



September 2012

China

THE VIOLATION OF THE MANDATORY ADMINISTRATIVE RULES DOES NOT LEAD TO THE NULLITY OF CONTRACT

SUMMARY OF THE CASE:

Plaintiff in the First instance and respondent in the Second instance: Company B

Defendant in the First instance and appellant in the Second instance: Company A

JUDGMENT:

First instance: Company A condemned to pay the charges and interest of the contract to Company B. Company B bears the government fine of Company A.

Second instance: Judgment confirms First instance ruling.

BACKGROUND OF THE CASE:

Company A signed a contract with Company B in which they agreed that Company B will provide electronic equipment and post-sale services to Company A. Furthermore, the contract provided that the equipment belonging to the Company B, will belong to Company A after the completion of the contract, and that no party to the contract can terminate the contract without cause, except for force majeure events.

However, two years later, Company A unilaterally terminated the contract for alleged system crash of equipment. Later, Company A bought other equipment from third parties to replace the equipment provided by Company B. Months later, the government fined Company A because the equipment without CCC ("China Compulsory Certification") provided by Company B did not comply with the mandatory administrative rules. Consequently, Company A allegedly believed that the contract was not valid and therefore refused to pay Company B.

Company B started a lawsuit against Company A demanding payment based on the contract. The Court rules in favor of Company B; thus, condemning Company A to pay the charges and interest of the contract to Company B. In addition, Company B bears the government fine punishing Company A for non-compliance with the mandatory administrative rules.

FOCUS OF THE DISPUTE:

Q1. Is the contract signed by Company A and Company B one of the named contracts?

A1. Company A believed that the contract is a sales contract covering the installment and the retention of title. But the cost of equipment was not covered by that contract. Consequently, it is not a sales contract, and the contract signed by Company A and Company B is not one of the named contracts. Opinion of the Court: that the contract signed by Company A and Company B does not have the basic elements of a contract for sales. Therefore, it is a different type of contract.



Q2. Is the contract signed by Company A and Company B valid?

A2. Company A argued that the equipment provided by Company B does not comply with the mandatory administrative rules. Consequently, Company A argued that the contract signed by Company A and Company B is null. Nevertheless, according to the judicial interpretation of contract law, the mandatory rules regulated in contract law are the mandatory forceful rules rather than the mandatory administrative rules. Therefore, the equipment non-compliance does not lead to the nullity of the contract signed by the parties. Opinion of the Court: the non-compliance with the mandatory administrative rules should be punished by the government. However, non-compliance does not lead to the nullity of the contract between Company A and Company B.

Q3. Are there problems with the equipment provided by Company B? If yes, should Company A pay for the contract?

A3. Company A claimed that there are problems with the equipment provided by Company B. However, Company A did not provide enough evidence to prove the alleged equipment malfunction. Company A's evidence was a record of product quality solely signed by its own representatives; and not signed by Company B's engineer on site. Therefore, the judge did not retain this evidence and ruled that Company A should pay the charges and interest of the contract to Company B. Opinion of the Court: Company A's counter-argument cannot be supported. Company A should pay for the contract.

Agent experience:

See: article 52.5 of PRC Contract law; Article 14 of Interpretation of the Supreme People's Court on Certain Issues Concerning the Application of the Contract Law of the People's Republic of China ()

Compulsory provisions of the laws: (1) Effectiveness (strong: eg. Selling guns) and (2) **Management of social matter (not strong: eg. CCC regulation)**

CCC: China Compulsory Certification: for special products (eg: selling special computer requires CCC application)

This Newsletter is intended for general distribution to clients and colleagues and the information contained herein is provided as a general and abstract overview. It should not be used as a basis on which to make decisions and professional legal advice should be sought for specific cases. The contents of this Newsletter may not be reproduced, in whole or in part, without the express consent of the author. If you should require further information on this topic, please contact **Jeffrey Liu** (xinyu.liu@dachenglaw.com) or **Luís Sáragga Leal** (luis.saraggaleal@plmj.pt).

Avenida da Liberdade 224, 1250 -148 Lisboa, Portugal (headquarters)
T. (+351) 213 197 347 . F. (+351) 213 197 400 . www.plmj.com

12/15F, Guohua Plaza, No.3 Dongzhimennan Avenue, Dongcheng District, Beijing 100007, PRC (headquarters)
T. (+86) 10 5813 7799 . F. (+86) 10 5813 7788 (12/F) . www.dachenglaw.com
