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Incorporation Control of Standard Terms: The Approaches of Chinese Civil Code

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Abstract: With the advantages of governing an enormous range of transactions and improving the efficiency, standard terms are increasingly being applied to commercial transactions nowadays. The standard terms refer to the non-negotiated terms presented to consumers on a take-it-or-leave-it basis and the incorporation control refers to whether the standard terms can become a part of the contract. In this paper, the author adopts the article analysis method, the comparative study method and the case analysis method to interpret the Chinese latest legislation on the incorporation control of standard terms. According to Article 496(2) of the Civil Code of the People's Republic of China, the incorporation control includes following five elements: (1) determining rights and obligations in accordance with the principle of fairness, (2) the provider's obligation of calling attention, (3) the provider's obligation of giving explanations, (4) the commitment of the counterparty, (5) the legal effect of violating the incorporation control.

Keywords: Standard terms, Incorporation control, Chinese Civil Code

1. Introduction

The standard terms refer to the non-negotiated terms presented to consumers on a take-it-or-leave-it basis, which govern an enormous range of transactions and make consumers unable to bargain effectively [1]. Regarding to the incorporation of standard terms into contracts, there have been different regulations worldwide. In the American Law Institute's Restatement of Consumer Contract, Section 2(a) provides the "pre-assent review" model and Section 2(b) provides the "post-assent review" model [2]. In the Unfair Contract Terms Directive of the European Union, the incorporation is limited to a transparency requirement in Article 4 and 5 [3]. In the German Civil Code, Section 305 provides the general rule of incorporation and Sections 305a through 305c modify the general rule for special cases, individually negotiated terms and surprising and ambiguous terms [4].

In China, Civil Code of the People's Republic of China (hereinafter referred to as Civil Code) came into effect on 1st January 2021 with new provisions on incorporation control and the Interpretation by the Supreme People's Court of Several Issues Concerning the Application of Title One General Provisions of Book Three Contracts of the Civil Code of the People's Republic of China (hereinafter referred to as Interpretation) came into effect on 5th December 2023 with more detailed provisions on incorporation control. In this paper, the author adopts the article analysis method to interpret the provisions of the Civil Code and the Interpretation, adopts the comparative study method

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to consult the foreign legislation such as the German Civil Code and Draft Common Frame of Reference (hereinafter referred to as DCFR), and adopts the case analysis method to research on the judicial practice by the precedents of the Supreme Court and high courts in recent years, aiming to fill the gap in the interpretation of latest Chinese legislation on the incorporation of standard terms.

2. Chinese Legislation on Standard Terms

The judicial control process of standard terms is as follows.

The first step is to determine whether the disputed term is a standard term according to the definition in Article 496(1). Article 496(1) stipulates three constituent elements of standard terms. First, "for the purpose of repeated use". According to Article 9(2) of the Interpretation, it should be interpreted as the purpose for repeated use rather than being actually reused; Second, "formulated in advance". Third, "has not been negotiated with the other party when concluding the contract", which should be interpreted as the possibility of substantive negotiation [5].

The second step is to determine whether the standard term can become part of the contract according to the incorporation control in Article 496(2), which will be discussed in detail in the following paper.

The third step is to interpret the standard term according to the rules in Article 498, which stipulates that the term shall be interpreted in accordance with its common understanding and be interpreted in a manner unfavorable to the provider if there are multiple interpretations.

The fourth step is to judge whether the standard term is valid according to the content control in Article 497, which stipulates three invalid circumstances. First, the clause is invalid according to Article 506 of the Civil Code; Second, the provider unreasonably exempts or alleviates himself from the liability, imposes heavier liability on the other party, or restricts the main rights of the counterparty; Third, the provider deprives the counterparty of his main rights.

3. Incorporation Control of Standard Terms

According to Article 496(2), the incorporation control includes five elements: (1) determining rights and obligations in accordance with the principle of fairness, (2) the provider's obligation of calling attention, (3) the provider's obligation of giving explanations, (4) the commitment of the counterparty, (5) the legal effect of violating the incorporation control.

3.1. The Principle of Fairness

Scholars generally believe that determining rights and obligations in accordance with the principle of fairness is not a requirement for incorporation, but rather a rule of effectiveness. Because if the fairness of the standard terms is reviewed during the formation of a contract, it will lead to a conflict between incorporation control in Article 496(2) and the content control in Article 497. Therefore, it should be regarded as an advocacy rather than a substantive element [6].

3.2. Provider's Obligation of Calling Attention

3.2.1. The Scope of the obligation

According to Article 496 (2), the scope indicated by the provider of standard terms is "the clause concerning the other party's major interests and concerns". It can be seen that unlike Article 305 of the German Civil Code, Article II-9:103 (1) of DCFR, and Article 1341 of the Italian Civil Code, which define the scope as all standard terms in the contract, the scope of obligation in Chinese Civil Code is regarded as "partial regulation" [7]. Partial regulation can highlight the terms that the

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counterparty truly need to pay attention to, improve transaction efficiency, and reduce excessive intervention in contracts, but it also raises the issue of determining the exact scope.

Due to the lack of further explanation in Article 496 (2), the determination of the scope of obligation in practice is relatively confusing. In the court's judgments, it is often only based on whether the term exempts or alleviates the liability of the provider to determine whether the obligation exists, referring to the Supreme Court's judgment of (2017) Zui Gao Fa Min Zhong No.152 and the Supreme Court's judgment of (2017) Zui Gao Fa Min Shen No.72.

In response to this, the Interpretation provides a clearer explanation of the scope of obligation. In Article 10(1), it is refined as "abnormal clauses concerning the other party's major interests and concerns". The so-called abnormal clauses refer to clauses that are not foreseeable by the counterparty based on the normal circumstances of the transaction [8]. Some argue that abnormal clauses can be further distinguished into abnormal clauses in form and abnormal clauses in content [7]. Abnormal clauses in form refer to clauses with abnormal expression, which make it difficult for the counterparty to pay attention to due to their external form, such as placing them in the corner or in the back of the contract, or using smaller fonts. Abnormal clauses in content refer to clauses where the content deviates significantly from arbitrary norms, and the counterparty often do not review them based on the experience. Due to the fact that people would not enter into the contract if they were aware of abnormal clauses at the time of contract formation, it is necessary to call attention for abnormal clauses [9].

In addition, Article 10(1) also uses "excluding or limiting the liability" and "excluding or limiting the rights" as examples. Firstly, clauses that exclude or limit the liability of the provider, such as deductible clauses in insurance contracts, age limitation clauses in amusement parks, and breach of contract clauses that exclude or limit the liability of the defaulting party. Secondly, clauses that exclude or limit the rights of the counterparty, such as restrictions on compensation for defects in sales contract, prohibitions on entrusting multiple intermediaries in intermediary contracts, and prohibitions on reverse engineering in the field of intellectual property. Thirdly, in addition to the above two examples, some argue that clauses that increase the liability of the counterparty also belong to "abnormal clauses" and it should be understood as obligations that the counterparty should not bear according to normal trade practices, such as punitive interest clauses in loan contracts, compensation for damages to leased property in lease contracts, seat fees in catering, and breach of contract clauses that increase the counterparty's liability [10]. However, industry practices should be excluded from the clauses that increase the liability, such as clauses that require payment or confiscation of margin [11].

In legislation of other countries and regions, the exclusion rule for abnormal clauses is also a common practice. As stipulated in Article 305c(1) of the German Civil Code, surprising and ambiguous clauses "do not form part of the contract". As stipulated in Article 864a of the Austrian Civil Code, provisions of unusual content "do not become part of the contract if they are disadvantageous to the other party and the other party did not have to expect them". As stipulated in Article 14 of the Consumer Protection Law of Taiwan, "if a standardized contract is not recorded in a standardized contract and is not foreseeable by the consumer under normal circumstances, this clause does not constitute the content of the contract".

3.2.2. The Performance of the Obligation

Regarding the performance of the obligation, Article 496(2) only states "in a reasonable manner". In response to this, Article 10(1) of the Interpretation further refines it to "by using writing, a symbol, a font, or any other conspicuous sign that is ordinarily sufficient to attract the attention of the other party when entering into the contract".

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In academia, the performance of the obligation of calling attention is usually considered from the following aspects:

Firstly, in terms of the appearance, calling attention should make the counterparty aware that the text contains terms that affect the major interests and concerns, otherwise the counterparty cannot be expected to read it [6,9]. For instance, if the text belongs to a contract, it should include words such as “contract” or “attention”, rather than appearing in the form of a receipt.

Secondly, in terms of the language, the language should be clear, so that the ordinary people can understand them [6,12]. In foreign legislation, similarly, Article II-9:402 (1) of the DCFR requires that “they are drafted and communicated in plain, intelligible language”.

Thirdly, in terms of the methods, the principle of individual reminders should be followed, with the exception of public announcement [6,12]. For restaurants and supermarkets with high foot traffic, as well as “one to many” contracts on large online platforms, if it is difficult for providers to make individual reminders, they can use other methods such as broadcasting and posting public notice to call attention. In foreign legislation, similarly, Article 305(2) of the German Civil Code provides that reminders can be made through public announcement in situations with disproportionate difficulty.

Fourthly, in terms of the time, it should be done before or during the formation of the contract [6,9]. For example, when registering applications on mobile phones, users are often required to open the protocols and forcibly stay for a certain period of time. In foreign legislation, Article 2:104 (1) of the European Principles of Contract Law also stipulates that “bring them to the other party’s attention before or when the contract was concluded”.

Fifthly, in terms of the extent, it must be prominent and sufficient to attract the attention of the counterparty, which is now stipulated in Article 10 (1) [6,9]. In judicial practice, judges usually determine the performance of the obligation based on whether the providers have changed the font, size, color, or added symbols, referring to Supreme Court’s judgment of (2021) Zui Gao Fa Min Zai No.24, Sichuan Higher Court’s judgment of (2021) Chuan Min Zai No. 15, Jiangsu Higher Court’s judgment of (2020) Su Min Shen No. 1403, and Fujian Higher Court’s judgment of (2020) Min Min Shen No. 2161. However, for those who only use bold and black font in situations where there are too many bold and black fonts and the text is long and compact, it is often not recognized that they can be clearly distinguished from other clauses, referring to Changzhou Intermediate Court’s judgment of (2021) Su 04 Min Xia Zhong No.248 and Shenzhen Intermediate Court’s judgment of (2016) Yue 03 Min Zai No.94. In addition, Article 10(3) of the Interpretation adds a new provision on the obligation of calling attention of electronic contracts. “In the case of an electronic contract entered into on the Internet or any other information network, if the party providing the standard terms claims to have performed its obligation of calling attention or providing explanations only on the grounds of using a checkbox, a pop-up window, or any other means, the people's court shall not uphold the claim unless the party providing the standard terms adduces evidence of compliance with the provisions of the preceding two paragraphs.”

3.3. Provider’s Obligation of giving explanations

According to Article 496 (2), the provider of standard clauses shall “give explanations of such clause upon request of the other party”. Unlike the obligation of calling attention, scholars generally believe that the obligation of giving explanations belongs to a passive obligation, that is, the provider only has the obligation of giving explanations when the counterparty makes a request [6,12,13].

The Article 10(2) of the Interpretation also provides detailed provisions on the obligation of explanations. “If the party providing the standard terms, at the request of the other party, provides a generally understandable explanation in writing or orally regarding the concept, content, and legal consequences of abnormal clauses with major interests and concerns to the other party, the people's court may determine that it has performed the obligation of giving explanations stipulated in the

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Article 496(2) of the Civil Code." According to the Interpretation, the scope of the obligation of giving explanation is the same as the scope of the obligation of calling attention, see the above "abnormal clauses with major interests and concerns"; The content of the obligation includes the concept, content, and legal consequences of the terms; The form of obligation can be oral or written; The degree of the obligation adopts an objective standard, which is to judge the performance of the obligation based on whether it has reached the understanding level of ordinary people, without the need to meet the subjective standard to make the specific counterparty understood [14].

However, in practice, the counterparty may not have the means to request explanations. For instance, the counterparty of electronic contracts concluded online often lack channels to request explanations from the provider, while the provider can easily use the counterparty's failure of request as a defense when the dispute arise. In this case, some suggest that the "obligation of giving information" should be added as a supplementary obligation to the obligation of giving explanations, which means that the provider should have an obligation to inform the counterparty of important facts that may hinder the achievement of the contracting purpose [11]. It can be performed by attaching corresponding explanations in the paper contract, or setting up a link to jump to the corresponding explanations in the electronic contract [11].

3.4. Counterparty's Commitment

Article 496 (2) does not include the counterparty's commitment as part of the incorporation control, while scholars generally believe that standard terms should follow the general rules of contract formation-reaching agreement through the provider's offer and the counterparty's commitment. Similarly, Article 305(2) of the German Civil Code requires the counterparty to agree to the applying of the terms and Article 13 of the Consumer Protection Law of Taiwan also stipulates that "the clause is the content of the contract if the consumer agrees to be bound by it".

As for the form of commitment, some judges have ruled that implied commitment represented by the acceptance of goods or services cannot be regarded as the counterparty's commitment, referring to Beijing Higher Court's judgment of (2016) Jing Min Zai No.28. However, scholars generally acknowledge both the explicit way and the implied way of making the commitment, but the commitment should be subject to certain limitations, such as the premise that the provider has performed the obligation of calling attention and giving explanations [6,9].

3.5. Legal Effects of Violating the Incorporation Control

3.5.1. Validity of Standard Terms

Scholars believe that the validity of standard terms that violate the incorporation control includes three perspectives: "revocable", "invalid", and "not established", which fall within the semantic scope of "not become part of the contract" in Article 496(2), and therefore need to be discussed separately [9]. For the perspective of "revocable", the prerequisite for revocation is that the legal act is established and valid, while the standard term without attention or explanations has not yet been included in the contract and the exercise of revocation right has a statute of repose, which is not conducive to the protection of the counterparty; For the perspective of "invalid", invalidity is a value judgment after the establishment of a legal act, while standard term without attention or explanations has not yet been included in the contract and the provider's claim of invalidity can result in the deprivation of the counterparty's right to continue performing the terms. Therefore, the interpretation of "revocable" and "invalid" is not reasonable in terms of legal principles and the protection of the counterparty.

Considering that the counterparty has not made a commitment to the clause without attention or explanations and both parties cannot reach an agreement on it, therefore, it is more appropriate to

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interpret “not become part of the contract” in Article 496(2) as “not established” [11]. On the other hand, according to Article 496 (2), violating the incorporation control does not necessarily mean that the standard term does not become part of the contract, so the effect of “not established” requires the counterparty to make a claim. As there is no time limit for the counterparty to make a claim, it ensures the counterparty’s right to independently decide whether to continue performing the term, thus protecting the counterparty’s interests [7].

3.5.2. Validity of the Remainder of the Contract

Regarding the impact of the failure to establish a standard term that violates the incorporation control, scholars generally believe that the validity of the remainder of the contract is still valid in principle. There is a viewpoint that only when the contract is fully performed can the counterparty achieve its expected contracting purpose, so negating the validity of the entire contract will further harm the counterparty’s interests [11]. Therefore, as long as the contract composed of the remaining terms can continue to be performed and the contracting purpose can still be achieved, the contract should be recognized as still valid. There is also a viewpoint that although the standard term that violates the incorporation control is not “invalid”, the effect caused by “not established” and “invalid” is similar. Therefore, Article 156 of the Civil Code can be applied, which states that “if invalidation of a part of a civil juristic act does not affect the validity of the other part, the other part of the act remains valid” [7].

In foreign legislation, similarly, Article 306 (2) of the German Civil Code stipulates that “the remainder of the contract will remain in effect” and Article II-9:408 (2) of the DCFR also stipulates that “the other terms remain binding on the parties”.

4. Conclusion

According to Article 496(2) of the Chinese Civil Code, the incorporation control contains five elements. First, to determine rights and obligations in accordance with the principle of fairness, but it should be interpreted as an advocacy and not as a substantive element. Second, the provider’s obligation of calling attention for “abnormal clauses with major interests and concerns”. The “abnormal clauses” include abnormal clauses in form and abnormal clauses in content and the “major interests and concerns” include excluding or limiting the liability of the provider, excluding or limiting the rights of the counterparty, and increasing the liability of the counterparty. The performance of the obligation of calling attention usually requires the appearance of a contract, clear language, individual reminders in principle and public announcement as exceptions, being performed before or during the formation process, and being prominent and sufficient to attract the attention of the counterparty. Third, the provider’s obligation of giving explanations is based on the request of the counterparty. The scope of explanation is “abnormal clauses with major interests and concerns”; The content of explanation includes the concept, content, and legal consequences of the term; The form of explanation is oral or written; The standard of explanation is the understanding level of ordinary people rather than the specific counterparty. Fourth, the commitment of the counterparty. Although lacking corresponding legal provisions, it has been widely regarded as part of incorporation control in academia and judicial practice. Fifth, the legal effect of violating incorporation control should be interpreted as “not established”, while the legal effect of the remainder of the contract should be interpreted as “valid” in principle.

In summary, this paper fills the gap in the interpretation of latest Chinese legislation on the incorporation control of standard terms, helping to protect the interests of the counterparties of the standard terms. However, this paper is limited to the discussion of incorporation control, and future research can be extended to the field of content control.

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