonably).

171 The *li* in *heli* translates into reason or reasonable and “it was used in strict connection with the concept of *yi*, a term that is generally translated as justice or righteousness.” Marina Timoteo, *Vague Notions in Chinese Contract Law: The Case of Heli*, 18 EUR. REV. PVT. L. 939, 942 (2010).

striking a balance between the “relationship, rightness, and law.”\textsuperscript{173} Timoteo argues that these factors have had an important impact on the creation of operative rules in the Chinese courts.\textsuperscript{174}

Thus, despite no formal adoption by the CCL, heli paved the way for the Chinese courts’ recognition of the doctrine of \textit{rebus sic stantibus} or change of circumstances in the enforcement of contracts.\textsuperscript{175} The SPC recognized, in a \textit{Guiding Opinion}\textsuperscript{176} and a \textit{Judicial Interpretation},\textsuperscript{177} the doctrine of change of circumstances and the idea of contractual adjustment. The SPC indicates in its guidance that the parties should renegotiate an adjustment of the contract when there is a material change of circumstances and the courts should act to mediate an adjustment if the parties fail to reach agreement.\textsuperscript{178} Article 26 of the Interpretation provides that if a material change in circumstances occurs after the formation of a contract, which would render continued performance of the contract manifestly unfair, the court can amend or terminate the contract.

As of the present, the best that can be said is that China in a short period of time has created a formal legal system and a great body of substantive law; however, it still has a long way to go to be considered as a country governed by the rule of law, as least not in the Western sense.\textsuperscript{179} Clearly, it has never been the goal of the Chinese government or Communist Party to have China evolve into a liberal democracy based on Western standards.\textsuperscript{180} The creation of a

\textsuperscript{173} Timoteo, \textit{supra} note 161 at 943.
\textsuperscript{175} Timoteo, \textit{supra} note 161 at 944.
\textsuperscript{176} See SPC, “Opinion on Several Issues Relating to the Trial of Civil and Commercial Contractual Disputes under the Current Situation” (July 7, 2009).
\textsuperscript{177} SPC, “Second Interpretation on Several Issues Concerning the Application of the Contract Law” (May 13, 2009).
\textsuperscript{178} Timoteo, \textit{supra} note 161 at 949.
\textsuperscript{179} Orts, \textit{Rule of Law}, \textit{supra} note 1, at 47 (“there is a substantial difference from a normative perspective between the mere existence of a legal system and establishing the rule of law”).
\textsuperscript{180} See, e.g., Charles Burton, \textit{China’s Post-Mao Transition: The Role of the Party and Ideology in the ‘New Period’}, 60 PACIFIC AFFAIRS 431, 431 (1987) (the overriding purpose of post-Mao reforms “is to
modern legal system has served a more instrumental goal of stimulating economic development and wealth creation, but also to maintain the unquestioned power of the government (Party) as the core source of law. In this sense the adoption of Western-Style law and the recognition of freedom of contract as an important private ordering instrument has been a key to China’s economic growth.

Despite, however, the introduction of the rule of law through the adoption of Western-style substantive law, the impartial, objective, and well-reasoned judicial application of the law has not been a hallmark of the Chinese court system. Important government (bureaucracy), Party, and local non-governmental power structures (organizations, rural collectives) continue to influence judicial decision-making. As one scholar has noted, the Communist Party is the “ghost hidden in the legal machine.”\textsuperscript{181} For most courts if there is a perceived conflict between government policy (national, regional, local) and formal law they will most often ignore the law and side with policy objectives.\textsuperscript{182}

Just as the vague general principles found in the CCL and the General Rules, and other borrowed Western legal concepts, the rule of law is an empty vessel to be defined in the unique context of Chinese culture, values, and power structures. The next section will revisit the role of general principles and the example of the good faith principle in the framing of a contract law with Chinese characteristics.

\footnotesize{\textsuperscript{181} Orts, Rule of Law, supra note 179 at 67.}
\footnotesize{\textsuperscript{182} Placing it in the context of the rule of law, a scholar in 1994 stated: “the use of Party policy documents to provide the necessary context for legal interpretation. These doctrines have also sustained the view that law derives its coherence of meaning more from its political and social context than from a reasoned interpretation of statutory language.” Perry Keller, Sources of Order in Chinese Law, 42 AM. J. COMP. L. 711, 711 (1994). In the following two decades this is still largely the case. But, on going improvements in legal education and the training of judges has improved the legal reasoning skills of the judiciary leading to better reasoned legal decisions based on the rule of law, at least in the relatively mundane, apolitical nature of most contract disputes.}
D. Purpose of General Principles

The CCL enumerates several important principles and places them at the very beginning of the instrument to show their importance in understanding and interpreting the CCL. These articles, distinguished from legal rules, are treated as general or “fundamental.”\footnote{Shiyuan Han, “General Principles of the CCL” at 11 (manuscript on file with author).} The general principles can be used in a number of ways. First, the principles are used to interpret and apply the more specific rules found in the law. Secondly, general principles may be used to prevent injustice due to the strict application of specific contract law rules.\footnote{Id. at 7.} Thirdly, the general principles can be used to interpret and fill in gaps of a contract. Fourthly, general principles can be used to police contracts and monitor the improper conduct of the contracting parties. An example of the second and third use of general principles is the Chinese Supreme Courts recognition of change of circumstances. There is no express provision in the CCL on parties’ obligation to re-negotiate a contract that has become a burden on one of the parties due to an unforeseeable change of circumstances. The SPC filled the gap in its “Interpretation of the SPC on Certain Issues Concerning the Application of the Contract Law of the PRC (II).”\footnote{Supreme People's Court, Interpretations of the SPC on Certain Issues Concerning the Application of the Contract Law of the PRC (II) (effective May 13, 2009).} Article 26 reads as follows:

When after the conclusion of a contract there is a grave change of objective circumstances, which is not foreseeable by the parties at the time of the conclusion of the contract, and which is not caused by a force majeure and which should not be classified as commercial risks, to continue to perform the contract will be obviously unfair for one party or will not achieve the
purpose of the contract, the party requests the people’s court to modify or terminate the contract, the people’s court shall determine whether to modify or terminate it or not, according to the principle of fairness, and taking the real situations of the case into consideration.

The use of a general principle to supplant a specific rule in order to avoid an unjust result is a controversial concept. In fact, the mainstream view is that specific rules supplant any application of a general principle. The purpose of specific, fixed rules is to provide certainty to the law of contract.

At times a given dispute raises the issue how to resolve the application of conflicting principles? One such case is Xinyu Co. Ltd. v. Feng Yumei, which involved a shopping center owner’s attempt to terminate a contract of sale. After the owner sold shopping space to the defendant, the owner decided to change the theme of the complex and proceeded to buy back the nearly 150 spaces that it sold. The defendant was one of two parties that held out. The complex owner brought an action requesting a termination of the contract. The court held in favor of the complex owner, even though it was the breaching party. The court held that under the principles of fairness and good faith, the defendant-purchaser should have cooperated by selling back the shop space given the change in the theme of the complex. Despite the fundamental, principles of freedom of contract and pacta sunt servanda (sanctity of the contract), the court believed it was for the greater good to terminate the contract. Such a decision would be considered absurd in most other legal systems.

186 Xinyu gongsi su Feng Yu-mei shangpu maimai hetong jiufen [Xinyu Co. Ltd. v. Feng Yumei, 2006:6 Gazette of the Supreme People’s Court of the People’s Republic of China 37-42
187 It is important to note that the sales contract had not been registered as required by law and thus, the property although under contract had not yet been officially transferred.
188 CCL Art. 5.
189 CCL Art. 6.
190 See CCL Article 107.
Professor Shiyuan Han explains the rationale for the decision based upon Chinese cultural traits: “In China, it is generally acceptable to put social public interest before personal interest.”\textsuperscript{191} He further notes that Chinese judges tend to follow a “result-oriented” method of legal reasoning: “Chinese judges consider not only legal effects (Falü xiaoguo) of the judgments, but also their social effects (shehui xiaoguo).”\textsuperscript{192}

The idea of placing Chinese normative values inside of a Western-style body of law is explored below using the example of the principle of good faith. Put simply, the duty of good faith has more substantive sweep under Chinese values than it does under Western-style law, including the German law’s embrace of good faith as a core private ordering instrument.

\textit{E. Good Faith as Meta-Principle?}

1. Good Faith as Cultural Dependent Principle

In all legal systems, civil, common and mixed jurisdictions, the freedom of contract principle is the core foundation of contract law. But due to bargaining power and informational asymmetries there is allows the threat that freedom of contract if left unchecked will lead to abuse (unconscionable or illegal contracts). Therefore, there needs to be a countervailing principle that can be used to police contractual misconduct, overreaching, and abuse. There are numerous more tailored doctrines of principles used to police specific kinds of abuse—“abuse of rights” in French law (enforcement of contract rights); \textit{culpa in contrahendo} in civil law (pre-contractual misconduct); “surprise terms” in German law (standard terms regulation); duty to re-negotiate

\textsuperscript{191} Han, \textit{supra} note 172 at 11. \\
\textsuperscript{192} \textit{Id.} at 12.
(change of circumstances); waiver and estoppel in the common law; the penalty rule in the common law; and so forth. But, the general policing doctrine that best responds to abuse of freedom of contract is the principle of good faith. The duty of good faith is explicitly or implicitly found in most national and international contract laws.\textsuperscript{193} Although it is important to note that English law, one of the more popular choices of law in international contracts, does not expressly recognize a general duty of good faith, it often reaches similar outcomes by other means, such as through contract interpretation and implied terms.\textsuperscript{194} Finally, the principle of good faith has a strong influence in international commercial arbitration.\textsuperscript{195}

The good faith provision in the German Civil Code\textsuperscript{196} has had a pervasive impact on the enforcement and interpretation of contracts, and the application of contract law rules.\textsuperscript{197} One commentator explains that:

\begin{quote}

\textsuperscript{194} The mainstream opinion is that the United Kingdom is an outlier in the area of good faith. It is true that UK courts have soundly rejected such a duty. But, in reality, bad faith contract has been policed in more covert ways under English law leading to similar outcomes that result in countries that have expressly adopted a general duty of good faith in all contracts. See \textsc{Elisabeth Peden, Good Faith in the Performance of Contracts} 11 (2003) (noting that the duty of good faith "is slowly being introduced into England through European and international initiatives"); Elena Christine Zaccaria, \textit{The Dilemma of Good Faith in International Commercial Trade,} 1 MACQUARIE J. BUS. L. 101, 103 (2004) (noting that English law takes a different "route" to reach results arrived at in civil law, without recurring to good faith). More recently, a UK court has recognized that good faith can be an implied in fact term in a contract in certain circumstances. Yam Seng Pte Ltd v International Trade Corp Ltd., [2013] EWHC 111. It is also important to note that other common law countries, such as Australia, Canada, and the United States, have adopted the duty of good faith. See, (Australia); (Canada); and Uniform Commercial Code §§ and Restatement (Second) of Contracts (1981).


\textsuperscript{196} BGB §241.

\end{quote}
Paragraph 242 of the BGB has played an extremely important role in German jurisprudence. The judge or, as the case may be, the arbitrator, acts (a) in exercising his function, to apply the law and, as appropriate, to specify the consequences of what is established by law; (b) to limit the exercise of contractual rights where there may be an excess in the abusive exercise of the right; and (c) even contra legem, to impose himself in the form of a true ethical-legal rupture of the legal right. Hence, the German trier of fact has learned how to use the letter of paragraph 242 in a radically different manner depending on the ethical-political demands of the time. The German jurist has introduced, together with the principal obligations of any contract, so-called accessory obligations. These include, for example, the duty of vigilance, the obligation of clarification to the other party, loyalty, the obligation to cooperate, and the obligation to inform.\textsuperscript{198}

Good faith clearly acts as a meta-principle in German law in which most issues of contracts are seen through its prism. At the opposite end of the spectrum is English law’s rejection of the good faith principle; English law’s dislike of the principle is anchored in the view that such an abstract limiting principle adds an unacceptable degree of uncertainty to contract law and the enforcement of contracts.

2. Good Faith in the Chinese Cultural and Legal Context

The Chinese legal perspective of the good faith principle is aligned with German law. In fact, Chinese scholars refer to good faith as the “King clause” referring to the civil law use of the

\textsuperscript{198} Cremades, \textit{supra} note 184 at 773.
term “general clause” or to what the common law would call a general principle.199 This is not surprising due to the strong influence German law has had on Chinese law—historically it had an indirect influence through the Chinese study of the Japanese Civil Code, which was based on the German Civil Code, and directly in the drafting of China’s modern contract laws.200 Also, the good faith principle aligns with Confucian thought and values.201 Along with its relationship to traditional Chinese values, the principle of good faith has served functional needs. Because of the rapid rate of change (economic and legal) Chinese laws often are filled with numerous gaps in coverage. The good faith principle is often used as a gap-filler of choice.202

As under other civil law systems, good faith constitutes one of the fundamental principles of the entire Chinese civil or private law.203 The CCL recognizes a duty of good faith in the negotiation, performance, and enforcement of contracts.204 Chinese scholars have favored the use of the good faith principle by the courts to fill in gaps in statutory law and by its use in the interpretation and enforcement of contracts.205 The importance of good faith is that it provides the judicial discretion needed to work out new law through the adjudication process. Also, as

200 “The legal model chosen by Chinese reformers is the German system, filtered by the Japanese experience.” Novaretti, 955 (referencing the drafting of the Chinese (Republican) Civil Code of 1931. Japan adopted the German Civil Code (Burgerliches Gesetzbuch or BGB) in 1898. Given the role of Confucianism in Japanese society the Japanese enactment of the German law was created much interest, and subsequent study, in China. Keller, supra note 171 at 718. This influence was demonstrated by the enactment of the “Six Codes” in the 1930s, which was essentially the Chinese government’s “reception of the Romano-German civil law tradition.” Id.
201 “The doctrine recognizes and enforces traditional Chinese notions of morality and business ethics.” Leonhard, supra note 128 at 310.
202 Id. at 311.
204 CCL Arts. 6, 42(3), 60, 92, & 125.
noted previously, the Chinese have a built in affinity for good faith because of its civil law tradition, as well as being consistent with Chinese cultural norms:

Good faith has not only been one of the general principles for people's everyday conduct but has also been a crucial moral precept in China's commercial practice. By embracing the principle of good faith, the Contract Law is recognizing China's traditional morality and business ethics, which is also consistent with the norms of international commercial practice.206

Professor Novaretti explains the malleability of the good faith term in Chinese legal tradition due to its association with a basket of societal norms. The good faith principle in Chinese culture captures the norms of “honesty and credibility,” good intentions, trust, human virtue, integrity, benevolence, solidarity, doing right, morality, loyalty, social justice, fairness, and collective well-being.207 This normative set is the context upon which the principle of good faith is to be applied. The practical implication of this broad societal view of good faith include: (1) a greater likelihood of avoiding terms of contract in favor of ethical standards and trade practice; (2) reliance on broader use of contextual evidence; (3) more likely to consider societal and collective interests and policies of the State; (4) promoting contractual justice or a fair balance in the contract;208 (5) recognition of a duty to re-negotiate contract terms to achieve fairness in cases of change of circumstances; (6) duty to disclose information,209 (7) duty to perform additional

206 Wang & Xu, supra note 44 at 15.
207 Novaretti, supra note 188 at 954, 956, 958, 960 & 962.
208 Id. at 965 & 967.
209 The duty to disclosure information may mean disclosure of materials facts related to the contract and in some cases a duty to disclose alternatives or options available. See People’s Court of Xiling district, city of Yichang (Hubei), Case 497/2004, available at www.chinacourt.org/ajdq (posted April 5, 2007).
duties not formally specified in the contract,\textsuperscript{210} and (8) promote mediation of contract disputes. Due to the importance placed on collective interests, societal norms, and cultural values, in some instances, the contract can be viewed as a three-party contract: party-to-party and parties-to-society; in an informal way society can be seen has having third-party rights or being third-party beneficiaries.\textsuperscript{211} Exhibit 1 shows the use of good faith and associated principles throughout the CCL and the General Rules.

\textbf{Exhibit 1}

\textbf{Duty of Good Faith in Chinese Law}

<table>
<thead>
<tr>
<th>Value</th>
<th>Article CCL</th>
<th>Article General Rules</th>
<th>Concrete Application</th>
</tr>
</thead>
<tbody>
<tr>
<td>Good Faith (core)</td>
<td>6</td>
<td>7</td>
<td>In the exercise of their rights and performance of their duties; Adhere to honesty and keep their commitments</td>
</tr>
<tr>
<td>Fairness</td>
<td>5</td>
<td>6</td>
<td>In determining their respective rights and duties; In determining reasonably the rights and obligations of all parties concerned.</td>
</tr>
<tr>
<td>Bad Faith Negotiation</td>
<td>42</td>
<td></td>
<td>Negotiates in bad faith under the pretext of concluding a contract; intentionally conceals a material fact; other acts that violate the principle of good faith;\textsuperscript{212} liability under preliminary agreements\textsuperscript{213}</td>
</tr>
<tr>
<td>Public Interest</td>
<td>52</td>
<td></td>
<td>Conceals an illegal purpose in a lawful form; violates the public interest</td>
</tr>
<tr>
<td>Malfeasance to Malfeasance</td>
<td>59</td>
<td></td>
<td>Harm the interests of the state, a collective organisation or</td>
</tr>
</tbody>
</table>

\textsuperscript{210} Novaretti, \textit{supra} note 188 at 973.

\textsuperscript{211} The principle of good faith as expressed by the General Principles of Civil Law, therefore, is not merely aimed at regulating the relationship among the parties to an agreement but, rather, seeks to weigh the interests of the subjects involved in the legal relationship in question against the interests of the state and society. \textit{Id.} at 963.

\textsuperscript{212} The SPC expanded the reach of Article 42 (3) (“engages in other acts that violate the principle of good faith”) into to the area of conditional contracts. So if one party is obligated to register or obtain a government approval “fails to complete such procedures [related to registration or obtaining an approval], such party shall be deemed to have committed "any other act in violation of the principle of good faith" specified in Item (3) of Article 42 of the CCL.” Interpretation of the Supreme People's Court on Certain Issues Concerning the Application of the Contract Law of the People's Republic of China II, Article 1 (effective date May 13, 2009) (Interpretation on Contract Law II)

\textsuperscript{213} The SPC broadened the duty of good faith negotiations to include preliminary agreements, stating that: “if one party does not perform the obligation of concluding a sales contract and the other party requests that it assume liability for breach of the preliminary agreements or demands the rescission of the preliminary agreements and claims compensation for damages.” SPC Interpretation on Issues Concerning Disputes over Sales Contracts (effective July 1, 2012), Article 2.
<table>
<thead>
<tr>
<th>Third Parties</th>
<th>a third person</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cooperation, Notice, Confidentiality</td>
<td>Observe the principle of good faith and perform such duties as giving notice, providing assistance and maintaining confidentiality in accordance with the nature and purpose of the contract as well as the usage of transaction</td>
</tr>
<tr>
<td>Post-Contractual Obligations</td>
<td>After contractual rights and obligations are discharged, the parties shall observe the principle of good faith and perform such duties as giving notice, providing assistance and maintaining confidentiality in accordance with the usage of transaction</td>
</tr>
<tr>
<td>Contract Interpretation</td>
<td>In light of the words and expressions used in the contract, the related terms in the contract, the purpose of the contract, the usage of transaction and the principle of good faith; the use of the words, in combination with the relevant terms, the nature and purpose of the conduct, the habits and the principle of good faith shall not be restricted by the used words and sentences, the relevant clauses, the nature and purpose of the conduct, the habits and the principle of good faith shall be considered in combination to determine the genuine meaning of the persons of the civil conduct²¹⁴</td>
</tr>
<tr>
<td>Setting a Reasonable Price relating to debtor</td>
<td>Debit transfers his property at a price that clearly is unreasonably low²¹⁵</td>
</tr>
<tr>
<td>Standard Terms Regulation</td>
<td>Comply with the principle of fairness when determining the rights and duties of the parties, shall, in a reasonable manner, draw the attention of the other party to the terms which exclude or limit his liability and term is void if it increases the liability of the other party or deprives the other party of a major right²¹⁶</td>
</tr>
<tr>
<td>Change of</td>
<td>SPC</td>
</tr>
<tr>
<td></td>
<td>Recognition by Supreme People’s Court²¹⁷</td>
</tr>
</tbody>
</table>

²¹⁴ The role of good faith in contract interpretation is re-emphasized in the Interpretation on Contract Law II, Article 1. The SPC states that a valid contract only needs to provide the name of the parties, subject matter, and the amount, and the court will imply the remaining terms through Articles 61, 62 and 125 of the CCL (principle of good faith).

²¹⁵ Interpretation on Contract Law II, Article 19 clarifies what is an unreasonable law price as one that is 70% lower than the market price.

²¹⁶ Interpretation on Contract Law II, Article 6 clarifies the Article 39 (CCL) obligation of the party supplying the standard terms to bring them to the attention to the other party in a “reasonable manner.” It states that: “the party providing the standard clauses, at the time of conclusion, adopts the word, symbol, character style or other special marks that are sufficient to invite the other party's attention to the exemptible and restrictive clause regarding its liability and render explanations of such clauses upon the other party's request, the people's court shall determine that the former party has "adopted the reasonable manner” as specified in Article 39 of the CCL.” Article 9 again recognizes that in the area of exemption from liability or exculpatory clauses the supplier of the standard terms has the “obligation of reminder and explanations.” Failure to do so results in the voiding of the clauses.

²¹⁷ Interpretation on Contract Law II, Article 26 (if an unforeseeable and significant change of
<table>
<thead>
<tr>
<th>Circumstances</th>
<th>Page No.</th>
<th>Source</th>
<th>Explanation</th>
</tr>
</thead>
<tbody>
<tr>
<td>Reasonable liquidated damages or penalties</td>
<td>114</td>
<td>SPC</td>
<td>If liquidated damages are excessively higher than the loss incurred, the parties may apply to the people's court or arbitral institution for an appropriate reduction.</td>
</tr>
<tr>
<td>Reasonable time to give notice of non-conformity (defect)</td>
<td></td>
<td>SPC</td>
<td>SPC Interpretation on Issues Concerning Disputes over Sales Contracts (effective July 1, 2012), Article 17 states that the court should determine a reasonable time for inspection of goods “based on the principle of good faith”</td>
</tr>
<tr>
<td>Agency</td>
<td>61, 62, 170</td>
<td></td>
<td>Restriction on the authority of the legal representative by the Articles of Association of the legal person or the governing body of the legal person shall not confront the counterparties in good faith and limitation on the authority of personnel who complete the tasks for the legal persons or the non-incorporated organisations shall not confront the counterparties in good faith.</td>
</tr>
<tr>
<td>Registration of company or organization</td>
<td>65</td>
<td></td>
<td>If the actual situation of a legal person is inconsistent with the registered items, it shall not confront the counterparty in good faith.</td>
</tr>
<tr>
<td>Improper Company Resolutions</td>
<td>85</td>
<td></td>
<td>Resolutions between the legal person and the counterparties in good faith shall not be affected.</td>
</tr>
<tr>
<td>Company governance</td>
<td>86</td>
<td></td>
<td>A for-profit legal person who engages in business activities shall abide by business ethics, maintain transaction security, accept government and social supervision, and assume social responsibility.</td>
</tr>
<tr>
<td>Civil rights</td>
<td>110, 132</td>
<td></td>
<td>Natural persons enjoy the right to life, physical rights, health rights, name rights, portrait rights, reputation, right of honour, privacy, marriage autonomy and other rights. The civil subjects shall not abuse the civil rights and damage the national interests, the social public interests.</td>
</tr>
<tr>
<td>Public order &amp; social customs</td>
<td>143(3), 153</td>
<td></td>
<td>Civil juristic acts that violate public order and social customs are invalid.</td>
</tr>
</tbody>
</table>

3. Good Faith in Chinese Legal Practice

circumstances that are not ordinary “commercial risks, and to continue with the performance of the contract will be obviously unfair to one concerned party or will not realize the purpose for which such contract was concluded” then the court may “modify or terminate the contract on the basis of the principles of fairness”).

218 Interpretation on Contract Law II, Article 29 specifies any reduction in the amount of liquidated damages shall be “according to the principles of equity and good faith.” It further states that any liquidated damages amount that is 30% or more than the actual damages incurred will be deemed to be excessively high.
In practice, the actual application of the good faith principle has been characterized by uncertainty. First, good faith is often directly connected with trade practice. In some parts of the CCL the principle of good faith is subjugated to trade practice. Article 60 provides that parties in the performance of their obligations shall perform such duties as notification, assistance and confidentiality “in accordance with the nature and purpose of the contract and trade practice.” Article 92 states that good faith performance duties after the termination of the contract shall be “in accordance with trade practice.”

In the area of contract interpretation, Article 125 provides that the meaning of a contract term should be based upon its wording, the purpose of the contract, trade practice, and the principle of good faith. Thus, the good faith principle is only one element to be used in the interpretation of contracts. Even a reference to a self-standing requirement of good faith may be qualified by its context. CCL Article 42 extends the good faith duty to the negotiations of contracts, such as: (1) bad faith negotiation with no real intention to contract; (2) deliberate concealment of material facts or the deliberate conveying of misinformation; or (3) ‘other conduct in contravention of the principle of good faith’. The first examples are obvious cases of bad faith conduct so the question is how broad should the third example be construed in the regulation pre-contract? It is uncertain whether withdrawal from an ongoing negotiation without a good reason or failure to notify, assist or protect the other party’s interests amounts to “other conduct in contravention of the principle of good faith.”

Despite scholarly consensus in support of the use of the good faith principle, there is no general agreement on its practical meaning.\(^{219}\) Good faith translates from Chinese into “honesty, 

\(^{219}\) McKendrick & Liu, supra note 192, citing UNDERSTANDING AND APPLYING THE SPC INTERPRETATION II ON CONTRACT LAW 73 (Shen Deyong, XI Xiaomin & SPC Research Office eds., People’s Court Press, 2009).

\(^{220}\) Id. citing, See Xu Guodong, Two Notes on the Principle of Good Faith, 4 CHINESE J. L. 74 (2002).
trustworthiness, and creditability.”221 However, the breadth of good faith has yet to be worked out by Chinese scholars or judges. Must a party disclose confidential information during the negotiation of a contract? How should the implied duty of loyalty be defined and applied? Since specific definitions often fail, Professor Laing suggests the following approach:

[A party is required to] respect the interests of the other party, attend to its affairs with the same care used for one’s own affairs, ensuring that each party to the legal relationship obtains its due share of benefit, and not to benefit oneself at the cost of the other’ [and, additionally, not to] ‘harm the interests of a third party or the society by one’s own conduct’ [and to] ‘exercise one’s right in a way congruent with its social-economic purposes’.222

This is a very abstract and broad view of good faith that is far beyond the notion of good faith in the civil or common laws. It shows the continuing influence on some scholars of socialistic principles held over from communism. Professor Bing Ling offers a more modern and practical version of the role of good faith as being the standard of conduct accepted in a community, such as “in the community in which the transaction takes place,” which can be characterized as the demands of commercial reasonableness.223


223 Bing Ling, Contract Law in China 54 (Sweet & Maxwell Asia 2002), as quoted in McKendrick & Liu, supra note 192 at 5.
There is also confusion, despite the use of the good faith principle by Chinese courts, regarding its actual importance in judicial reasoning. For example, good faith is often used unnecessarily in the application of specific rules articulated in the CCL.\textsuperscript{224} Professors McKendrick and Liu note that: “there exists a common practice amongst Chinese courts, particularly courts at the lower level of the hierarchy, of blindly resorting to good faith as an omnipotent solution irrespective of the availability of a direct and specific solution to the dispute before the court.”\textsuperscript{225}

McKendrick and Liu also note that it is common in Chinese judicial decisions not to cite the good faith principle independently of also citing other general principles in the CCL, such as the principles of equality, voluntariness, and fairness.\textsuperscript{226} This shows that many judges do not make a distinction between the general principles despite the fact that they serve different normative values. For example, parties may act in good faith and still produce a one-sided or unfair contract.\textsuperscript{227} The courts have also confused the principle of good faith with invalidity of contracts or contracts due to concerns of public policy and morals.\textsuperscript{228}

The Chinese courts recognition of an unlimited duty of good faith are most likely due to cultural influences, such as socialist norms and Confucian values, that have been previously discussed.\textsuperscript{229} These norms and values focus on communal or societal interests and not on private

\textsuperscript{224} McKendrick & Liu, \textit{supra} note 192, citing Luo Yi, \textit{The Application of the Principle of Good Faith in Civil Judgments – An Empirical Survey of 53 Cases Reported in the SPC Gazette}, 11 J. L. APPLICATION 58 (2009); Xiaoyi City Chenming Coal Char Ltd v Shanxi Province Gangyu Coal Char Ltd., SPC, 24 Dec 2012, (2012) Min Er Zhong Zi No. 104 (attempted termination of contract because output capacity was less than stated in the contract; Supreme People’s Court held that termination should not be permitted because the output capacity was fairly close to the amount stated in the contract).

\textsuperscript{225} McKendrick & Liu, \textit{supra} note 192.

\textsuperscript{226} CCL Articles 3 to 5.

\textsuperscript{227} Matheson, \textit{supra} note 42 at 353.

\textsuperscript{228} Yu Fei, \textit{Distinguishing between the Principle of Public Order and Morality and That of Good Faith}, 11 SOCIAL SCIENCES IN CHINA 146 (2015).

\textsuperscript{229} Pattison & Herron, \textit{supra} note 140.
autonomy. This is seen in the continuation of rural collectives and public ownership of real property. In such a context, contracts and personal rights are interests that are routinely subordinated to group rights and interests. To some extent, every contractual relationship is regarded as embedded in a deeper, wider societal relationship. Consequently the signing of a contract as a symbol of its sanctity is downgraded to merely ‘the beginning’ of the parties’ real business relationship.\(^{230}\) It is for this reason not objectionable to raise, beyond the terms of a contract, an expectation that the parties cooperate and help each other out when needed. Equilibrium in the reciprocal exchange between the parties is accepted as an essential part of what contractual justice comprises.

Coupled with a civil law tendency to resort to general clauses of civil codes,\(^{231}\) the above cultural factors have led to a reluctance or inability of Chinese lawyers at times to separate law from morality and a corresponding over-anxiousness in them to succumb to the influences of cultural codes of ethics in spite of the direct applicability of fixed rules of law or clear terms of contract.\(^{232}\) The antagonism between the principle of good faith and that of freedom of contract has not gone unnoticed. In contrast to its Western counterpart, the modern Chinese law of contract seems to have followed a path of evolution in the opposite direction. While the common law countries have moved in the direction of a wider acceptance of the implied duty of good faith, Chinese legal reasoning has become more rigorous resulting in the diminishing of the over use of good faith as the rationale for case decisions.

Since the establishment of the PRC, the notion of good faith gained a foothold and acquired a wide reception in Chinese contract law. The notion was then gradually encroached upon as a

\(^{230}\) Id. at 491.
\(^{232}\) Examples can be seen observed from Wang & Xu, supra note 44 at 16, 18, 19 & 20-21.
result of the rise of freedom of contract.\textsuperscript{233} An accompanying development has been the disappearance of cases in which a court relied solely upon such general principles as that of good faith in reaching a decision. Chinese courts are now increasingly aware of the need to identify concrete rules of law applicable to the dispute. However, as noted earlier, there is still a widespread judicial practice that the principle of good faith is invoked together with other, more specific provisions of law, even when the specific provisions deal directly with the issue at hand.

A decision of China’s premier international arbitration panel, China International Economic and Trade Arbitration Commission (CIETAC), provides an example of what seems like a case of straightforward contract interpretation to one in which the principle of good faith and reference to customary practices are used to provide additional justificatory weight to the arbitration panel’s decision.\textsuperscript{234} The case involved the sale and purchase of space heaters from a German seller to a Chinese buyer. The obvious time of year to sell such heaters is during the winter season. The contract provided that the buyer could return any unsold units and receive a full refund. This ended up being the case. The buyer sent notice to seller’s agent of its intent to return a number of units. The facts show that the buyer delayed in giving notice until after the winter season had come to an end and failed to provide the warehouse location where the seller could take over the goods. Nonetheless, the arbitral panel held in favour of the buyer.

The panel recognized the CISG as the applicable law, but used provisions in the CCL to render its decision considering the issues of the case to be outside the scope of the CISG. The panel began its opinion by unnecessarily confirming two general principles—“reflects the true minds of the two parties and does not violate mandatory provisions of the laws and

administrational regulations of China.” Despite the application of specific provisions the panel’s analysis essentially rested on whether the buyer acted in bad faith by delaying notice and not providing sufficient content in its notice or whether the seller acted inappropriately in not making prompt arrangements to take back the goods? The first issue concerned the calculation of the price of the heaters for purposes of setting the refund amount. The court held that the parties had subjectively different interpretations on the appropriate method of calculation. The panel sided with the seller using the reasonable person standard of CISG Article 8(2): “a reasonable person of the same kind as the [Seller] would have understood the contract price as the unit price of each model, but not the total contract price as alleged by the [Buyer].”

The panel, then wrongfully disregarded the CISG interpretive methodology (interpretation through the general principles of the CISG) and, instead, utilized provisions 60 to 62 of the CCL. In the end, it didn’t matter since the content of those provisions were the same general principles as provided for in the CISG. In regard to the appropriateness of the buyer’s notice and the seller’s response, the panel referred to CCL Article 60: “The parties shall fully perform their respective obligations in accordance with the contract. The parties shall abide by the principle of good faith, and perform obligations such as notification, assistance, and confidentiality, in light of the nature and purpose of the contract and in accordance with the relevant usage.”

---

235 Id. at 13.
236 Interpretation should provide a meaning “according to [the] intent where the other party knew or could not have been unaware what that intent was.” CISG Article 8(1). If such meaning is not determinable than the interpretation shall be according to the understanding that a reasonable person of the same kind as the other party would have had in the same circumstances.” CISG Article 8(2).
237 Heaters case, supra note 223 at 15.
238 CCL Article 60 (emphasis added).
panel held that the listing of the goods to be returned was sufficient notice since it allowed the seller enough information to prepare for taking back the goods.\(^{239}\)

In regard to the setting of the refund price, the panel references Article 61 of the CCL: “[If an] agreement is unclear, the parties may agree upon supplementary provisions to such terms through negotiation. In the case of a failure in doing so, the terms shall be determined from the context of relevant clauses of the contract or by transaction usages.” Finally, the panel recognizes the civilian notion of purposive interpretation as noted in Article 62 of the CCL: “If the method of performance was not clearly prescribed, performance shall be rendered in a manner which is conducive to realizing the purpose of the contract.” It is from these open-textured rules (standards), the panel reasons that the buyer’s notice, although not complete in content, was sufficient to trigger the seller’s obligation to tack back the goods.

The panel states the first order rule is the parties’ mutual obligation to negotiate a resolution in good faith. Failing a successful negotiation, then recourse would be through analogical reasoning from other provisions in the contract and then to applicable trade usage. If this proves unsuccessful, then “the performance shall be rendered in a manner which is conducive to realizing the purpose of the contract.”\(^{240}\) The purpose of the contract was for the seller to supply a sufficient number of heaters for the winter season and allow the buyer to return the unsold units. In the end, the court reasoned that the seller “violated the honest and good faith principle”\(^{241}\) since it did not attempt to directly negotiate a return of the goods from the buyer, instead using surrogates, and then failing to provide a “letter of entrustment” requested by the

\(^{239}\) “[As to the] content of the return notice, the Arbitration Tribunal deems that as long as the models and quantity of the goods were clearly indicated in a notice which would enable the [Seller] to make preparation to accept the goods, the requirements for a reasonable return notice is fulfilled.” Heaters case, supra note 223 at 16. The panel should have referred to CISG in determining the reasonableness of the notice.

\(^{240}\) Id. at 15.

\(^{241}\) Id. at 17.
buyer stating that the seller’s agents had the authority to negotiate the return. Finally, the seller’s
demand that the refund was to be made in the Chinese currency (renminbi) instead of the
currency stipulated in the contract (euros) “set an unreasonable barrier to the return of the
goods.” As we can see from this case, the direct interpretation from the provisions of the
contract through specific CISG or CCL rules is abandoned in favor of general principles,
expressed or implied by the relevant law— a reasonable person of the same kind; parties shall
abide by the principle of good faith; violated the honest and good faith principle; realizing the
purpose of the contract; and an unreasonable barrier to the return of the goods.

In the same case, the principle of good faith worked in the seller’s favor on the issue of
liquidated damages. The contract provided for a 1 % per diem liquidated damages charge. The
court found the per diem amount to be too high and reduced the amount to 10% per annum under
Article 114 of the CCL and holding that a reduction to the 10% per annum was justified under
“the equal and reasonable principle.”

Finally, Professor Novaretti has shown that Chinese courts sometimes use the good faith
principle to shift the burden of proof from the plaintiff to a defendant. In one case, a
replacement refrigerator (the original refrigerator was defective) was delivered without the buyer
able to personally inspect the refrigerator at the time of delivery. Subsequently, the buyer
noticed mold and other imperfections leading to a claim that the seller had delivered a used

242 Id.
243 CCL Article 114 states that: “if the agreed liquidated damages are excessively higher than the loss
incurred, the parties may apply to the people's court or arbitral institution for an appropriate reduction.”
244 Heaters case, supra note 223 at 17.
245 Novaretti, supra note 188 at 976-78.
246 Id. at 977-78. It is important to note the Chinese civil procedure rules provided for such a shift in the
burden of proof. Article 7 of the Regulations on Evidence in Civil Proceedings (Supreme People’s Court
on November 9, 2003) states that: “In the event that the present Regulations, existing provisions, and
judicial interpretations cannot be adapted to a given legal question in order to determine the burden of
proof, the People’s Court ought to base the determination on the principles of good faith and fairness, as
well as the parties’ evidentiary competence.”
refrigerator instead of a new replacement. The court shifted the burden of proof from the plaintiff (consumer) to the merchant-seller to prove that the refrigerator was new. In sum, without legislation that spells out the boundaries of judicial discretion, a mechanism to guide court reasoning in applying specific rules in a timely way, and a body of well-trained judges, unjustified intrusion by courts into the autonomy of contracting parties remains a real danger in China.

IV. THE PARADIGM OF HARD-SOFT LAW

This part will use the analogy of hard-soft law found in international law study—the CCL and future Civil Code being the hard law and cultural values acting as soft law in the interpretation and application of the hard law. The second section makes some recommendations as China advances toward a general civil code.

A. Chinese Contract Law as a Hard and Soft Law System

In international private law, the concept of soft law or customary international law plays an important role in the performance of contracts and in the resolution of disputes. Courts and arbitral tribunals will at times look outside the applicable hard law, such as domestic contract law or the CISG, to evidence of trade usage, business customs, and commercial practice to interpret contracts and in determining if there is a case of bad faith performance. In other areas, such as international finance, soft law takes the form of standards and principles. At times, soft law can

247 Lou & Liu, supra note 222 at 41.
trump hard law when a court or arbitral tribunal recognizes something as international customary law to preempt the application of attributable domestic hard law (choice of law or conflicts of law).\(^{249}\) Such a dichotomy is also at work in domestic legal systems.\(^{250}\) This is especially true of countries like China with a long history of informal customary law. So, in China’s case just looking at the hard law (CCL, CISG, General Rules, administrative regulations) is not sufficient to truly understand the role of law in Chinese society.

Another way of approaching the topic of the interrelationship between Chinese law and Chinese culture is to view hard law as theory and customary or soft law as praxis. The new modern, Western-style contract laws of China provide the hard rules that are intended to be the basis of contracting and contract dispute resolution. But, at the present time this is more theoretical than real. First, Chinese cultural norms still weigh in favor of mediation, compromise, and relationship preservation than recourse to litigation.\(^{251}\) Second, because of the need for continued growth in the skill level of the Chinese judiciary, especially at the lower court levels, and their lack of familiarity with the Western legal concepts found in the CCL, the rational judicial reasoning in the application of hard rules and principles is sometimes lacking. This leads to a great deal of uncertainty as different courts interpret and apply the same contract rules in different ways.

Third, The Chinese civil law tradition doesn’t aide in the harmonization of law intended by

\(^{249}\) See, e.g., ICC Case No. 5873 of 1989 (CISG, which was not the law of the case was used as evidence of international customary or soft law to preempt the application of Dutch law, which was the law of the case; the panel held that the unusually short statute of limitations—six months—found in Dutch law was contrary to international customary law as represented by the two-year limitation period in Article 39 of the CISG).


\(^{251}\) Confucianism saw resort to litigation or formal arbitration as a disgrace and that parties should mediate their differences in order to maintain social harmony. Cohen, supra note 125 at 1206-07.
the enactment of the CCL since referencing the reasoning of other courts is not a general practice. Fourth, the importance of social roles and networks, the importance of the common good and public interest, and the dominate role played by the Communist Party and state agencies continue to influence or bias the judicial process. In a meaningful way, these norms and cultural tendencies are the soft law of the Chinese legal system or “the law beyond the state.”

In China’s case a better description is to see its cultural norms (Confucianism, guanxi, socialistic-communal-collective ideals) as the law behind the law. Thus, the meaning attached to the hard rules of contract is heavily influenced by this background normative structure, which one scholar has characterized as the “normative richness of life in China.” The application of contract law and its remedies will continue to be influenced by the cultural norms of the common good (most often represented by the plans and policies of the State), fairness, and equity, at the expense of a purely objective application of formal rules.

B. Towards a General Civil Code

This article has emphasized the importance of being aware that words taken or borrowed from Western law by the drafters of Chinese contract law are often applied by Chinese courts in non-conventional manners. The application of vague principles like good faith, fairness, and

---

252 Van der Sluijs, supra note 239 at 1. This idea of the “law beyond the state” has a long history in Chinese Confucian’s view of arbitration and litigation as coerced conclusions of disputes that disrupt social harmony. Thus, the role of informal mediation through negotiation, compromise and third-party persuasion is strongly supported by the Confucian value structure. In this form of mediation legal rules are all but irrelevant.

253 Keller, supra note 171 at 711.

254 See Glenn Morgan and Sigrid Quack, Law as a Governing Institution, in THE OXFORD HANDBOOK OF COMPARATIVE INSTITUTIONAL ANALYSIS 275, 277, 300 (Glenn Morgan, John L. Campbell, Colin Couch, Ove Kaj Pedersen, & Richard Whitley eds. 2010) (observing that the law is influenced by and changes through contextual forces, and also influences that context).
reasonableness will reflect traditional Chinese values. So good faith in application should not be seen as trying to mimic its use in Western law, but as being consistent and coherent with Chinese cultural values. Thus, the law as written and perceived by Westerners and the law as applied immediately diverge when the new law is placed within Chinese cultural and legal traditions.

It is important to realize that the Western perspective of foreign legal systems’ “misuse” of Western legal concepts is at least somewhat a product of bias based upon a line of argument that since the West makes up much of the developed world, as such it necessarily evolved advanced legal systems; since Western laws have been adopted in places like China this is further evidence of its superiority; and therefore, the lack of a proper understanding of Western law and applications of that law in a non-Western way will lead to uncertainty and inefficiency. This is, of course, nonsense! The borrowing of foreign law or legal concepts does not mean that the interpretation and application of those concepts need to be in complete harmony with how they are applied in the country from which they are borrowed. This is because law is never a completely autonomous system since it works within and is influenced by non-legal considerations of historical nuance and cultural diversity. This is not to say that there are no differences between good and bad applications. This has been recognized by the SPC in its issuance of “Interpretations” and Guiding Opinions in order to bring greater certainty and consistency in the application of Chinese contract law among the various levels of the Chinese court system.

However, the consequences of the above divergence between the meaning of legal concepts

255 See Hendrik Zwarensteyn, Some Observations of the Comparison of Legal Institutions and the Concepts of Law in Different Societies, 10 AM. BUS. L.J. 17, 20 (1972) (“the view that our approaches to foreign legal systems . . . are imperceptibly interwoven and inter-connected by our underlying feelings of superiority of our own system(s)”).
256 See supra note 20.
257 See supra note 16.
in the country of transplant and the country from which the law was borrowed are numerous. First, a Western business will need to understand that the Chinese court system may process well-known legal concepts in peculiarly Chinese ways. Second, the Western businessperson should always place the written contract into a relational mindset. What may be a fixed, hard term from a Western perspective, with a clearly defined meaning, may be malleable in the face of Chinese cultural norms. Third, this divergence may recede as the Chinese judiciary becomes better trained and sophisticated in the application of legal reasoning to render more objective decisions. Fourth, at the least, through continued use of SPC “Interpretations,” as well as the full implementation of the *Guiding Opinion* system, it is hoped that divergent opinions in the regional and local courts in the application of similar provisions of the CCL and the future Civil Code will be worked out of the system resulting in greater certainty and consistency in judicial outcomes. Fifth, it is important that the Chinese government continues to improve on its contract law. The Civil Code Project provides an opportunity to craft a third generation contract law that should remain a stable force for decades to come. The CCL’s unification of the different Chinese contract law regimes was a major step forward in the unification and modernization of the law. But, the almost two decades of its existence has shown it to be a flawed instrument with numerous redundancies, inconsistencies, and gaps. It is the hope that the new Civil Code will be a meticulously drafted instrument that will correct the imperfections of the current CCL.

**Conclusion**

The movement to a third generation of modern Chinese contract law has begun with the enactment of the introductory part of what is expected to be a Chinese Civil Code. The 2017
*General Rules of the Civil Law of the People’s Republic of China (General Rules)* provides the framework for a full-fledged Western-style civil code. The focus of this article is on the general principles provided in the CCL and the *General Rules*. The comparison reveals that Chinese longstanding civil law tradition continues to be highly influenced by cultural norms, as espoused in Confucian values, as well as socialistic principles carried over from the era of the Communist planned economy. It is this normative structure and other extralegal influences, such as the dominant roles played by the Communist Party and its policies that differentiate the Chinese view of the rule of law with its Western conception.

These cultural influences play a crucial role in the interpretation and application of Western legal concepts embedded in modern Chinese contract law. Based upon China’s Confucian-Socialistic value structure, which focuses on the value of the collective over the individual and relational structures over formal law, the duty of good faith has become a meta-principle in Chinese jurisprudence. The study of the application of transplanted legal concepts, such as the good faith principle in Chinese law, shows that law in action is always dependent on the interrelationship between the legal, cultural, political, and economic dimensions of society.

It may be that Chinese commercial law, including contract, company, and property laws, will play an outsized role in China if it is to transition to a full-fledged rule of law society. The reasons are three-fold—the importance of recognizing personal rights in the transition to a market economy; private law is relatively unthreatening to the current power structure; and application of private law may serve as a training device to improve the legal reasoning skills of the Chinese judiciary.

Confucian cultural norms have been waning as the Chinese people have increasingly used the court system to resolve contract disputes. The recognition of personal rights to property and
to seek legal redress has increased the role of private autonomy in Chinese society, leading to economic growth by the creation of an entrepreneurial spirit. This has enabled people to move above the “status” upon which they were born into aided by increased mobility from rural to urban centers. The enactment of business and contract laws, along with the recognition of private property, have been the major forces driving China’s rapid economic growth. Thus, it is in the Chinese government’s interest that such laws are efficient and properly applied.

Finally, the improvement in legal reasoning skills in the judiciary—aided by improvements in legal education and guidance offered by the Supreme People’s Court through the issuance of “Interpretations” and Guiding Opinions, has led to more consistency and objectivity in judicial decisions. With these new skill sets, it is likely that the courts will move away from extralegal sources of law and influences to more ‘rule of law’ based decisions in other areas of law including human rights. However, the impact of the judiciary’s improved knowledge of China’s Western-style laws and improved legal reasoning skills on the overall legal system is hampered by the lack of an independent court system. There have been some moves in the direction of greater independence, but for the time being the continued professionalization of the judiciary is the most likely area of improvement. At the same time, it is important to realize that a more independent and objective judiciary is unlikely to change the Chinese concept of the rule of law, which does not assume the eventual creation of a liberal democracy.