

# Application of the Defaulting Party's Right to Rescind the Contract in Chinese Civil Code

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**Abstract:** The issue of "whether the defaulting party has the right to rescind the contract" in Article 580, paragraph 2 of Civil Code of the People's Republic of China (abbreviated as Chinese Civil Code) has given rise to many controversies. After organizing the practice cases, the focus of the controversy should be placed on the basis of the legitimacy of the right, that is, in the event of a material breach of contract and other circumstances, can be considered to give the defaulting party "the option of remedy means for breach of contract". Although this system is similar to the theory of "efficient breach" in the common-law system, there are significant differences in the specific application of the two systems. It should be further clarified that the party in breach of contract enjoys not the right to terminate the contract, but the right to rescind. And the subject who has the right to exercise this right is the defaulting party itself rather than the people's court or arbitration institution. When applying the system, in addition to considering the scope of cases specified in Chinese Civil Code, it should also be combined with the relevant provisions of the Minutes of Civil and Commercial Trial Work Conference of the National Court. Only when the defaulting party subjectively meets the requirements of "there is no malicious breach", "the conduct of the abiding party is contrary to the principle of honesty and credibility", and objectively meets the requirements of "obviously unfair to the defaulting party" and "the purpose of the contract cannot be achieved", can the defaulting party rescind the contract. As an innovative right, the defaulting party's right to rescind the contract must be exercised across a number of legal hurdles. Only in this way can the fairness of the transaction and the order of the market be safeguarded, and the right to rescind the contract be ensured that it does not become a legal tool for evading responsibility.

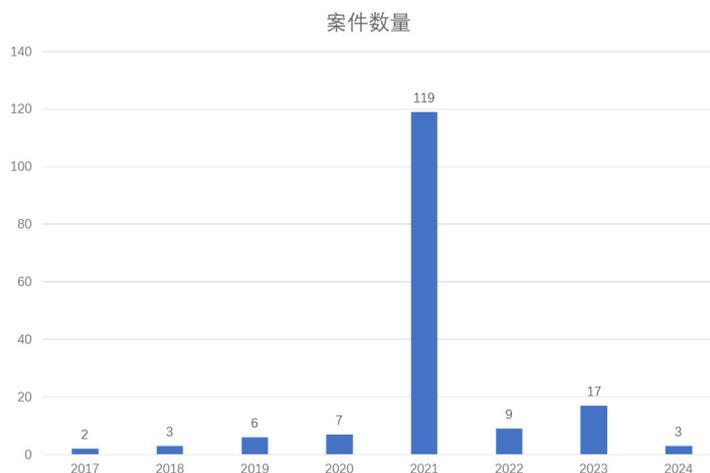
**Keywords:** Defaulting party; right to rescind contract; efficient breach; breach of contract liability.

## 1. Typical Problems Presented by Practice Cases

The general view is that the right to rescind a contract can only be enjoyed by the observant party, but Article 580(2) of Chinese Civil Code affirms the system of the defaulting party's right to rescind a contract to a certain extent, which triggered a controversy between practical and academic circles. However, it should be noted that the interpretation and application of this system has a long history of controversy, which can be traced back to the "Xinyu Company v. Feng Yumei Shop Sale and Purchase Contract Dispute".<sup>[1]</sup> The court held that the defaulting party's continued performance of the contract would result in the failure to achieve the

purpose of the contract, and thus, in order to balance the interests of the two parties, the court pioneered to support the defaulting party's rescission of the contract. The establishment of this decision has had a demonstration effect in judicial practice, and a series of similar cases have gradually emerged. In order to standardize the standard of decision and respond to the theoretical controversy, it is urgent to study the practical problems in depth, and to guide the practice by the theory.

The author conducted empirical research and search through the judgment documents retrieval website "the Magic Weapon of Peking University" with the keyword of "the defaulting party's right to rescind the contract". As of April 8, 2025, 166 legal documents have been found, including 9 rulings and 157 judgments.



It is not difficult to find that after the implementation of Chinese Civil Code, the application of the defaulting party's right of rescission in the adjudication documents has shown a spurt of growth, marking the development of the system in China has entered a new stage. Meanwhile, in order to avoid the subjectivity of case search as much as possible, the author will summarize the research results of the previous researchers, including Tian Meng, [2] Yi Jia,[3] Zuo Rongxian,[4] Kan Xujie,[5] Zhang Wanqi [6] and so on, in anticipation of a more comprehensive understanding of the issue. The researchers conducted meticulous searches for similar topics using authoritative case search platforms such as "China Judgements Online", "the Magic Weapon of Peking University", and "Jufa Cases", and analyzed and summarized the results in multiple dimensions, including the types of contracts involved in the cases, the trial procedures of the cases, and the winning rates of the cases. The synthesis of different researchers' analyses on similar topics can significantly enhance the objectivity and comprehensiveness of the research results, so as to carry out in-depth discussions while standing on the shoulders of giants. The research results of the above researchers are summarized as follows:

First, most of the cases focus on contractual disputes, in which the types of contracts involved are characterized by both diversity and concentration. Despite the differences in the research data of different researchers on this issue, the core conclusions reached are highly consistent. Specifically, the cases involving the right to rescind by the defaulting party are mostly concentrated in house-leasing contracts, followed by housing sales contracts, with other types of contracts occupying only a small proportion.

research worker	Tian Meng	Yi Jia	Kan Xujie
Lease contracts (concentrating on housing)	57%	52%	54%
Sale and purchase contracts (concentrating on housing)	29%	22%	23%
Other contracts	14%	26%	23%

Secondly, a high percentage of cases supported the exercise of the defaulting party's right to rescind the contract by the defaulting party. The cases studied by the researchers involve both the period of the Contract Law and the period of Chinese Civil Code. During the period of the Contract Law, the court usually supports the defaulting party to rescind the contract on the grounds of "balancing the interests of both parties" and "the main purpose of the contract cannot be realized", etc.,[7] However, some courts opposed the exercise of the right of rescission by the defaulting party on the grounds that "the right of rescission is a right of formation and no counterclaim has been filed" and that "the contract can continue to be performed". [8] After the promulgation of Chinese Civil Code, although the legal provisions have been further improved, the interpretation and application of the law are still controversial. Some courts support the defaulting party's rescission of the contract on the grounds of "imbalance of interests between the two parties" and "excessive cost of performance", etc.,[9] However, some courts still insist that the law does not give the defaulting party the right to rescind the contract.[10]

Therefore, scholars need to further explore the legitimate basis for the existence of the defaulting party's right to rescind, the specific conditions for the exercise of the system and the scope of application.

research worker	Tian Meng	Yi Jia	Zuo Rongxian	Kan Xujie
winning rate	66.7%	70%	66%	60%

Third, the invocation of article 110 of the former Contract Law or article 580 of Chinese Civil Code accounted for a relatively high percentage of retrieved cases. The legal basis for the defaulting party to exercise the right to rescind the contract is also arbitrary to a certain extent in the judge's practical decision due to its ambiguity. However, it is clear that Article 110 of the former Contract Law or Article 580 of Chinese Civil Code is regarded as an important basis for the defaulting party's right to rescind the contract, and therefore an in-depth study of Article 580 of the current Chinese Civil Code will help to achieve judicial unification.

research worker	Tian Meng	Yi Jia	Zhang Wanqi
Article 94 of the Contract Law or article 563 of Chinese Civil Code	16%		27%
Article 110 of the Contract Law or article 580 of Chinese Civil Code	42%	54%	42%

By summarizing and analyzing the results of the researchers, it is easy to find that in the current judicial situation, the right of rescission is of great significance as a tool to break the deadlock of contract, especially for solving long-term contracts. Secondly, judges hold different views on whether the defaulting party enjoys the right to rescind the contract, and there is also a divergence between the "negative theory"[11] and the "restrictive affirmative theory"[12] in the academic circle, which is the foundation for the development of the system, and the legitimacy of the existence of the system needs to be clarified after weighing a number of elements. At the same time, in the specific application of the system, due to the lack of accurate scope of application and perfect application standards, in practice, it is easy to appear the same case with different judgments. In order to clarify the application path of the right to rescind the contract, this article is based on the "restrictive affirmative theory", and at the same time draws on foreign practices in dealing with contractual impasse, to provide countermeasures and suggestions for the improvement of the system, in order to help safeguard the lawful interests of both parties to the contract, and the rational allocation of social resources.

## 2. The Legitimate Basis for a defaulting party's Right to rescind a Contract

Traditional civil law upholds the notion that the contracting

party has a legal right to rescind the contract. [13] The system of the right to rescind the contract of the defaulting party established in the paragraph 2 of Article 580 of Chinese Civil Code is an innovation in the official legal documents of our country, demonstrating the Chinese wisdom gathered in the judicial practice process. However, due to the lack of strong theoretical basis, its rationality and legitimacy are facing challenges. If the defaulting party is given the right to rescind the contract, the rights that originally belonged to the observant party are reversed to the defaulting party, will the reversibility of rights lead to abuse of rights? If the defaulting party obtains a higher income by rescinding the contract in breach of contract, will it disturb the market order? In order to solve the above problems, this paper will combine the scholars' multiple perspectives for more in-depth investigation, with a view to providing a justifiable basis for the defaulting party's right to rescind the contract.

### **2.1. Rationalizing the reversibility of the option of remedy**

Some scholars put forward the defaulting party's right to rescind the contract is on the surface of the right to rescind the contract to the defaulting party. However, if the right to rescind the contract is regarded as a remedy that the defaulting party can choose to apply or waive, then, it also means that when there is a serious breach, the defaulting party has the option that originally belongs to the observant party. Therefore the defaulting party can choose to exercise the right to rescind the contract without any concerns. [14] However, there are different opinions on whether this option can be transferred between creditors and debtors.

Rescission of contract, as a means to get rid of the contractual relationship constraints, the main purpose is to "liberate contractual obligations" of the parties to the contract.[13] Therefore, the contracting party enjoys the right to end the contract as soon as possible in a state of uncertainty without doubt. However, can the defaulting party obtain such "option" when the observant party does not make any choice for a long time, leaving the contract in an uncertain state? The opposing view that the right of choice reversibility, although not unfamiliar in theory, can not be applied by analogy to the defaulting party's right to rescind the contract. In the civil law, it is well known that optional obligation can be reversed, that is, when the party who has the optional obligation does not actively exercise the right will lose the right at last, the other party accordingly obtain the right of choice. [15] However, it should be noted that there is a significant difference between the reversibility of the optional obligation and the reversibility of the defaulting party's right to rescind the contract. The optional obligation focuses on the different payment content of the right to claim, can be seen as a choice of different sides of the same cube. While the choice between the right to perform the contract and the right to rescind the contract discussed in this paper is a choice between different types of rights, which can be regarded as the choice of different cubes, and there is a competitive exclusion relationship between the two. The optional obligation is certainly a panacea to deal with the impasse, but the direct application of other system without combining the specific legal environment is unavoidably biased, which is easy to cause the abuse of option reversal and damage the interests of creditors.

The supporting view is based on the principle of good faith, that the creditor in a long period of time does not make a choice will cause the emergence of a state of uncertainty, this

state of uncertainty of the legal relationship will put the debtor in a disadvantageous position. Therefore, by interpreting and applying the law to grant debtors greater agency in proactively dealing with contract related matters—shifting from a passive to an active role—the defaulting party should be permitted to rescind the contract under exceptional circumstances.[16] It should be noted that this reversal of rights is not automatic, but requires the debtor to urge the creditor to make a decision to terminate or perform the contract. Once the creditor does not respond within a reasonable time, the option is reversed. [14] Therefore, when the contract deadlock occurs, if the defaulting party has the initiative to rescind the contract, both parties can get rid of the rights and obligations stipulated in the contract as soon as possible, so as to avoid further losses.

### **2.2. The relationship between the defaulting party's right to rescind the contract and efficient breach of contract**

Another point of view that denies that the defaulting party has the right to rescind the contract is that the defaulting party has the right to rescind the contract is based on the foundation of the theory of efficient breach of contract in the common law. The theory of efficient breach of contract originated from the American law, Posner pointed out that: "if a party can get more benefits by breaching the contract, and the benefit exceeds the benefit of performing the contract, there may be the consciousness and behavior of breaching the contract. By this logic, if a party's benefit of breaching the contract is far greater than the benefit of contract compliance, and the amount of loss is limited, the party is very likely to be incentivized by such situation, so as to commit a breach of contract." [17] If the defaulting party has the right to rescind the contract, then the defaulting party will actively pursue the default in case of profit. Scholars believe that the introduction of efficiency default will produce great moral hazard,[18] and it is obviously against the basic legal principle of prohibiting profit from illegal acts. At the same time, if the defaulting party enjoys such initiative, it will be contrary to the strict adherence to the basic principles of the contract.[19] What's worse, it will generate incorrect incentives for the actor from the legislative level, and ultimately harm the security and stability of the trading market.

Before studying the relevant provisions in China, it is necessary to explore the attitude of civil law countries on the breach of contract to enjoy the right to rescind the contract. The German Civil Code does not specify the defaulting party's right to rescind the contract, but its introduction of "positive infringement theory" also reduces the influence of fault degree on the recession of contract. At present, the restriction conditions of contract recession in the German Civil Code are more and more relaxed. When the contract performance can not be produced, the original payment obligation can be automatically converted into damages, thus avoiding the contract deadlock. Another representative of the civil law system—France, similar to Germany, the defaulting party's right to rescind the contract did not make specific provisions, but pointed out that various other dissolution systems can be used to alleviate contractual deadlock. For example, a contract may be automatically rescinded in the event of a permanent obstacle to performance. Although the civil law system does not give the defaulting party the right to rescind the contract, but have taken different measures to deal with the contract impasse, and not be trapped

in the rule that the contract must be obeyed. No matter the civil law system or the common law system, countries maintain a high degree of unity in the pursuit of transaction efficiency.

As a big trading country, China's pursuit of efficiency has also run through the Contract Law and Chinese Civil Code. We cannot abandon the path of improving transaction efficiency for fear of some speculators, and we can set up barriers to the application of the law to stop the contracting parties who try to take shortcuts to disrupt the market order. In addition, the act of giving the defaulting party the right to rescind the contract does not mean that our country introduces the theory of efficient breach of contract. Although both are to avoid the waste of social resources, there are big differences in the specific application. First of all, the possibility of actual performance is different. In the case of actual performance, in order to pursue interests and efficiency, the breach of efficiency is actively pursued by replacing actual performance with damage compensation. In contrast, the right to rescind the contract is that when the actual performance is difficult and the contract falls into an unstable state, the defaulting party has to exercise the right to rescind to stop the loss in time. Second, they have different core values. The default of efficiency default is active default, with the purpose of obtaining greater benefits. This system pays more attention to transaction efficiency. However, the right to rescind the contract of the defaulting party is a remedy, which not only includes the pursuit of efficiency, but also takes into account fairness and good faith. Therefore, the defaulting party's right to rescind the contract is not a simple transplantation of the theory of efficiency breach of contract. Although there are similarities between the two system, they all serve the legal environment of their respective countries and the reality of the demand, so the differences between them can not be ignored.

### **3. Application of the defaulting party's right to rescind the contract in the context of Chinese Civil Code**

Chinese Civil Code grants the defaulting party the possibility to enjoy the right to rescind the contract through simple provisions. However, if this right is not limited, there is a high risk that the cornerstone of trust between the contracting parties will collapse. Of course, the value of this right cannot be denied because of the risks it poses. Therefore, it is crucial to limit this right through the interpretation of the law. First of all, this article should explore the nature of the right, in order to clarify its legal position. Secondly, this article should limit the scope of application of the right in order to clarify its legal boundaries. Thirdly, this article should analyze the composition of the right in order to clarify the prerequisites for the exercise of the right. Lastly, this article should pay attention to the exercise of the right and the legal consequences of the exercise of the right in order to clarify the procedural points and the effect of the exercise of the right. Only through this series of legal interpretation and application considerations, can we truly select the defaulting party with the right to rescind, and can we escort the contractual relationship in the society under the rule of law.

#### **3.1. Interpretation of the defaulting party's right to rescind the contract**

Based on Article 110 of the original Contract Law, article

580 of Chinese Civil Code adds a clause on contract rescission, specifying that if any of the foregoing circumstances makes it impossible to achieve the purpose of contract, the people's court or arbitration institution may terminate the relation of contractual obligations and rights at the request of the parties, without affecting the assumption of the liability for breach of contract.[20]The author believes that this clause gives the defaulting party the right to rescind the contract, which is essentially to safeguard the rights and interests of the defaulting party. However, a closer examination of the wording of the clause reveals its vagueness. The expression of the law does not explicitly point out the "defaulting party", nor does it use the legal term "rescission of the contract", but only "the parties" and "terminate the relation of contractual obligations and rights" are generally described. This kind of vague expression leaves room for discussion, and also makes the interpretation of the defaulting party's right to rescind the contract become a hot topic in the academic and practical circles.

a) The parties have a right of rescission and not a right to terminate the contract

After reading relevant legal literature, the author agrees with the scholars that the parties enjoy the right of rescission rather than the right of contract termination based on this clause. According to the civil law system in the classic theory, "contract termination" usually only applies to continuous contracts and the effect of such contracts is not retrospective. "Rescission of contract" applies to dual contracts, which have the corresponding retroactive effect.[21] However, since the period of the domestic Contract Law, neither the laws and regulations nor the judicial interpretation, there is no clear breakdown of the "contract rescind" and "contract termination". Article 557 (2) of Chinese Civil Code states that when the contract is rescinded, the rights and obligations of the contract are terminated. The termination of the contract is the final legal result, and the rescission of the contract is one of the reasons leading to this result. In other words, if the parties exercise the right to rescind the contract, the contract rights and obligations will be terminated. In addition, article 563 of Chinese Civil Code belongs to general provisions of the statutory right of rescission, article 580 paragraph 2 belongs to the special rules of the right of rescission. In general, the scope of application of general provisions includes special rules. However, considering the differences between the two kinds of rescission rights in the substantive and procedural elements, although they have similarities, they still need to be carefully applied. Therefore, in order to avoid conflicts between clauses, Article 580 does not use the expression "contract termination".

2. The people's court or arbitration institution does not have the right of judicial rescission, but the defaulting party really enjoys the right of rescission.

As the law clearly stipulates that the people's court or arbitration institution shall rescind the rights and obligations in the contract in accordance with the specific request of the parties, some scholars believe that this article only provides for the right of judicial rescission.[22] However, the author more agree that the people's court or arbitration institution does not enjoy the right of judicial rescission, in fact, it is the defaulting party that really enjoys the right. An application to a people's court or an arbitration institution is only a procedural requirement for the realization of the right to rescind. In order to reach this conclusion, we must first clarify the concept and nature of "the right of judicial rescission". It

means that the people's court can rescind the contract at any time according to the development of the case and the specific circumstances.[23] The reason why scholars argue on this issue is that the law does not clearly stipulate the relationship between the court's discretion and the parties' rights. To prove it, take revocable juristic act as an example, the right of revocation belongs to the rights of the parties is uncontroversial, because the law stipulates that the right of revocation is the formation of the right of action, which must be promoted through litigation and arbitration procedures. Therefore, the role of courts and arbitration institutions in the exercise of rights is just to promote the process. On the issue of the defaulting party's right to rescind, the court or arbitration institution needs to take into account the actual situation of each case and combine with the relevant legal norms, and ultimately make a decision on whether to support the claim of the right holder. Therefore, although the court or arbitration institution plays an important role in the relevant cases, it does not affect the determination of the rights of the parties. Based on the above analysis, it is more reasonable to think that the defaulting party has the right to rescind the contract.

b) The subject matter of the rights provided for in this provision shall be limited to the defaulting party.

As to whether "party" refers only to the defaulting party or literally includes both defaulting and observant parties, the author believes that the subject of the right should be limited to the defaulting party. Since article 580, paragraph 1, gives the defaulting party a defence against the creditor's claim for continued performance of the contract in three exceptional circumstances, the scope of "party" in paragraph 1 should logically be limited to the defaulting party. Paragraph 2, as a supplement to and extension of paragraph 1, should be interpreted in accordance with paragraph 1 and should not be interpreted in isolation from the two provisions. Therefore, the "party" stipulated in paragraph 2 is limited to the defaulting party with the actual defense right, which is more consistent with the system of legal interpretation.

### **3.2. Scope of application of cases on the right of the defaulting party to rescind the contract**

According to the law, in the case that the party has breached the contract but the creditor requires the actual performance of the contract, the breaching party must first satisfy the scope of application of the right to exercise the right of rescission. Under the Civil Code, the right to rescind can be applied in cases where performance is unable to be performed in law or in fact, where the subject matter of the obligation is unfit for enforcement or the performance expenses are excessively high; and where the creditor does not request performance within a reasonable time limit. In addition, it should be noted that, due to the special nature of monetary debts, the defaulting party's right to rescind the contract applies only in the case of non-monetary debts.

Performance which is unable to be performed in law means that the content of the contract cannot be carried out according to the law, and once carried out, it violates the mandatory provisions of the law. Performance which is unable to be performed in fact refers to the fact that the contract cannot continue to be implemented due to the impact of the objective natural environment. Besides, the scope of contracts in which the subject matter is not suitable for compulsory performance is mainly limited to personal contracts.[24] If continued

performance of the contract may entail higher costs for the parties, a proper balance needs to be struck between the costs of performance of the contract by the debtor and the benefits of performance by the creditor. Finally, in the case that the creditor does not request performance within a certain period, it should be noted in practice that the period must be specified according to the actual situation such as the normative purpose, contract terms or trading habits.[24] The law summarizes the situation that may appear in the contract deadlock in life, which is called the obstacle of performance in law. If one party insists on continuing to perform, it may cause the result of mutual harm. Therefore, in these specific circumstances, Chinese Civil Code allows the defaulting party to apply for termination of the contract.

In addition, compared to non-pecuniary debts, money belongs to the general equivalents, there is no irreplaceable extinction, and it does not involve unreasonable circumstances on the economic level. However, there are many cases involving the sale or lease of houses, in which one party to the contract has the obligation to pay the price, which means that the case belongs to the category of money debt, but the court supports the defaulting party to terminate the contract on the grounds that it cannot actually perform or the performance cost is too high. The party liable to pay the price is often cited as being unable to make the mortgage payment, which prevents the performance of the obligation, [25]or as an unforeseen default due to a new government policy, [26]or as being unable to meet the monetary payment obligation due to poor management.[27] The author believes that the money debt can always be actually performed in principle, so there are theoretical and logical loopholes in supporting the defaulting party's rescinding right in the case of money debt. In order to balance the interests of both parties, the court can solve the problem through the gross misunderstanding system or the principle of changed circumstances.

As in the Contract Law period, Chinese Civil Code also does not clearly specify the circumstances of compulsory performance of monetary debts, only in the Article 580, paragraph 1 clearly states that the subject matter of the obligation is unfit for enforcement, through which the debtor is granted the right to defend performance in non-monetary debt cases. In accordance with mitigation rule and the basic principle of good faith, when the condition is met, the debtor may perform the corresponding damage compensation obligation so that the original contract will lose its actual effect.

### **3.3. Elements of the defaulting party's right to rescind the contract**

The right to rescind the contract of the defaulting party is a new legal system, and its constituent elements have not yet formed a unified conclusion. At present, the academic circles for the composition of the right to hold a variety of views. One point of view indicates that the constitutive elements mainly include the absence of fault of the defaulting party, the emergence of a deadlock in the transaction, the loss of the efficiency of the contract performance, etc.[28] Meanwhile, there are also views indicating that the main conditions for the defaulting party's right to rescind are contractual deadlock and contractual violation of equitable principle.[29] A representative one is Article 48 of minutes of civil and commercial trial work conference of the national court. It argues that the defaulting party, in order to enjoy the right to rescind the contract, must satisfy three constitutive

requirements, including "there is no malicious breach", "the conduct of the abiding party is contrary to the principle of honesty and credibility", and "obviously unfair to the defaulting party". Besides, in accordance with the requirements of Chinese Civil Code, "the purpose of the contract cannot be realized" is also a key constitutive requirement. Since this generalization still leaves a lot of room for interpretation, judges have to make it specific when applying the system of the defaulting party's right to rescind. In order to make the elements of the analysis more clear, this paper will divide these requirements into subjective and objective aspects, subjective elements for "there is no malicious breach" and "the conduct of the abiding party is contrary to the principle of honesty and credibility". Objective elements are mainly "obviously unfair to the defaulting party" and "the purpose of the contract cannot be realized".

#### a) Subjective elements

One of the subjective elements is "there is no malicious breach", which requires that the debtor shall not obtain unlawful gains through breach of contract, or at least shall not actively pursue breach of contract as in the common law theory of efficient breach of contract. But to "there is no malicious breach" as the specific elements of the expression can be further elaboration and qualification. In the civil law system, "malice" is opposed to "good faith". Some scholars summarize "good faith" as the objective fact of "not knowing the existence of a certain situation".<sup>[30]</sup> Usually, scholars will measure the subjective good faith of the actor in the acquisition in good faith to measure the subjective good faith of other systems. In addition, some scholars equate "good will" with "no fault".<sup>[31]</sup> In other words, as long as the defaulting party is subjectively aware of its duty of care and takes the principle of good faith as the code of conduct, it can be considered that the party's behavior is in good faith. Then, "malice" can also be analyzed from the two aspects of subjective consciousness and subjective intention. On the one hand, the parties need to realize that their own behavior is not in accordance with the provisions of the law or the lack of legal rights.<sup>[32]</sup> In addition, "malice" also requires the defaulting party to know that its behavior is not in line with the contractual obligations and will bring adverse consequences to the other party, but still maintain a negative indulgence or active pursuit of intentional mentality. This judgment method is a feasible way in theory, but in practice, the case is complicated, judging whether the parties subjectively "malicious breach" by these two aspects is still far from enough.

The other element of the subjective component is "the conduct of the abiding party is contrary to the principle of honesty and credibility". The principle of honesty and credibility is generally understood as requiring all market participants to pursue their own interests without infringing on the interests of others and the public. In judicial practice, the judge for the application of the principle of honesty and credibility has great discretion. However, in cases involving the defaulting party's right to rescind the contract, judges should take into account that the contract transaction is not a zero-sum game between the parties, but should be based on mutual benefit and win-win. Both parties should take into account the reasonable expectations of the other party. Even if the observant party has the right to demand the rescission of the contract or the defaulting party to continue to perform the contract, when the rescission of the contract is the best choice, the observant party should also take into account the

interests of the defaulting party based on the principle of good faith. To judge whether the observant party's refusal to rescind the contract violates the principle of honesty and credit and how to interpret the principle of honesty and credit in individual cases is a test for judges, and it is also a place for further improvement of judicial practice in our country.

#### b) Objective Elements

In discussing the element of "obviously unfair to the defaulting party", the term "obviously unfair" also has a specific meaning in civil law, and therefore its terminology needs to be carefully scrutinized. In civil law, this term refers to a party taking advantage of the other party's subjectively weak position, such as lack of relevant experience or judgment ability, relatively weak willpower, etc., objectively resulting in a serious imbalance between the rights and obligations of the two parties, thus damaging the rights and interests of the other party.<sup>[33]</sup> In the system of the defaulting party's right to rescind, the consideration of fairness is more focused on the economic impact on the parties if the contract continues to be performed. However, in judicial practice, this measurement is usually based on two standards, one is from the perspective of both parties, using the standard of "the destruction of contract equivalence" in the system of changed circumstance, and the other is from the perspective of the defaulting party, taking the high performance cost as the judgment standard. To pursue efficiency or fairness, the two standards have their own rationality and limitations, but the judicial practice needs a clear and unified standard to maintain the predictability and fairness of judicial judgment.

The element of "purpose of the contract" refers to the common goal or desired effect pursued by the parties when entering into the contract. The purpose of the contract is one of the core elements of the contract and usually includes economic benefits, legal rights and commercial opportunities. Therefore, "the purpose of the contract cannot be realized" in the case of contract deadlock is because the parties can not achieve the expected benefits. For example, in a sales contract, the buyer is required to purchase a large number of costumes to prepare for the ceremony. However, the buyer found that the clothing was damaged after receiving the goods. The seller requires payment before replacement, while the buyer believes that the price can only be paid if the subject matter meets the requirements. In these similar circumstances, both parties can not achieve the purpose of the contract, the performance of the contract is deadlocked. In order to avoid further losses, the court should support the defaulting party to rescind the contract according to Article 580 of Chinese Civil Code. Because according to this clause, the premise for the defaulting party to exercise the right to rescind the contract is that "the purpose of the contract cannot be achieved", and the exercise of this right can terminate the contract as soon as possible to avoid further deterioration of the transaction situation.

### 3.4. Manner of exercising the defaulting party's right to rescind the contract and legal consequences

According to Chinese Civil Code, the defaulting party's right to rescind the contract is exercised by means of a judicial rescission application and not by means of a notice of rescission.<sup>[34]</sup> Article 59 of the Judicial Interpretation of Contracts of Civil Code makes specific provision for the effective time of rescission of the contract by the defaulting party. Under normal circumstances, the termination time of

the rights and obligations of the parties is when the copy of bill of complaint is served. It should be noted that the interpretation also gives the judge discretion, based on the principles of fairness and good faith, the judge can still choose other time points based on the specific circumstances of the case.[35] As for the choice of other time points, some scholars have proposed that in some cases, the specific time point when the defaulting party's right to rescind meets all the constituent elements can be considered as an important reference for judges to determine the validity of contract rescission.[16] The purpose of granting the defaulting party the right of rescission is to solve the loss caused to the defaulting party by the contract deadlock. When the observant party refuses to rescind the contract and causes losses to both parties to a certain extent, the defaulting party should be freed from the contractual obligations as soon as possible, so as to solve the contract deadlock. Of course, whether it is the time when the parties receive the copy of a bill of complaint as the contract rescission point, or other more appropriate time as the contract rescission point, the judge should consider the interests of both parties based on the principle of fairness and efficiency.

Article 566, paragraph 1 of the Civil Code stipulates the legal consequences after the rescission of the contract, which adopts the form of extracting common factors, adopts different remedies according to whether the contract is performed, and clarifies the legal responsibilities to be borne at each stage of contract performance after the rescission of the contract. Since paragraph 2 of Article 580 refers to "the assumption of the liability for breach of contract shall not be affected", the provisions of Article 566 on liability for breach of contract also apply to the exercise of the right of rescission by the defaulting party. In practice, if the breaching party rescinds the contract, it usually needs to bear certain liability for damages. Due to the particularity of the system of rescind right of the breaching party, the degree of liability for damages should be determined according to the fault degree of the parties in a specific case. At the same time, in order to further improve the system, the standard system of damage compensation should be established to ensure that it is more sound.

#### 4. Conclusion

As the embodiment of social rules, law inevitably has a lag. In view of the actual demand of the defaulting party's right to rescind in current practice, Article 580 (2) of the Civil Code provides corresponding answers, providing new ideas and legal basis for judicial adjudication to deal with contract deadlock. "Xinyu Company case", as a case of gazette, has practical guidance significance, but because of the lack of clear provisions in the Contract Law, there is no uniform standard for local courts. The implementation of the Civil Code has undoubtedly injected new vitality into the construction of the defaulting party's right to rescind the contract. On the premise of the legitimacy and rationality of the system in combination with China's national conditions and practical needs, this paper discusses the nature and positioning of the defaulting party's right to rescind the contract, the limitation of the scope of application, the clarity of the exercise conditions, the exercise manner and the legal consequences. Try to provide a more comprehensive interpretation path, so as to better balance the rights and obligations of both parties in the contract. However, as Holmes said, "the life of the law does not lie in logic, but in

experience.". The combination of theory and practice is a process of continuous exploration, the establishment and improvement of the system can not be achieved overnight. It needs to go through countless debates and discussions, countless tests and amendments. Only in this way can the system meet the needs of the trading market and fulfill the expectations of our society under the rule of law.

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