

On the Establishment of General Rules for Termination for Compelling Reasons in the Civil Code

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Abstract

The Civil Code lacks sufficient provisions regulating the termination of continuing contracts, thereby failing to address issues arising from continuing contract deadlock in practice. It is therefore essential to establish general rules for contract termination for compelling reasons in the Civil Code. Provisions such as Article 899(2), Article 933, Article 1022(2) of the Civil Code, and Article 45(3) of the Partnership Enterprise Law all contain principles for termination for compelling reasons, which are consistent with the principle of good faith stipulated in Article 7 of the Civil Code. As such, both juridical methods, overall analogy and the concretization of the principle of good faith, have their theoretical and normative bases when establishing general rules for termination for compelling reasons in the Civil Code. From the perspective of certainty, the method of overall analogy can be prioritized. To overcome the mismatch of this method and the overall professionalism of judges, guiding cases should be issued by the Supreme People's Court to provide references for courts at lower levels in their adjudication.

Keywords

Compelling Reasons, General Rules, Overall Analogy, Principle of Good Faith

1. Introduction

During the compilation of the Civil Code, there was heated discussion on how to resolve the deadlock problem of continuing contracts in practice. This issue can be described as follows: the parties lose their reasonable expectations for ongoing performance due to changes in either objective or subjective circumstances during the execution of these contracts, yet they lack the means to liberate them-

selves from the binding of contracts that are no longer meaningful. To address issues arising from continuing contract deadlock in practice, Article 580(2) of the Civil Code was added, stipulating that “Where one of the situations specified in the preceding paragraph exists so that the purpose of the contract cannot be achieved, the people’s court or an arbitration institution may terminate the contractual relationship of rights and obligations upon request by a party, but the default liability shall still be borne without being affected”. This is the rule of judicial termination which excludes continuing performance. Nonetheless, the application scope of this rule is restricted by the first paragraph of the same article, it only applies to non-monetary debts. As a result, this rule cannot address the issues of contract deadlock caused by non-performance of monetary debts. This indicates the insufficiency of the Civil Code regarding termination rules for continuing contracts. To fill this legal loophole, many scholars have proposed learning from relevant provisions in German law and introducing general rules for termination for compelling reasons (Han, 2020). The core question arising thereof is how to establish such general rules using other relevant articles in the Civil Code when general rules for termination for compelling reasons are not provided in the Book of Contracts in the Civil Code. Observing the experience of German law, we may note that before the German Civil Code explicitly stipulates general rules for termination for compelling reasons in the general part of the law of obligations, German law mainly achieved the generalization of this rule through two juridical methods: overall analogy and concretizing the principle of good faith. Therefore, this paper will examine the theoretical and normative foundations for establishing general rules for termination for compelling reasons in the Civil Code using these two juridical methods and analyze the potential challenges and response strategies.

2. Theoretical Basis and Object Examination of Overall Analogy

2.1. Theoretical Basis of Overall Analogy

The application of analogy, that is, dealing with the same matters in the same way, is a justice requirement in implementing the principle of equality (Larenz, 2003). Through comparative law, we observe that countries such as Germany, Austria, Italy, and Russia all explicitly designate analogy as a source of law in their civil codes, with effectiveness second only to statutes and customs, taking precedence over other supplementary sources of law. Although the Civil Code of China does not explicitly set forth analogy as a source of law, judicial practice and prevailing academic theories recognize the validity of filling legal gaps through analogical reasoning (Wang, 2009).

Before Article 314 of the German Civil Code expressly stipulated the general rule of termination for compelling reasons, German scholars initially derived the general principle of termination for compelling reasons from specific rules governing the termination of continuing contracts using the method of overall

analogy. Overall analogy, as a method of applying analogy, refers to the process of deducing general legal principles from legal provisions that assign the same legal effects to different constituent requirements. Professor Larenz summarized this induction process as follows: First, for contracts such as leases, the law grants parties the right to terminate contracts for special reasons, which often relate to the loss of trust between the parties; Second, the aforementioned contracts are all of the type of continuing contracts; Third, a continuing contract refers to a legal relationship in which the parties are continuously and extensively involved in the lives of the parties in the long run, resulting in a close interweaving of interests between the parties, and the parties thereby attach great importance to cooperation, goodwill, and trust; Fourth, based on these characteristics of continuing contracts, the law stipulates the termination of contracts due to the breakdown of trust; Fifth, consequently, the statutory reasons based on the breakdown of trust can be applied to all kinds of continuing contracts and become a general legal principle (Larenz, 2003).

Most Chinese scholars agree to extract the general rule of termination for compelling reasons from the Civil Code through the method of overall analogy (Wang, 2020).

However, there are also scholars expressing concerns, citing the relative lack of objects suitable for overall analogy in the Civil Code. Therefore, it is necessary to conduct a comprehensive examination of the norms containing the idea of termination for compelling reasons in China's current civil legislation.

2.2. Examining Objects of Overall Analogy

1) By applying interpretation *econtrario* to Article 899(2) of the Civil Code, it is understood that a custodian may terminate a custody contract prematurely in the presence of a special cause. Custody contracts are typical continuing contracts; that they use "special cause" as selection criteria for both individual and overall analogies is not contradicted within civil law academia.

2) Article 1022(2) of the Civil Code stipulates that a person holding the right to likeness may terminate a contract authorizing the use of the image with just cause, provided that the other party is notified within a reasonable period of time and compensation is paid. Since a contract authorizing the use of the image is a continuing contract, the term "just cause" here can be interpreted as compelling reasons. Therefore, many scholars propose that this provision can serve as a selection criterion for overall analogy (Han, 2020). Regarding this reasoning of analogy, opponents argue that: Firstly, the "just cause" in this provision includes the circumstance of "change of inner conception," which falls within the scope of the risks on the side of the person holding the right to likeness, whereas compelling reasons typically stem from the risk domain of the counterparty and do not fall within the responsibility scope of the terminating party. Secondly, from the teleological perspective, this provision aims to safeguard the right holder's freedom of personality development and dignity from infringement,

which differs significantly from the purpose of the rule allowing termination for compelling reasons, which aims to resolve contract deadlocks. It is not appropriate to hastily draw analogies. In this paper, it is believed that, firstly, compelling reasons are not limited to the risk domain of the counterparty because the risk domain is only one of the factors to consider when determining whether compelling reasons exist. The key for judgment lies in “examining all specific circumstances of the case and weighing the interests of both parties, thereby concluding that there is no reasonable expectation for the terminating party to continue the contractual relationship”. Secondly, in terms of the purpose of the provision, although this article aims to protect the right holder’s freedom of personality development and dignity from infringement, it does not conflict with the normative purpose of termination for compelling reasons. In fact, it is precisely because the counterparty’s use of the likeness does not align with their expectations that the person holding the right to likeness opts to terminate the contract. The counterparty’s act might not constitute a breach but can lead to the loss of the right holder’s reasonable expectation of continuing to perform the contract and a desire to be released from the contractual obligation, which aligns perfectly with the principle of termination for compelling reasons. Therefore, this rule can serve as a selection criterion for overall analogy.

3) Teleological reduction of the discretionary termination right in entrustment contracts stipulated by Article 933 of the Civil Code. There has been considerable controversy in civil law academia regarding the legislative purpose and legitimacy of the rules concerning discretionary termination rights. Some scholars argue that the primary consideration of the legislator is that contracts are typically established for the benefit of the principal alone, with the other party having only monetary interests. Therefore, the principal can, without any justification, terminate the contract without being bound by it, provided compensation is made for the losses of the other party (Cui, 2016). Regarding the aforementioned rationale, it is pointed out that it is not always well grounded. For one thing, entrustment contracts do not necessarily solely concern the interests of the principal; the agent may also benefit from performing the entrusted tasks. For instance, professional agents equally value the maintenance of their brand and reputation (Lv, 2006). For another, the agent’s interests cannot be fully compensated in every circumstance. When the agent simultaneously benefits from handling the entrusted matters, the losses incurred by it due to the principal’s termination are uncertain (Wu, 2018). Consequently, the discretionary termination rules in entrustment contracts can lead to an imbalance of interests between the principal and the agent in its application.

To address the said issues, scholars have proposed various approaches to restrict the application scope of the rules for discretionary termination rights. One approach is to differentiate between civil and commercial entrustment and confine the application of discretionary termination to civil entrustment. Another approach is to introduce measuring factors for comprehensive judgment. Scho-

lars holding this view also have different opinions in terms of the specific designs. One viewpoint holds that the core characteristic of discretionary termination rights is that it can be exercised without reason, and the substantive judgment by introducing measuring factors would compromise this rule. Therefore, Article 933 of the Civil Code should be subject to teleological restriction. Its application scope should be restricted to situations where no “agent interests” is involved. Measuring factors should be removed from discretionary termination rules and handled through the system of continuing contracts termination for compelling reasons (Wu, 2018). Another viewpoint opines that Article 933 of the Civil Code can be directly interpreted as a rule for terminating contracts for compelling reasons through teleological reduction. This view is based on the idea that only by conditioning termination upon compelling reasons and imposing liability for damages as a cost for being freed from a contract bound can a balance of interests between the contacting parties be achieved (Wang, 2020). The author believes that the first viewpoint involves a detour in handling the issue. For situations where no agent interests are involved, terminating the contract for compelling reasons can also protect the principal’s right to be released from the contract, and a balance of interests between the parties can be achieved through compensation for damages. Therefore, it is preferable to directly reduce Article 933 of the Civil Code as “allowing the parties to an entrustment contract to terminate the contract and assume corresponding liability for contractual breach when they no longer have reasonable expectation for continuing performing the contract as a result of compelling reasons”. Based on the above, Article 933 of the Civil Code, through teleological reduction, can serve as a selection criterion for overall analogy in applying the rule of termination for compelling reasons.

4) Another contentious issue is whether the provisions regarding divorce are objects for analogy. Supporters argue that since there is no rule for termination for compelling reasons governing lease contracts, the rules for granting divorce due to no longer existing mutual affection as stipulated by Para. 2, Article 1079 of the Civil Code may be analogically applied to contracts such as leases, which are based on trust. The reason is that continuing contracts, which emphasize the maintenance of trust, are very similar to marital relationships. A fundamental breach in contractual relationships is akin to infidelity in marital relationships. Factors causing a couple’s loss of affection are rather complex and not limited to severe events like infidelity. This same truth applies to continuing contractual relationships, where the trust between the parties may not be only caused by fundamental breaches, thus necessitating additional grounds for termination (Peng, 2022). The rationale for this viewpoint lies in the fact that marital relationships also involve a binding future agreement affecting the continuous long-term relationship. The gradual relaxation of divorce grounds can also be seen as an example of the diminishing binding force of future agreements (Atiyah, 2022). In contrast, opposing views argue that marriage concerns identi-

ty relations with strong ethical implications. Therefore, it is fundamentally different from the contract law, which deals with property relationships. Moreover, given the long-standing independence of the marriage law from the civil law system in our country, analogical application of divorce provisions carries significant uncertainty and is difficult to achieve the desired adjudication effect (Han, 2020).

This paper argues that at the current stage, it is indeed inappropriate to consider divorce rules as an object of overall analogy for rules on termination for compelling reasons. Apart from the obvious differences in identity and property relationships mentioned above, upon reexamination of the rules for terminating lease contracts, it may be noted that Article 711 of the Civil Code stipulates that a lessee shall use the leased object in a manner as agreed by the parties or in line with its nature; otherwise, the lessor may terminate the contract and request for compensation. Article 716(2) of the Civil Code provides that the lessee shall obtain the lessor's consent to sublease the property; otherwise, the lessor may terminate the contract. It is generally believed that the behaviors of not using the leased object in the agreed-upon manner or subleasing the property are not serious enough to fail the lessor's contractual purpose. Therefore, it can be seen that the above rules are not a specific manifestation of the general rules for statutory termination in the Civil Code in typical contracts. The rationale behind the law granting the lessor the right to terminate lies precisely in the idea of termination for compelling reasons. That is, although the lessee's behavior may not amount to a fundamental breach, it still undermines the trust between the parties, which is fundamental for maintaining relationships in lease contracts, which are continuing contracts. Besides the aforementioned rules, there are similar considerations behind the design of regulations such as Article 729, Article 756, and Article 857 of the Civil Code. In conclusion, it is worth noting that the Civil Code already provides sufficient objects for analogy, and to avoid further complicating the interpretation task, there is no need to analogically apply the rules regarding divorce in Article 1079(2) of the Civil Code.

5) In addition to the Civil Code, legal provisions dealing with issues similar to termination for compelling reasons are dispersed across special civil legislations. For instance, Article 45(3) of the Partnership Enterprise Law stipulates that partners may withdraw from the partnership on the grounds which make it difficult to continue to participate in the partnership. Similarly, Article 182 of the Company Law provides where a company faces difficulty in operations, the shareholders representing more than 10% of the voting rights of all the shareholders of the company may file a request with the competent people's court to dissolve the company. On this basis, Article 1 of the Judicial Interpretation II of the Company Law further delineates circumstances of severe operational difficulties for companies. These rules can also serve as objects for the overall analogy of rules concerning termination for compelling reasons.

In summary, a sufficient number of rules for terminating typical continuing

contracts exist within China's Civil Code and other civil legislations. These rules embody the concept of termination for compelling reasons. Through them, we can extract general principles for termination for compelling reasons by means of overall analogy.

3. Theoretical Basis and Feasibility of Concretizing the Principle of Good Faith

Another approach to generalize the rule of termination for compelling reasons is to “concretize the principle of good faith”, which also originated from case precedents prior to the reform of the German law of obligations. Examining the development history of the German system of termination for compelling reasons, in the absence of general clauses, the German federal courts applied the principle of good faith to prevent placing one party in a difficult position due to the unexpected continued performance of a contract. However, whether experiences from comparative law can be applied to China's Civil Code requires analysis of its theoretical basis and feasibility.

3.1. Theoretical Basis of Concretizing the Principle of Good Faith

Source of law in civil law typically refers to the forms of existence of civil law (Wang, 2009). From the perspective of judicial decisions and adjudication by judges, the source of law is “a generic term referring to all norms that can serve as the major premises for adjudication” (Zhu, 2016). The essence of provisions on the source of law in civil law is providing guidance to civil law judges in finding bases for their judgments (Yu, 2018). China's Civil Code establishes a two-tier “law-custom” source of law system in Article 10, while the basic principles of civil law are not delineated as a source of law.

The limitations of the two-tier “law-custom” source of law system primarily lie in its inability to overcome the inherent untimeliness and inadequacy of empirical law when adjusting the evolving social relations (Xu, 2013). Article 10 of the Civil Code fails to answer the question of what judges should do in the absence of relevant empirical law, thereby making it impossible to realize the concept of “judges shall not refuse to render judgement” (Rüthers et al., 2013). For this reason, it is necessary to introduce a third-tier source of law as a supplement. The legitimacy of delineating the basic principles of civil law as the third-tier source of law lies in two aspects. First, there are numerous legislative examples in comparative law that incorporate principles into the source of law.¹ Second, basic principles are explicitly stipulated in legal documents formulated by various authoritative bodies, and judges also utilize principles as adjudication reasons in the process of legal reasoning. Setting forth basic principles as a source of law possesses both authoritative and substantive justifications (Yu, 2018).

It is to be emphasized that, to limit uncertainty in applying abstract principles,

¹Such as Article 12 of the Italian Civil Code; Article 1 of the Romanian Civil Code; Article 7 of CISG.

during the process of filling legal gaps through basic principles, it is the “rule” established based on basic principles that serves as a source of law, not the basic principles themselves (Yu, 2018). This process is termed as “concretization of legal principles”, which involves four stages: determining the applicable legal principle, identifying the subordinate principles of the principle, establishing new rules based on the principle, and judges interpreting the new rules established based on the principle according to the specific circumstances of a case in individual adjudication, ultimately formulating norms for individual case (Larenz, 2003).

3.2. Feasibility of Deriving the Rule of Termination for Compelling Reasons from the Principle of Good Faith

In this paper, it is argued that concretizing the principle of good faith is a viable approach to achieving the generalization of the rule of termination for compelling reasons. At the normative level, Article 7 of China’s Civil Code clearly stipulates the principle of good faith, which by no means merely declarative. In a continuing contract deadlock, freeing the debtor who has lost reasonable expectations of continuing performance from the contractual obligation and restoring the balance of the parties’ interests through compensation for damages is precisely where this principle should be applied.

In its Article 48, the Minutes of the National Courts’ Civil and Commercial Trial Work Conference regulates the deadlock issues commonly seen in practice concerning continuing contracts such as leases of houses. Examining the wording of the three legal requirements stipulated in this provision, namely, “without malicious intent”, “obviously unfair”, and “good faith”, it is evident that rich notions of good faith are embedded within this article. In judicial practice, some courts have also upheld parties to continuing contracts in terminating the contract by applying the principle of good faith when they have lost reasonable expectations on continuing performance due to compelling reasons.²

4. Challenges in the Application of the Two General Methods and Solutions

4.1. Challenges in Applying the Two General Methods

As mentioned earlier, both approaches, overall analogy and concretizing the principle of good faith, have their theoretical foundations and feasibility in establishing general rules governing termination for compelling reasons in the Civil Code. However, this does not imply that there are no challenges in their application.

Undeniably, the principle of good faith embodies significant abstraction and instability, leading inevitably to great uncertainty in the application of the law and improper expansion of judges’ discretionary power. The principle of good faith should be concretized into specific norms for individual cases before appli-

²Civil Judgement (2023) Gui 1221 Min Chu No. 1107.

cation. Nevertheless, there has been a lack of methodological consciousness in China's judiciary regarding how to specify this principle into norms. Since legal principles do not define specific rights, obligations, and legal consequences, it is inappropriate to directly invoke them as the basis for judgments without rigorous legal reasoning and argumentation. Otherwise, this could result in a loss of methodological verifiability in judicial judgments and lead to a lack of objectivity and certainty in court rulings (Peng, 2018).

In comparison, the overall analogy method demonstrates more certainty, which is manifested as follows. Firstly, certainty in the acquisition of rules. Analogy generates a new rule based on existing rules, and the certainty and reliability of this process surpass other methods of gap filling. Secondly, appropriateness in the acquisition of rules. Existing statutory rules contain legal evaluations that have been legislatively confirmed. The legitimacy of analogy is precisely rooted in these existing legal evaluations, and its function lies in maintaining these legal evaluations in similar fields that the law initially fails to regulate (Yu, 2018). Therefore, based on considerations of certainty, the approach of overall analogy should be preferred as a method for achieving the generalization of rules governing the termination for compelling reasons.

However, despite the recognition of overall analogy as preferable due to its relative certainty, achieving the generalization of rules regulating termination for compelling reasons using this method remains quite challenging at the current stage. This is because the application of this legal method necessitates a relatively high level of general professional competence among judges. Presently, some judges find it challenging to clearly articulate the process of overall analogy in their adjudication reasoning. This problem also extends to concretizing the principle of good faith.

4.2. Achieving Generalization through Guiding Cases Issued by the Supreme People's Court

Observing the development of rules regulating termination for compelling reasons in German law, we note that before legislations explicitly stipulated them, the Federal Court of Justice first applied the rule of termination for compelling reasons in case precedents. This, together with the support of legal doctrines, prompted legislators to eventually accept the rules developed from these precedents and legal doctrines (Yu, 2018).

From this perspective, the derivation of general rules concerning termination for compelling reasons necessitates relevant case precedents, particularly support from guiding cases issued by the Supreme People's Court. In 2010, the Supreme People's Court issued the Provisions on Case Guidance, which marked the establishment of China's guiding case system. Article 7 specifies that lower-level courts should refer to the guiding cases issued by the Supreme People's Court when adjudicating similar cases. The use of the phrase "should refer to" has prompted considerable doubts in academia regarding the nature of guiding cas-

es. In 2015, the Supreme Court issued the Detailed Rules for the Implementation of the Provisions on Case Guidance, which denies the status of guiding cases as a source of law. This paper refrains from engaging in the debate on the nature of guiding cases because the rules governing termination for compelling reasons can be discerned through overall analogy and the concretization of the principle of good faith. What needs to be emphasized here is that guiding cases help improve judges' ability to "find the law". Currently, the best method to promote the establishment of stable precedents for rules regarding compelling reasons in judicial practice is through the Supreme People's Court's issuance of guiding cases. These cases should clarify the thinking process behind overall analogy, elucidate the basis and objectives of applying analogical reasoning, and provide clear guidance for judges in lower courts when adjudicating similar cases. Additionally, to achieve the goal of uniform judgments for similar cases in the rule of law, support from the theoretical realm is also necessary. Through discussions, academia should form a consensus in legal doctrine that continuing contracts can be terminated for compelling reasons and elaborate on how to establish such rules.

5. Conclusion

While both overall analogy and concretizing the principle of good faith have theoretical and normative foundations in establishing general rules regulating termination for compelling reasons, their application also places relatively high demands on judges' reasoning abilities. Currently, the most effective approach is through the Supreme Court's issuance of guiding cases that clarify the process of overall analogy in applying rules on compelling reasons in their adjudication reasoning, thereby enhancing the accuracy of adjudication reasoning. By establishing stable precedents, a foundation can be laid for supplementing rules for termination due to compelling reasons in the general provisions of the Book of Contracts in the Civil Code in the future.

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The author declares no conflicts of interest regarding the publication of this paper.

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