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Zhang Yuqing

James S. McLean

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China's Foreign Economic Contract Law: Its Significance and Analysis

*Zhang Yuqing**

*James S. McLean***

I. INTRODUCTION

Postrevolutionary China did not trade with the West prior to the announcement of its "open door policy" in 1977, when one-fifth of the world's population joined the mainstream global trading system. Since then, China's trade has increased dramatically, particularly with the United States. China's need for trade regulation and control resulted in the Foreign Economic Contract Law¹ ("FECL") in 1985. Through an understanding of the FECL's provisions and East-West trade characteristics, the practitioner may become an effective advisor to clients who trade with China or who are considering doing so.

A. Nonmarket Economic Foreign Trade Model

Before China opened its doors, its trading practices were typically those of a socialist state. As expected, international trade with a socialist state (commonly referred to as a nonmarket economy ("NME")) is quite distinct from trade with countries having market economies.² In NMEs,

* Official, Department of Treaties and Law, Ministry of Foreign Economic Relations and Trade ("MOFERT"), Beijing, China. Graduate 1974, University of International Business and Economics (China), LL.M. 1982, University of International Business and Economics (China), LL.M. 1986, Georgetown University Law Center.

The views and opinions in this Article are those of the Author and do not necessarily reflect those of the Chinese government.

** Principal, Johnson, McLean & Riccelli, Spokane, Washington. A.B. 1964, Gonzaga University, J.D. 1975, Gonzaga University, LL.M. 1987, Georgetown University Law Center

¹ Foreign Economic Contract Law [hereinafter FECL], *reprinted in* China L. Foreign Bus. (CCH Austl.) ¶ 5-550 (1987).

² See generally T. HOYA, EAST-WEST TRADE (1984).

the state centrally plans the economy and owns the means of production.³ It establishes foreign trade organizations ("FTOs") to plan and provide general direction to foreign trade. The FTOs are allowed to monopolize part of a country's trade⁴ while maintaining a legal status separate from the state.

A socialist state generally has few FTOs, and they are subject to state planning and price control. Typically, socialist states require application of their law in transactions involving FTOs and further require that disputes be settled in their fora.⁵ The Soviets originated this NME foreign trade model; members of the Council for Mutual Economic Assistance⁶ ("CMEA"), as well as other socialist states, were subsequently influenced by its practices. When Deng Xiaoping introduced the open door policy, China adopted new ways of international trading.

B. Effects of the Open Door Policy

In moving away from the traditional socialist trade model, China has altered dramatically its international trading structure. "Over the last six years, China gradually has set-up an extroverted economic structure encompassing special economic zones, open port cities, coastal economic open zones and enterprises in its interior, pumping new life into the country's economy."⁷ When Deng decided to break from postrevolutionary China's traditional foreign economic trade policies, he brought enormous economic expansion and diversification into China's international economic relations.⁸ Deng's liberalized trade policies encouraged China to "strive for the four modernizations," that is, to attempt to "improve industry, agriculture, defense, and science and technology" simultaneously.⁹

In order for China to modernize, the country had to import necessary products and technology from the industrially developed West, particularly the United States. Thus, China and the United States concluded a trade agreement in 1978 (shortly after the implementation of the open door policy) which granted reciprocal most-favored-nation

³ *Id.* at 11.

⁴ *Id.*

⁵ *Id.* at 289.

⁶ The Council for Mutual Economic Assistance ("CMEA") is sometimes referred to as the Eastern European Common Market. See T. HOYA, *supra* note 2, at 4-5.

⁷ BEIJING REV., Apr. 28, 1986, at 6.

⁸ See Barnett, *Ten Years After Mao*, 65 FOREIGN AFF. 53 (1986).

⁹ Carl, *Contemporary Law in the People's Republic of China*, 32 Sw. L.J. 1255, 1259 (1979).

trading status.¹⁰ In addition, China established trade relations with many other Western trading nations.

China has experienced strong economic growth as a result of its liberalized trade policy. Its 1985 foreign trade totalled a record \$69 billion, representing a 34% increase over 1984.¹¹ As of September 1985, China had attracted \$20 billion in new foreign investments.¹² Data on China's new commercial enterprises are equally impressive: more than 3,210 joint ventures, 4,390 cooperative enterprises, and 138 foreign owned enterprises.¹³ Furthermore, foreign investment has played an important role in the exploration and development of China's own natural resources.¹⁴

By far the most controversial aspect of China's new economic policy has been the expanded role of the marketplace in its domestic economy. This has resulted in the creation of a "socialist commodity economy," the goal of which is a form of market socialism.¹⁵ To this end, China's leaders have modified the NME foreign trade model by expanding the number of enterprises possessing foreign trade contracting authority.¹⁶ Most important, in 1982 China created the Ministry of Foreign and Economic Relations and Trade ("MOFERT") to expedite foreign trade contracts.¹⁷

C. Legal Modernization and Codification

Soon after China's revolution, its leaders implemented a broad legal

¹⁰ See China-United States Agreement on Trade Relations, *reprinted in* 18 INT'L LEGAL MATERIALS 1041 (1979)[hereinafter China-United States Trade Agreement].

¹¹ Communiqué, State Statistical Bureau, PRC, Feb. 28, 1986, *reprinted in* Foreign Broadcast Info. Serv. Daily Rep., Mar. 3, 1986, at K3.

¹² BEIJING REV., Feb. 10, 1986, at 12.

¹³ People's Daily, Jan. 24, 1987, at 1 (int'l Chinese ed.).

¹⁴ See *supra* note 12.

¹⁵ Barnett, *supra* note 8, at 58.

¹⁶ *Id.* at 59. To quote Professor Barnett with reference to the changes which China's economic system is undergoing:

Numerous steps have been taken to increase the decision-making authority of enterprises. Formerly, enterprises operated essentially as subunits of central ministries and equivalent organs at lower levels. The goal is now to give them more autonomy. Experiments in this direction began in the early 1980s. One early step was the introduction of a profit sharing system. Gradually, the percentage of profits that enterprises were allowed to keep—and use for reinvestment, wages and bonus hikes, and other purposes—was increased; since 1984 an entirely new system of taxation of profits has been introduced to replace profit sharing.

Id.

¹⁷ MOFERT has the authority to approve or reject all contracts with foreign entities. See generally Regulations for the Implementation of the Law of the People's Republic of China on Joint Ventures Using Chinese and Foreign Investment [hereinafter Joint Venture Regulations], *reprinted in* China L. Foreign Bus. (CCH Austl.) ¶ 6-550, art. 8 (1987). As an official in the Department of Treaties of MOFERT, Mr. Zhang has direct knowledge of the ministry.

system based on socialism.¹⁸ In contrast, the years immediately preceding China's open door policy—particularly during the Cultural Revolution—were characterized by a retrenchment in its legal development.¹⁹ Since implementing the open door policy, China again has placed a high priority on the codification of its law.²⁰ The Chinese leadership recognized that China's modernization was largely dependent on economic factors: the attraction of foreign investment and the purchase of foreign technology. Thus, China enacted economic, trade, and investment legislation covering economic contracts, trademarks, patents, joint ventures, wholly-owned foreign enterprises, taxation of foreign enterprises, and also promulgated miscellaneous related regulations.²¹ China's FECL is one of the most recent and significant laws in this series. Consequently, China's legal framework is poised to respond to its burgeoning economic sector.

D. China's Current International Economic Policies

China's current five-year plan recognizes the vital role foreign technology plays in China's economic growth. The plan signals the country's intent to use its precious foreign exchange for the purchase of technological imports and machinery.²²

In the five-year period (1986-1990), the total volume of imports and exports will grow at an average annual rate of 7%, reaching US\$83 billion by 1990. Exports will grow at a rate of 8.1% and imports at a rate of 6.1%.

We shall continue to increase exports of petroleum, coal, nonferrous metals, grain, cotton, etc. In addition, we shall gradually increase the proportion of manufactured goods to the total volume of export.

So far as imports are concerned, priority will be given to computer software, advanced technologies and key equipment, as well as certain essential means of production that are in short supply in the domestic

¹⁸ STAFF OF FAR EASTERN LAW DIVISION, LIBRARY OF CONGRESS. HOUSE COMM. ON ENERGY AND COMMERCE, 98TH CONG., 2D SESS., CHINA'S NEW PATENT LAW AND OTHER RECENT LEGAL DEVELOPMENTS (Comm. Print 1984).

¹⁹ *Id.* at 5.

²⁰ An extract from a speech by Ren Jianxin is particularly insightful.

China's long-term strategic policy for accelerating the realization of four modernizations is to exert our efforts with the prerequisite of self-reliance in taking in all merits of foreign countries, developing foreign trade, importing advanced technology, utilizing foreign capital and expanding economic cooperation and technological exchange with foreign countries. In order to insure the implementation of the policy, it has, at present, become a task of prime importance to continuously ameliorate and strengthen our foreign economic and trade law work.

Speech by Ren Jianxin, *reprinted in* S. LENG & S. CHIN, CRIMINAL JUSTICE IN POST-MAO CHINA 37 (1985).

²¹ See generally China L. Foreign Bus. (CCH Austl.) (1987). See also E. THEROUX, LEGAL ASPECTS OF DOING BUSINESS WITH CHINA (1985).

²² The 7th Five-Year Plan of the People's Republic of China for Economic and Social Development, *reprinted in* BEIJING REV., Apr. 28, 1986, at 16-17 [hereinafter 7th Five-Year Plan].

market.²³

To counteract the outflow of China's foreign exchange in the purchase of high technology, China plans on increasing its foreign exchange by resuming its membership in the General Agreement on Tariffs and Trade ("GATT").²⁴ Such a move will also make China's goods more competitive in the global marketplace. China also intends to relax price control regulations in order to permit the laws of supply and demand to operate.²⁵ This policy shift is consistent with China's intention to develop a socialist market system.²⁶

China's decision to allow enterprises to become "relatively independent socialist commodity manufacturers and dealers with full authority for their own management and full responsibility for their own profits and losses"²⁷ has the most bearing on a discussion of the FECL. This policy is a clear departure from the NME foreign trade model discussed earlier. Read in conjunction with the current five-year plan targeting expanded trade with the West, the full significance of the FECL becomes apparent. The law regulates contract approvals and provides a preliminary framework for United States-Chinese contracts involving various types of ventures and transfers. It also articulates China's public policy concerns in contracting with capitalist economies and their corporations.

E. The Ministry on Foreign Economic Relations and Trade

China's policies concerning foreign economic relations and trade matters are implemented by MOFERT, which is also the chief government agency responsible for their functioning. Prior to MOFERT's creation in 1982, the functions were dispersed among four separate agencies. Currently, MOFERT has twenty-one departments and eighteen trading headquarters, covering the broad spectrum of international trade and business. The ministry performs various policy, trade, and regulatory functions. In the policy area, MOFERT is responsible for drawing up plans and strategies on a one- and five-year basis for economic issues such as imports and exports, foreign investments, and aid to developing nations and other foreign countries. It is also responsible for drawing up specific economic and trade policies and principles regarding trade on global, regional, and country levels.

²³ *Id.*

²⁴ General Agreement on Tariffs and Trade, Oct. 30, 1947, 61 Stat. A3, T.I.A.S. No. 1700, 55 U.N.T.S. 187 [hereinafter GATT].

²⁵ 7th Five-Year Plan, *supra* note 22, at 20.

²⁶ *Id.*

²⁷ *Id.*

By authority of the People's Congress and the State Council, MOFERT is responsible for formulating laws and regulations dealing with foreign economic relations and trade. MOFERT has recently developed laws and regulations such as: the FECL; the Joint Venture Law and its implementing rules; China's import and export licensing regulations; interim provisions controlling resident offices in China for foreign enterprises; and regulations on administration of technology acquisition contracts. MOFERT also negotiates trade agreements, investment protection treaties, and international conventions regarding international trade. Furthermore, the ministry oversees the foreign economic and trade activities of the various trade corporations and provincial foreign economic and trade commissions or bureaus.

MOFERT's role in approving joint venture agreements is of special concern to international transactions practitioners doing business with China. The ministry regulates various facets of foreign private investment, international financial organization activity, and in addition approves technology import and export transactions. In sum, MOFERT may be of tremendous value to the international practitioner as a source for new laws and regulations, legal consulting, and the categorization and approval of contracts negotiated under the auspices of the FECL.

II. INTRODUCTION TO THE FECL

A. Background

Unlike Chinese domestic contract law,²⁸ the FECL only governs contracts concluded between Chinese corporations or enterprises and foreign companies or individuals, provided that Chinese law applies to such contracts.²⁹ Except for international transportation contracts, all other international economic or commercial contracts will generally be governed by the FECL. Joint ventures (including the exploration and development of natural resources), the sale of goods, insurance, processing and assembling arrangements, and compensation trade are within the FECL's scope. It also extends to other contracts including leasing, coproduction, technology transfer, licensing, engineering projects, provision of credits, consignment sales, agency cooperative research, and storage.

The FECL's purpose is to "protect the lawful rights and interests of

²⁸ Economic Contract Law, *reprinted in* China L. Foreign Bus. (CCH Austl.) ¶ 5-550 (1987). This law exclusively governs contracts concluded between domestic enterprises, individuals or enterprises, and other individuals.

²⁹ The FECL may also govern contracts concluded between foreign companies if the parties decided to apply the FECL or the law applies because of private international law rules.

the concerned parties to foreign economic contracts and promote the development of China's foreign economic relations."³⁰ Moreover, the FECL is the legal vehicle which consolidates the Chinese government's open door policy.³¹ The FECL's fundamental principles and objectives, as well as grounds for its promulgation, are found in the provisions of two documents. First, the preamble of China's 1982 constitution states:

The future of China is closely linked with that of the whole world. China adheres to an independent foreign policy as well as to the five principles of mutual respect for sovereignty and territorial integrity, mutual nonaggression, noninterference in each others' internal affairs, equality and mutual benefit, and peaceful coexistence in developing diplomatic relations and economic and culture exchanges with other countries. . . .³²

Second, Article 55 of the Economic Contract Law stipulates that: "Regulations on the signing of economic contracts for international trade will be worked out separately in reference to the principles of this Law by international practices."³³ Thus, the FECL encompasses basic constitutional and legal goals of the Chinese government.

B. Guiding Principles

Four principles provide the actual basis for the FECL: equality and mutual benefit; the primacy of international treaties to which China is a party; honoring the contract and maintaining good faith in business activities; and national laws and regulations protect national sovereignty and social welfare. The first principle, that of equality and mutual benefit, has been instrumental in promoting and developing China's foreign economic relations. It is also observed by Chinese economic entities in their international economic activities. Thus, it is not surprising to find this principle incorporated in Article 3 of the FECL: "contracts should be made in conformity with the principles of equality and mutual benefit, and of achieving unanimity through consultations."³⁴ The first component of the principle—equality—requires that parties, regardless of their size and strength, should be on an equal footing in negotiating their contract.³⁵ The contractual agreement should reflect the parties' interests,

³⁰ FECL art. 1.

³¹ Some of the functions of the Chinese economic law are to: pursue China's open door policy; attract foreign investment; promote technology import; expand international economic and technological cooperation; and expand international trade. See Gu Ming, *Economic Legislation and Socialist Modernization Construction*, 12 HONG QI 17 (1985).

³² Preamble of 1982 Constitution of the People's Republic of China.

³³ Economic Contract Law art. 55.

³⁴ FECL art. 3.

³⁵ See WANG TIEYA, *INTERNATIONAL LAW 76-78* (1981)(Chinese ed.).

needs, and understanding of contract terms.³⁶ No party has the right to use its economic power to impose or force the other party to accept unfair or unreasonable conditions.³⁷ The second component of the principle—mutual benefit—means that the interests of both parties to a contract should be reasonably considered and realized, so that a party enjoys benefits only after fulfilling its obligations under the contract.³⁸ Under Chinese commercial practice, the concepts of equality and mutual benefit are so closely linked that there is to be no mutual benefits unless the parties are on an equal footing.

The acceptance of this principle by most of the nations of the world is evidenced by its incorporation in the preamble to the United Nations Convention on Contracts for the International Sale of Goods. Pursuant to a suggestion by the Chinese delegation, the preamble states that: “[t]he development of international trade on the basis of equality and mutual benefit is an important element in promoting friendly relations among States.”³⁹ Thus, the principle of equality and mutual benefit is consistent with international commercial practice.

A second major principle incorporated in the FECL is the primacy of international treaties to which China is a party, influenced by China's open door policy and its desire to further its economic contacts with foreign countries. In recent years China has participated in the discussion and conclusion of various international treaties and conventions,⁴⁰ which greatly influenced the drafting of the FECL. (For example, many of the Vienna Sales Convention provisions have been incorporated in the

³⁶ *Id.*

³⁷ *Id.*

³⁸ *Id.*

³⁹ United Nations Convention on Contracts of the International Sale of Goods, ST/LEG/SER.E/4/Add. 1, reprinted in 19 INT'L LEGAL MATERIALS 668 (concluded at Vienna on Apr. 11, 1980)[hereinafter UNCITRAL]. An interesting question arises in comparing Article 3 of the FECL with the preamble of the 1980 Vienna Sales Convention. The principle of equality and mutual benefit used in the FECL refers only to the conclusion of contracts. The principle embodied in the Sales Convention, however, seems to have a broader meaning. Some Chinese legal experts believe that the parties should abide by this broader principle throughout the contract. “All the above-mentioned provisions (including Article 3) guarantee that the concerned parties can make and carry out contracts on the basis of equality and mutual benefits.” *MOFERT Official's Answer to Questions on Foreign Economic Contract Law*, China Econ. News, July 8, 1985, at 2 (emphasis added). Thus, the scope of this article requires clarification.

⁴⁰ China participated in the diplomatic conference leading up to the final drafting of UNCITRAL in 1980. See *supra* note 39, at 47. Now China is a member state of UNCITRAL. See Report of the United Nations Commission on International Trade Law on the Work of its 18th Session, 40 U.N. GAOR Supp. (No. 17) at 2-3, U.N. Doc. A/40/17 (1985). China is also a member state of the International Institute for the Unification of Private Law (“UNIDROIT”). Since 1983, China has participated in meetings and conferences held by the Hague Conference on Private International Law. Concerning China's Bilateral Investment Treaty program, see *supra* note 22, at 573.

FECL.⁴¹) It is evident that the drafters intended the FECL to be consistent with international commercial practice. Consequently, Article 6 of the FECL may be used by foreign parties to safeguard their rights and interests since they may invoke provisions of international treaties if they find those provisions more favorable.⁴²

When an international treaty that relates to a contract and which the People's Republic of China has concluded or participated in has provision(s) that differ from the law of the People's Republic of China, the provision(s) of the said treaty shall be applied, but with the exception of clauses to which the People's Republic of China has declared reservation.⁴³

In order for treaty law to take precedent over domestic Chinese law, the following conditions must be met, as deduced from the FECL: 1) the provisions of the treaty must relate to the particular issue or issues resulting from the relevant contract; 2) a conflict must exist between the provisions of the treaty and Chinese domestic law; 3) China is a party to the treaty; and 4) China has not declared reservations under the treaty provisions invoked by one party.

China's Civil Procedure Law, Article 189, similarly provides: "[w]hen an international treaty which the People's Republic has concluded or participated in has different stipulations, the provisions in that international treaty are applicable except for those provisions on which our country has stated its reservations."⁴⁴ The inclusion of such provisions in Chinese domestic laws shows that the government respects international law regarding international business transactions, and defers to it when a discrepancy occurs between domestic and international law.⁴⁵

The FECL's third principle requires that the contract be honored and that good faith be maintained in business activities. These linked concepts require that Chinese corporations consciously consider whether they are capable of performing the contractual obligations before signing it. It is customary in China that, once a contract is signed, it should be

⁴¹ China, the United States, and Italy have deposited their instruments of ratification with the United Nations. Consequently, the convention will take effect on Jan. 1, 1988, between China, the United States, and nine other ratifying states. Gabor, *Emerging Unification of Conflict of Laws Rules Applicable to the International Sale of Goods: UNCITRAL and the New Hague Conference on Private International Law*, 7 NW. J. INT'L L. & BUS. 696, 700 (1986).

⁴² FECL art. 6.

⁴³ *Id.*

⁴⁴ *China's Civil Procedure*, British Broadcasting Corp.; Summary of World Broadcasts, Mar. 17, 1982, at FE/6980/C/1 (NEXIS library, BBCSWB file).

⁴⁵ Such order of precedence has not been clearly established by the Chinese Constitution. The Chinese Constitution, art. 5, § 2, states: "No law or administrative or local rules and regulation shall contravene the Constitution." China L. Foreign Bus. (CCH Austl.) ¶ 5-311 (1987). See also Gelatt and Kraiem, *The Foreign Economic Contract Law, More Autonomy for Contracting Parties*, E. ASIAN EXEC. REP., May 9, 1985, at 9.

performed exactly and fully according to its terms, except for events of *force majeure*.⁴⁶ Parties are not to take advantage of market changes to breach a contract intentionally. These principles of Chinese commercial practice are firmly embedded in the FECL.⁴⁷

The fourth and last FECL principle underscores that national laws and regulations are to protect national sovereignty and social welfare. One of the tasks of China's foreign trade laws is to serve the country's economic construction and to promote China's four modernizations. It is of paramount importance for China to keep its foreign economic activities in line with these goals. Consequently, it is not surprising that several articles of the FECL are designed to preserve China's sovereignty and social interest.⁴⁸ For example, contracts may be invalidated on public policy grounds.⁴⁹ In addition, the FECL provides that certain contracts be approved by the government.⁵⁰ This approval guards against Chinese enterprises entering into contracts that would contravene Chinese sovereignty or public policy. Consequently, Western lawyers and business executives must be aware that the contracts may be invalidated for public policy reasons.

C. Structure of the FECL

The FECL has seven chapters containing forty-three articles which are fairly concise and easy to understand. Moreover, the provisions are quite flexible, leaving to the parties their creative abilities to form or fashion contracts to fit the transactions.⁵¹ Chapter 1 deals with the general provisions of the FECL, defining the scope, public policy considerations, applicable legal provisions, and the primacy of international law.⁵² Chapter 2 deals with contract formation and imposes certain formal requirements. For example, the law requires that a contract be in writing and be signed. Government approval requirements are also defined. Additional public policy considerations, defenses to contract formation, and suggestions as to what a contract should include are also discussed.⁵³

Performance and remedy considerations are covered in Chapter 3.

⁴⁶ See *infra* notes 108-13 and accompanying text.

⁴⁷ See *infra* notes 97-121 and accompanying text.

⁴⁸ See *infra* notes 70-78 and accompanying text.

⁴⁹ See *infra* notes 70-73 and accompanying text.

⁵⁰ See *infra* notes 79-86 and accompanying text.

⁵¹ See FECL art. 12. Also note the persistent use of the word "should" throughout the law in contrast to the command "shall" found in China's domestic Economic Contract Law and the United States Uniform Commercial Code and common law.

⁵² FECL arts. 1-6.

⁵³ FECL arts. 7-15.

This chapter covers nonperformance, breach, liquidated damages, mitigation and *force majeure*. This chapter represents the core of the FECL, dealing with parties' rights and remedies with regard to performance disputes.⁵⁴ Chapter 4 concerns the assignment of contract questions. Although it is quite brief, this chapter involves important considerations for international practitioners dealing with Chinese enterprises.

Chapter 5, entitled "Modification, Cancellation, and Termination of Contract," delineates performance considerations and reflects Chinese business practices, both domestic and foreign. It addresses procedures which are to be followed when a party modifies, cancels, or terminates a contract.⁵⁵ Chapter 6 concerns dispute settlements, reflecting the Chinese custom of avoiding litigation and settling disputes through amicable consultations or mediation. Arbitration is always favored and litigation considered the avenue of last resort.⁵⁶ Chapter 7 encompasses various housekeeping provisions and includes a statute of limitations, change of law considerations during the course of a contract, and force and effect provisions.⁵⁷

D. Translation and Language Problems

It is important to note that several English translations of the FECL are in circulation in the United States,⁵⁸ and that they are substantially different in their use of the words "shall" and "should." Consequently, these different translations create confusion as to whether compliance with a specific provision is mandatory, because the Chinese version is unclear in its meaning and intent. Thus, the international transactions practitioner must exert caution in drafting contracts which would comply with the FECL. Resorting to other Chinese laws and regulations may be necessary to understand correctly whether a specific provision is mandatory.⁵⁹

Prior to the enactment of the FECL, there was confusion as to the legal effect of foreign language in contracts with Chinese parties.⁶⁰ For example, regulations applicable to contracts performed in the Shenzhen

⁵⁴ FECL arts. 16-25.

⁵⁵ FECL arts. 28-36.

⁵⁶ FECL arts. 37-38.

⁵⁷ FECL arts. 39-43.

⁵⁸ See *supra* note 1. (The version employed by the Authors appears in the official MOFERT version.) For example, see translation by the United States government, Foreign Broadcast Information Service, 1 Daily Report: China, Mar. 25, 1985, at K12 [hereinafter FBIS Translation]; translation by Paul, Weiss, Rifkind, Wharton & Garrison, in CHINA BUS. REV., July-Aug. 1985, at 54.

⁵⁹ See *infra* note 117 and accompanying text.

⁶⁰ Cohen, *The New Foreign Contract Law*, CHINA BUS. REV., July-Aug. 1985, at 52-53.

Special Economic Zone provide for the superiority of the Chinese language version.⁶¹ The FECL attempts to soften such provisions by allowing for the parties to agree on the language used and its effect.⁶² Once again, the practitioner should exercise caution in drafting agreements with Chinese business executives in order to avoid possible future ambiguities.

III. CONTRACT FORMATION UNDER THE FECL

A. Entering into Contracts

The FECL⁶³ expressly applies to contracts concluded between foreign parties and "enterprises or other economic organizations" of China.⁶⁴ Thus, Chinese individuals are expressly excluded from FECL coverage and from foreign trade contracts in general. In contrast, the term "foreign parties" does include individuals.⁶⁵

With the decentralization of China's economic system, Chinese enterprises have been given a new and expanded role while the central government has given enterprises increased contracting authority and autonomy.⁶⁶ Nonetheless, a Chinese enterprise's charter, Chinese law, and regulations limit the types of contracts it may negotiate and sign. Consequently, international business executives must pay close attention to the authority of the enterprise with which they are dealing, including the authority of the individual to represent the enterprise.⁶⁷ If the contract is entered into without the requisite authority, then Chinese contract law would invalidate it.⁶⁸ Further, Chinese practice dictates that

⁶¹ *Id.*

⁶² FECL art. 12.

⁶³ Chapter 2 omits detailed legal procedures for contract formation. It is intended that more detailed coverage of contract law will be provided by the Chinese Civil Code which will supplement domestic Economic Contract Law. At the time of this publication, the civil code portion of the Chinese contract law was not available although the General Principles of the Civil Code were promulgated by the 4th Session of the 6th National People's Congress on April 12, 1986.

⁶⁴ FECL art. 2.

⁶⁵ *Id.*

⁶⁶ *See supra* notes 25-27 and accompanying text.

⁶⁷ To clarify this matter, foreigners may ask the Chinese party to show relevant certificates, documents, or powers of attorney, and relevant enterprise charters or related documents. For joint ventures, almost all Chinese economic entities (except individual proprietorships) have the right to conclude such contracts. Nonetheless, each joint venture contract is subject to approval by the Chinese provincial or central government. After a joint venture has been approved and the joint venture established, it has a right, under Chinese law, to export its products and import raw materials and equipment necessary for production. *See, supra* note 17, Joint Venture Regulations at ¶ 6-551.

⁶⁸ *See also* FECL art. 9 and Economic Contract Law art. 7. It must be emphasized that China is a planned economy. Although great changes have taken place during the last several years in China's foreign economic relations, the country's foreign trade and other forms of economic cooper-

the central or provincial government does not involve itself with enterprise transactions.⁶⁹ Thus, in the event of a breach of contract, the foreign party will have to look to the Chinese enterprise for damages, not the government.

B. Contract Invalidity

Besides the contract invalidation consideration cited in the preceding section, the FECL will also invalidate foreign economic contracts if they: violate Chinese law;⁷⁰ are contrary to the public interest of Chinese society;⁷¹ or are concluded by means of fraud or duress.⁷² Under the general provisions of the FECL, contracts must be made "in accordance with the law of the People's Republic of China and without prejudice to the public interest of the People's Republic of China."⁷³ Thus, international business transactions are to be concluded in accordance with Chinese law and public policy. While the concept of public policy is not new to Western practitioners, it presents additional problems and difficulties in contracting when the foreign party is from a socialist legal system, especially since China has endured a long history of exploitation by the West.

The greatest problem in applying the FECL to contract invalidity situations is that its application is inherently intertwined with choice of law problems. Regardless of which country's law is chosen for the transaction, it must also be decided whether Chinese law and public policy will determine the contract's validity. Article 5 of the FECL provides that the parties may select the law "to be applied to the settlement of disputes arising from the contract."⁷⁴ Nonetheless, it is reasonable to assume that the Chinese party will take the position that Chinese law will control the validity of the transaction, especially if arbitration or litiga-

ation with foreign countries are still controlled by the Chinese government. *But see Peking Expands Scope of Central Planning as Hardliners Lead a Retreat from Reform*, Asian Wall St. J., Feb. 23, 1987, at 1. Many new corporations and enterprises have been established for international business purposes and, in China, foreign trade corporations can handle their business independently. It is impossible to tell exactly how many Chinese economic corporations or enterprises are now doing business with foreign companies. Following the process of continued decentralization of China's economy, more independent Chinese juridical entities may enter into business agreements with foreigners. This development creates problems for foreign businesses in that they must be certain that the Chinese party has the capacity and authority to conclude the contract.

⁶⁹ No private party has the right to sign trade contracts in the name of or on behalf of the Chinese government.

⁷⁰ FECL art. 9.

⁷¹ *Id.*

⁷² *Id.* art. 10.

⁷³ *Id.* art. 4.

⁷⁴ *Id.* art. 5.

tion occurs in China or before a Chinese tribunal. Indeed, even the trade agreement between the United States and China providing for the enforceability of arbitration awards conditions such enforcement on being "in accordance with applicable laws and regulations."⁷⁵

As contract validity in China under its new economic laws and regulations is yet unclear, and the application of such rules and policies to foreign economic contracts is still in the early stages of development, it is premature to predict Chinese practice. Furthermore, it is important to note that the FECL includes certain relief provisions for foreign parties caught up in the intricacies and ambiguities of a developing legal system. For example, Article 9 provides for the cancellation or revision of contract provisions that would invalidate a contract under Chinese law.⁷⁶ Furthermore, the FECL provides for the payment of the loss sustained to the innocent party by the party who "bears responsibility for the invalidity of the contract."⁷⁷ Thus, if the Chinese party is responsible (because, for example, it lacked contracting authority or failed to demand that conditions or provisions which violate Chinese law be deleted), the foreign party could not necessarily enforce the contract or seek contract damages, but it could seek compensation for losses sustained, pursuant to Article 11.⁷⁸

C. Government Approval of Foreign Economic Contracts

The FECL requires governmental approval of certain types of contracts.⁷⁹ Presumably its position will be that failure to obtain the requisite prior approval will invalidate the contract, regardless of what law applies. Since the FECL does not list all types of contracts requiring government approval, resort to other Chinese laws and regulations may be necessary. As China has a socialist economic system, and all centrally planned economies provide for substantial economic planning and enterprise control, it is essential for the international transactions practitioners to recognize this fact in order to transact business successfully with Chinese enterprises.⁸⁰

While not every contract between a foreign and Chinese party requires government approval, those which do are numerous, particularly so for those contracts which are part of China's modernization program

⁷⁵ See China-United States Trade Agreement, *supra* note 10, at 1050.

⁷⁶ FECL art. 9.

⁷⁷ *Id.* art. 11.

⁷⁸ *Id.*

⁷⁹ *Id.* art. 7, ¶ 2.

⁸⁰ See *supra* notes 2-6 and accompanying text.

to import technology and engage in joint ventures. Contracts currently subject to Chinese governmental approval include joint venture contracts, which require approval from either a provincial or central government (through the Ministry of Foreign Economic Relations and Trade) depending upon the amount of capital involved.⁸¹ Other contracts requiring prior review include technology import contracts,⁸² joint management contracts,⁸³ and contracts for joint exploration and development of natural resources.⁸⁴

Contracts for the sale of goods do not require governmental approval. If such contracts involve foreign technology or know-how, however, they become subject to approval by Chinese authorities.⁸⁵ Consequently, many contracts face some sort of approval requirement. In order to avoid breaching this requirement by a foreign or Chinese party, the foreign business executive or counsel must seek competent legal advice. The timing of this advice would occur both at the negotiation stage and prior to the conclusion of the agreement. (MOFERT would be the appropriate agency when negotiation had ended).

There are many contractual provisions which are explicitly prohibited under Chinese law. Joint venture contracts containing the following provisions will not be approved: 1) those detrimental to China's sovereignty; 2) those which violate Chinese law; 3) those not conforming to development requirements of China's national economy; 4) those contrary to environmental pollution standards; and 5) those which are inequitable because they impair the rights and interests of one of the parties.⁸⁶ There are also provisions of technology import contracts which are explicitly prohibited, including provisions which: 1) require the recipient to purchase unnecessary technology, tactical services, raw materials, equipment, and products; 2) restrict the recipient's freedom of choice to obtain materials and services from other sources; 3) restrict the recipient from developing and improving imported technology; 4) restrict the recipient from obtaining competing technology from other sources; 5) include nonreciprocal terms of exchange for the improvement of the imported technology; 6) restrict quantity, variety, and sales price; 7) unreasonably restrict sales channels and export markets; 8) restrict the use

⁸¹ Law on Joint Ventures Using Chinese and Foreign Investment [hereinafter Joint Venture Law], art. 3, *reprinted in* China L. Foreign Bus. (CCH Austl.) ¶ 7-801 (1987).

⁸² Regulations on Administration of Technology Import Contracts [hereinafter Technology Import Regulations], art. 4, *reprinted in* China L. Foreign Bus. (CCH Austl.) ¶ 6-685 (1987).

⁸³ China Econ. News, July 15, 1985.

⁸⁴ *Id.*

⁸⁵ Technology Import Regulations, art. 4.

⁸⁶ Joint Venture Regulations, art. 5.

of imported technology after expiration of the contracts; and 9) require the recipient to pay or undertake obligations for patents which are unused or no longer effective.⁸⁷

As noted previously,⁸⁸ a great number of joint ventures are already operating in China, indicating the central government rarely disapproves joint ventures. Furthermore, given China's policy supporting the import of technology, it appears unlikely that such agreements will not be approved in the future, providing that they meet the guidelines set forth above.

D. Formal Requirements and Recommended Clauses

The FECL requires a written agreement signed by the parties as a condition to contract formation.⁸⁹ In the event that a confirmation letter is also requested, the contract is not formed until the "confirmation letter is signed."⁹⁰ While these requirements appear to be somewhat more rigid than those in Western legal systems, most international transactions involve substantial documentation. Indeed, the international sale of goods is referred to as the "documentary sale,"⁹¹ and such writing requirements are consistent with practice in the Soviet Union and other Eastern European countries.⁹² This writing requirement contrasts with the more flexible international practice reflected in the 1980 Vienna Sales Convention which expressly negates the requirement of a writing.⁹³

The FECL also recommends including certain terms and clauses in the contract, but since it consistently uses "should" instead of "shall,"

⁸⁷ Technology Import Regulations, art. 9.

⁸⁸ See *supra* notes 12-14 and accompanying text.

⁸⁹ FECL art. 7.

⁹⁰ *Id.*

⁹¹ R. FOLSOM, W. GORDON & J. SPANOGLE, *INTERNATIONAL BUSINESS TRANSACTIONS*, ch. 4 (1986).

⁹² Most NMEs have followed the same pattern in concluding their international contracts. Some set forth even more rigid rules. According to Soviet law on foreign trade transactions, such transactions are generally signed by two persons, the director and deputy director, who have power of attorney. 2 W. BUTLER, *COLLECTED LEGISLATION OF THE USSR AND CONSTITUENT UNION REPUBLICS* 3 (1980). The Czechoslovakian International Trade Code § 24 has a similar requirement. 17 BULL. CZECHOSLOVAK L. 52 (1978).

Chinese enterprises use a substantial array of form contracts in practice. Even smaller enterprises have access to purchase orders with standard clauses, many of which are consistent with international practice. Consequently, there generally will be a written document or evidence of the transaction. The foreign party should be aware, however, that the Chinese party will probably want to use the Chinese form contracts. For a discussion of form contracts and clauses in United States-China trade, see Mitchell & Stein, *U.S.-China Commercial Contracts*, 20 INT'L LAW. 987-20 (1986).

⁹³ J. HONNOLD, *UNIFORM LAW FOR INTERNATIONAL SALES UNDER THE 1980 UNITED NATIONS CONVENTION* 472 (1982).

the law makes the recommendation instructive rather than mandatory.⁹⁴ Most contract terms and provisions will be obvious to foreign parties, but may be overlooked by the Chinese party; consequently, the inclusion of these terms is important. For example, the provisions for risks, insurance coverage, length of validity, and even *force majeure* appear to be present primarily for the benefit of the Chinese party and the Chinese enterprise.⁹⁵ The foreign party should also be aware of the operation of other laws, in the event that the contract is one of joint venture or technology importation. In such cases additional laws and regulations provide for the inclusion of other terms and conditions which must be specified.⁹⁶

IV. PERFORMANCE, BREACH, AND REMEDIES

A. Performance and Breach

Once a contract has been legally formed under the FECL, the law provides that it is "legally binding."⁹⁷ While the language used in the opening article of Chapter 3 of the FECL (MOFERT version) includes the word "should," the unofficial English language version is different; it appears that the drafters intended that full performance would be mandatory. The practice in China and in other socialist legal systems is that actual performance is required and is to be preferred over damages.⁹⁸ So even though the language in Article 16 appears to be consistent with Western law; nonetheless its intent is very different. Under United States law, full performance would not be mandatory, since the parties would have the choice of damages in lieu of performance.⁹⁹

B. Excuse of Performance

Consistent with United States common law and the Uniform Commercial Code ("UCC"), the FECL provides for the suspension of performance in anticipation of another party's breach—the doctrine of anticipatory breach or repudiation.¹⁰⁰ The party suspending performance without a proper basis must notify the other party¹⁰¹ and is liable

⁹⁴ FECL arts. 12-14. *But see* FBIS Translation, *supra* 58 which consistently uses the word "shall."

⁹⁵ FECL arts. 12-14.

⁹⁶ *See generally* Technology Import Regulations and Joint Venture Law.

⁹⁷ FECL art. 16.

⁹⁸ *See* T. HOYA, *supra* note 2, at 196-220.

⁹⁹ 11 WILLISTON ON CONTRACTS § 1418 (3d ed. 1968).

¹⁰⁰ FECL art.17.

¹⁰¹ *Id.*

for damages for breach of contract.¹⁰²

The FECL defines breach of contract simply as a situation in which the "performance of the contractual obligations does not conform to the agreed condition. . . ."¹⁰³ The concept of a general breach of contract is consistent with Western law and is uncomplicated by such doctrines as substantial performance. On the other hand, the FECL does identify a kind of breach that might appear to be unusual to a Western party. Article 21 states: "[i]n a case where both parties are in breach of the contract, each shall bear the corresponding liabilities respectively."¹⁰⁴ From this provision it is apparent that the Chinese drafters of the FECL envisioned what may be referred to as the doctrine of simultaneous breach. Contract law in the United States does not recognize such an occurrence.¹⁰⁵ Rather, it recognizes an order of performance, thus eliminating the possibility of mutual or simultaneous breach.¹⁰⁶ This concept of mutual or simultaneous breach is consistent with the Chinese view of dispute settlement. Characterized by the phrase "dividing one into two," the Chinese view a dispute from each party's perspective.¹⁰⁷ Thus, a foreign litigant and its counsel should be prepared to argue such concepts before a Chinese tribunal if disputes arise in transactions with Chinese enterprises.

Consistent with international practice and Western common law, contract performance under the FECL may be excused under circumstances of *force majeure*.

In case a party cannot perform his obligations within the time limit set in the contract due to a *force majeure* event, he should be relieved from the liability for delayed performance during the period of continued influence of the effects of the event. An event of *force majeure* means the event that the parties could not foresee at the time of conclusion of the contract and its occurrence and consequences cannot be avoided and cannot be overcome.¹⁰⁸

Consistent with the bias toward full performance, the Chinese view

¹⁰² *Id.*

¹⁰³ *Id.* art. 18.

¹⁰⁴ *Id.* art. 21.

¹⁰⁵ 6 WILLISTON, *supra* note 99, at § 832. Williston comments that, even in concurrent conditions, it is possible for each party to have a right of damages for breach of contract. *Id.*

¹⁰⁶ *Id.* § 829.

¹⁰⁷ Chew-LaFitte, *The Resolution of Transnational Disputes in the People's Republic of China: A Guide for U.S. Practitioners*, 8 YALE J. WORLD PUB. ORD. 236, 253 (1982).

¹⁰⁸ FECL art. 24. Article 24 of FECL is worded similarly to an article in UNCITRAL providing that:

A party is not liable for failure to perform any of his obligations if he proves that the failure was due to an impediment beyond his control and that he could not reasonably be expected to have taken the impediment into account at the time of the conclusion of the contract or to have avoided or overcome its consequences.

See J. HONNOLD, *supra* note 92, at 495.

of *force majeure* is rather strict, and is consistent with Soviet and CMEA practice as shown in the latter organization's General Conditions:

[A party] shall be relieved of liability for. . . nonperformance of obligations under a contract if such nonperformance was the consequence of circumstances. . . that arose after conclusion of the contract as a result of events of an extraordinary character that were unforeseen and unavoidable by the party.¹⁰⁹

Past practices of both the Chinese and CMEA interpret *force majeure* as some form of unforeseen natural disaster.¹¹⁰ The United States position is far more flexible, as seen in the doctrine of impracticability under the UCC.¹¹¹ Consistent with China's expansion of international trade and its modernization, China is also beginning to liberalize its view of *force majeure* events.¹¹²

It should be noted that liberalizing the Chinese interpretation of *force majeure* along the lines of the UCC could work in favor of the non-Chinese party. Although China's economic system is undergoing substantial change, including decentralization, its economy is still subject to substantial control and regulation by the central government. Under the liberal provisions of the UCC, either party to a contract could seek an excuse for nonperformance if it occurred by reason of "compliance in good faith with any applicable foreign or domestic governmental regulation or order. . . ." ¹¹³

C. Remedies

Consistent with the commercial practices of other NMEs, Chinese law before 1977 emphasized full performance as the norm in contracting situations. Under the CMEA General Conditions, for example, a buyer

¹⁰⁹ T. HOYA, *supra* note 2, at 223.

¹¹⁰ *Id.* at 235.

¹¹¹ A. ANDERSON, ANDERSON ON THE UNIFORM COMMERCIAL CODE, § 2-615:28 (1983). Anderson observes that the impracticability standard is less stringent than the common law requirement of impossibility. *Id.* at 283.

¹¹² Generally, natural disasters were recognized by Chinese trade corporations as a *force majeure* event. Some events which involve human elements, however, such as wars or strikes, were at one time difficult for Chinese trade corporations to treat as *force majeure*. Recently, more realistic and practical attitudes toward these issues have been adopted by Chinese corporations.

¹¹³ See *supra* note 111. Certain acts of state—withdrawal of import or export licensing, changing economic plans, and government decrees—may sometimes cause foreign business executives to have misgivings. They may worry that the Chinese party will take advantage of Chinese government acts to escape contractual obligations. This concern contrasts with the policy expressed in Chapter 33 of China's new 7th Five-Year Plan: "We must expand trade ties with all other countries and regions and make active efforts to open up new markets. We must faithfully observe contracts and deliver commodities on time, so as to maintain a good reputation in the world market." See *supra* note 21, at 17.

may demand specific performance on the part of the seller.¹¹⁴ Under this view:

[T]he purpose of a contract is the satisfaction of real, i.e. genuine needs: buyers's interest is attached to the delivery of goods specified by the contract. Notwithstanding in any disturbance interfering with the performance, the parties have to adhere to real, actual performance, for which no substitute, no "ersatz", such as cash or damages will do.¹¹⁵

In contrast to this earlier practice, the FECL does not include a provision for specific performance as a remedy. Rather, Chapter 3 makes reference to losses or damages on numerous occasions.¹¹⁶ Thus, it is reasonable to assume that the FECL is intended to conform to Western common law and international practice.

The damages and liquidated damages provisions of the FECL should be familiar to Western international transactions practitioners because such concepts as foreseeability¹¹⁷ and mitigation¹¹⁸ are covered. Moreover, the use of a penalty in conjunction with liquidated damages provisions is addressed.¹¹⁹ Nonetheless, there are minor and technical differences in this area. As noted earlier, the concept of simultaneous breach is foreign to Western practitioners.¹²⁰ Moreover, the mitigation requirement in Article 22 is more severe than, for example, the UCC optional cover provision in the sale of goods.¹²¹

V. ASSIGNMENT, CANCELLATION, AND TERMINATION

In contrast to United States common law providing for free assignability of contracts, the FECL provides that, prior to assignment, "consent should be obtained from the other party."¹²² Whether the FECL mandates such consent is unclear from the unofficial English translation; resort to other laws or regulations is necessary. For example, China's joint venture regulations make it clear that the assignment of joint venture contracts requires Chinese government approval.¹²³

The FECL further provides that a party is entitled to inform the other party of what is, in effect, unilateral cancellation of the contract by

¹¹⁴ T. HOYA, *supra* note 2, at 193.

¹¹⁵ I. SZÁSZ, *THE CMEA UNIFORM LAW FOR INTERNATIONAL SALES* 167 (2d ed. 1984).

¹¹⁶ *See* FECL arts. 18-22.

¹¹⁷ *Id.* art. 19.

¹¹⁸ *Id.* art. 22.

¹¹⁹ *Id.* art. 20.

¹²⁰ *Id.* art. 21. *See supra* note 104 and accompanying text.

¹²¹ *Id.* art. 22. *See also* U.C.C. § 2-712.

¹²² FECL art. 26.

¹²³ Joint Venture Regulations, art. 23.

reason of breach,¹²⁴ *force majeure*,¹²⁵ or the occurrence of the condition subsequent.¹²⁶ Cancellation notices are to be in writing.¹²⁷ English and United States common law appear to have no counterpart to such unilateral cancellation and notification provisions. These stipulations, however, appear to be consistent with the Chinese practice of informal dispute resolution without resort to third party adjudication.¹²⁸

The FECL provides for the standard discharge of contractual obligation provisions consistent with United States common law.¹²⁹ It also preserves a party's right to damages in the event of cancellation or termination.¹³⁰ Additionally, the law provides for the severability of contracts¹³¹ and ensures that settlement of dispute clauses will survive in the event of cancellation or termination.¹³²

VI. CHOICE OF LAW PROVISIONS AND DISPUTE SETTLEMENT

Before the open door policy, it was Chinese practice in international commercial transactions to exclude any choice of law provision.¹³³ In recent years, arbitration in a neutral third country (such as Sweden) was an alternative to excluding such a provision.¹³⁴ It was presumed, perhaps, that the neutral country arbitrator would apply applicable choice of law rules in selecting the applicable law.¹³⁵ The Chinese have expressed a justifiable reluctance to apply Western law to commercial transactions in China, given their history of exploitation by the West. Such hesitancy generally reflects the practice of the Soviet Union and CMEA nations.¹³⁶

Given past Chinese practices, the FECL makes a major concession for the foreign party in choice of law rules. Article 5 provides for party autonomy in selecting the law to govern the contract. The same article applies the law in the country with the most significant contacts,¹³⁷ a

¹²⁴ FECL art. 29(1-2).

¹²⁵ *Id.* art. 29(3).

¹²⁶ *Id.* art. 29(4).

¹²⁷ *Id.* art. 32.

¹²⁸ *Id.* art. 37.

¹²⁹ *Id.* art. 31.

¹³⁰ *Id.* art. 34.

¹³¹ *Id.* art. 30.

¹³² *Id.* art. 35.

¹³³ See Note, *An Analysis of Chinese Contractual Policy and Practice*, 27 WAYNE L. REV. 1229, 1241 (1981); see also Mitchell & Stein, *supra* note 92.

¹³⁴ Chew-LaFitte, *supra* note 107, at 316.

¹³⁵ See generally Croff, *The Applicable Law in International Commercial Arbitration*, 16 INT'L LAW. 613 (1982).

¹³⁶ T. HOYA, *supra* note 2, at 327.

¹³⁷ FECL art. 5.

practice consistent with private international conflict of laws rules. However, the FECL prohibits the parties from selecting the governing law if the transaction is a Chinese-foreign equity joint venture contract, a Chinese-foreign cooperative joint venture contract, or a contract for Chinese-foreign cooperative exploration and development of natural resources.¹³⁸ Such contracts are generally negotiated in and performed in China, consequently Chinese law would apply.

It appears that Chinese law will apply to a substantial number of foreign trade transactions, but in the absence of a relevant provision of Chinese law governing a specific contractual dispute, the FECL provides that "international practice" shall apply.¹³⁹ The problem with using this body of law is that it is undefined.¹⁴⁰

The FECL attempts to reconcile the complicated area of conflict of laws in a manner consistent with the Chinese position supporting the primacy of international law. This balancing is achieved by applying the provisions of an international treaty which relates to the contract, as long as China has not declared a reservation to that treaty.¹⁴¹ Thus, when the Vienna Sales Convention takes effect in 1988—and binds the United States and China as ratifying parties—this problem will be substantially resolved with respect to contracts involving the sale of goods.¹⁴²

Consistent with prior and current Chinese practices, the FECL encourages informal dispute settlements as opposed to arbitration or litigation.¹⁴³ The Chinese prefer settlement of disputes through consultation even over third party mediation.¹⁴⁴ As far as United States-Chinese foreign trade contracts are concerned, both parties apparently would prefer arbitration. China's accession to the 1958 Convention on the Recognition and Enforcement of Foreign Arbitral Awards in December 1986, and China's entry into the United States-China Trade Agreement in 1979 (which provides for the enforceability of such awards),¹⁴⁵ support that country's apparent preference for arbitration. Furthermore, Chinese arbitral awards are enforceable in China pursuant to China's Foreign Trade Arbitration Rules.¹⁴⁶ It is reasonable to assume that China's

¹³⁸ *Id.*

¹³⁹ *Id.*

¹⁴⁰ See P. VISHNY, GUIDE TO INTERNATIONAL COMMERCIAL LAW § 2.72 (1981).

¹⁴¹ FECL art. 6.

¹⁴² See *supra* note 45.

¹⁴³ FECL arts. 37-38.

¹⁴⁴ Chew-LaFitte, *supra* note 107.

¹⁴⁵ See People's Daily, Dec. 3, 1986, at 1 (int'l Chinese ed.). See also China-United States Trade Agreement, *supra* note 10, at 1050.

¹⁴⁶ Provisional Rule of Procedure No. 32, Foreign Trade Arbitration Commission of the China

courts will be hospitable to such awards issued both in China and abroad so that foreign business and investment will not be discouraged.

VII. PRACTICE RECOMMENDATIONS IN COMMERCIAL DEALINGS

As China's FECL is still relatively new, its interpretation by domestic courts and domestic and foreign arbitration tribunals presents both uncertainties and opportunities for the international transactions practitioner. Within the context of the FECL, as well as other general considerations involved in doing business with China, the following practice recommendations should be considered when negotiating contracts with Chinese enterprises.

First, a prudent practitioner should realize that it may be the exception to the rule to have a body of law other than Chinese law to apply to a transaction. Consequently, familiarity with applicable principles of Chinese law is strongly advised when structuring a transaction. Second, when a contract with Chinese parties is concluded, the practitioner should consider consulting lawyers in MOFERT or lawyers working for Chinese law offices. These individuals will be able to review a transaction for possible conflicts with Chinese rules or regulations. On a related point, the practitioner should have MOFERT also review the transaction to determine whether government approval is necessary. Third, during the negotiation stage, the practitioner should consult MOFERT or other government agencies to verify the authority of the Chinese enterprise and its officers to enter into a contract.

A fourth suggestion is that the practitioner must be patient when negotiating with Chinese parties and remember that China is a developing country. Its nonmarket economy possesses different values and cultural traits than Western trading partners. Fifth, the practitioner should obtain the various form contracts which are currently used by Chinese enterprises and are available in English. Sixth, the practitioner must remember that China is still in the process of codifying new laws and regulations, that English translations may be inexact or unavailable, and that care must be taken to understand the true meaning of the laws and regulations. Finally, in negotiating a commercial transaction in China, an attorney should be prepared to assume a secondary role, allowing the business parties to negotiate face-to-face as is customary in Asian countries.

Counsel for Promotion of International Trade, *reprinted in* China L. Foreign Bus. (CCH Austl.) at ¶ 12-809 (1987).

VIII. CONCLUSION

The FECL has been generally welcomed by foreign lawyers and business executives. It has been called a milestone¹⁴⁷ and a breakthrough¹⁴⁸ in China's legislation, and that it "marks a major step in the surprisingly fast creation of a framework for China's international economic relations."¹⁴⁹ The practitioner should be aware that the FECL has laid down only the most basic principles of contract law, most of which are quite familiar to Western lawyers. These principles reflect China's acceptance of and commitment to abide by international legal norms in the field of international trade and economic cooperation. The FECL can guide China's trade corporations and economic enterprises to transact business with foreign business executives, and it can also assure foreigners that their rights and interests will be legally protected. Accordingly, the FECL can facilitate the development of China's open door policy.

China will continue to expand economically, develop global markets for its goods, and pursue GATT membership. Parallel with these developments, China will continue with the goal of transforming its existing economy into a "socialist market system," resulting in an ever increasing demand for foreign goods and technology. The FECL provides a legal framework for a commercial bridge between China and the West. Successful trade, however, does not depend wholly upon legal acumen. Regardless of the countries involved, understanding the linguistic, cultural, political, economic, and social differences between China and the West is essential to a successful trading relationship.¹⁵⁰

¹⁴⁷ Lubman and Randt, *The Foreign Contract Law, Another Legal Milestone*, 13 CHINA TRADE REP. (May 1985).

¹⁴⁸ Chan, *Foreign Economic Contract Law, a Breakthrough*, EAST ASIAN EXEC. REP., Apr. 1985, at 9.

¹⁴⁹ See *supra* note 64.

¹⁵⁰ As one commentator has stated:

International contracts may be viewed as bridges between the legal systems of two or more countries. The economic traffic carried thereon is comprised of the goods and services exchanged between the parties. To be efficient, bridges must connect smoothly with the roadways at either end. If the ends of the bridge are too broad or too narrow, or if they are too high or too low for the connecting highways, the traffic of good[s] [and] services will encounter loss and accidents. If accidents and loss are substantial, knowledgeable travelers will seek alternative routes or forego the trip altogether.

If contracts are the bridges of international exchange, then lawyers are the engineers. If bridges can be constructed from each end toward the middle, a contract might be said to represent a "meeting of the minds" of the parties. Careful planning and compatible materials are a prerequisite for a stable bridge. Likewise, for international contracts to bridge the gap between two legal systems and withstand the pressure of changing circumstances, each party must understand well the demands of the other party. Without this fundamental agreement, the contract will have a shaky basis and an insecure life expectancy.

E. THEROUX, *supra* note 21, at 297.

China has the potential to become the United States' largest trading partner. The opportunities for both countries are so vast that they are difficult to comprehend. The exploitation of these opportunities is directly dependent upon continued improvements in mutual understanding and respect for cultural differences between East and West. Only with these extralegal considerations in mind can the international transactions practitioner be assured of a true meeting of the minds when constructing a contractual bridge between United States and Chinese parties.