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Taiwan Contract Law

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1. The Background, Style and Type of Contracts in Taiwan.

This section discusses issues arising from Taiwan's separate formulation of the Civil and Commercial Law systems and thus is fundamental to all contract law and theory on the island. Taiwan's Civil Law System does not have a distinct "Contract Law". Instead, the new overarching Property Law spreads contract law considerations over three sections: general principles of civil law, obligations, and property law. Articles concerning obligations appear throughout Taiwan's Civil Code. All such articles are based on abstract contract theories and civil codes, rather than in case law, as in Anglo-American legal system. The second chapter of Taiwan's Civil Code is called "Obligations", and serves as the basis for remedies arising from all obligations and torts.

Taiwan's Civil Code was promulgated in 1929. Since then, the relevant property section has been amended three times: General Principles Amendment in 1982, Obligations Amendment in 1999, and Property Amendment in 2010. The Juristic Acts (also called "Rechtsgeschäft" in German) are divided into principle, behavioral ability and declaration of intent. The development of the contract part can be classified into the following four stages:¹

1. Freedom of Contracts. The presence of a risk or uncertainty vitiates an agreement, since contracts generally allocate risks. At the same time, a "Freedom of Contract" is contained in Articles 247-1 and 166-1, both of which concern formal real estate contracts.
2. Change of Circumstances (also called "clausula rebus sic stantibus" in Latin). Where a change of circumstances that was not predictable when the contract was constituted makes the performance of the original obligations obviously unfair, the disadvantaged party may apply to the court to increase or reduce his consideration, or otherwise alter his original obligations.
3. Additional Provisions. New contract types, including a Travelling Contract

¹ Tez-chien Wang, *Rules of Obligations: 1st Volume*, pages 71-73 (Taipei, 2006).

and Third Party Guarantee, were added to the Civil Code.

4. Pre -contractual Liability. Where a contract has not been constituted but one party believes without negligence that it has been constituted, the second party is responsible for any injury caused to the first.

In the Civil Code's second part, the closest relationship with the contract law is the "Obligations" section, which is divided into two chapters. The first chapter concerns General Provisions, and is separated into six sections: sources of obligations, object of obligations, effect of obligations, plurality of creditors and debtors, transfer of obligations and extinction of obligations. The second chapter then focuses on particular kinds of obligations, and includes 27 kinds of different obligations. The relevant legislation mandates a "from the general to the particular" approach, and thus as a general rule this section applies to all kinds of obligations.² We still, however, must search for specific article rules and then general principles to deal with each issue. Compared with the Japanese and German legal provisions, Taiwan's Civil Code is voluminous and, as already noted, combines civil and commercial codes. All articles relating to a trustee broker (*de aestimato*), transportation, managers, and commission agents are legislated in the obligations chapter.³

2. What is the Influence of International Convention and Foreign Contract Law on Taiwan's System, and Should the Statute have Local Characteristics?

The increasing variety of modern economic and trade relationships has made it impossible for legislators to establish a uniform code for all types of contracts. Many articles in the Civil Code are subservient to the freedom of contract principle and are thus permissive statutes. Parties must sign an innominate contract to be bound by the relevant statutes. At the same time, the parties can

² Tez-chien Wang, *Rules of Obligations: 1st Volume*, page 60 (Taipei, 2006).

³ Tez-chien Wang, *Rules of Obligations: 1st Volume*, page 64 (Taipei, 2006).

expressly agree to exclude such statutory provisions. Based on the freedom of contracts provisions, contracts appear to be not only judicial acts,⁴ but also resources of law for both parties to apply in court. The same principles that undergird the civil-law remedies apply to the parties and contract code (*lex contractus*).

The 2010 Principles of International Commercial Contracts, composed by UNIDROIT, are intended to harmonize the law of international commercial contracts. The first edition published in 1994 was followed by a second, enlarged edition published in 2004. The most recent 2010 third edition adds a section on illegality. All three documents influence how many countries regulate obligations established by agreement (express or implied) between private parties. They have, for example, influenced the Contract Law of the People's Republic of China and the 2002 edition of the German Contract Law. The CISG has also heavily influenced the Japanese Civil Code, especially its "Obligations" section.

In short, though all countries may not be able to agree on a uniform contract code, many international commercial contract doctrines have sought to unify various contract practices. Many countries have already modified their contract laws and are increasingly using the CISG provisions. Recently, countries have also accepted that statutes will regulate parties less, and the system will be based on extant trading customs that suit a new uniform global contract custom.

As for whether a local contract law should contain local characteristics, this question must distinguish between civil and commercial contracts. With respect to civil contracts, sociological jurisprudence argues that they should be judged by local traditions and suit the local law. For commercial contracts and merchant customs, on the other hand, convenience dictates they should be specifically harmonized, since they cannot be known by legislators.

⁴ Tzu-Chiang Chen, *The Harmonization of Contract Law*, pages 249-255 (Taipei, Angle 2011).

3. The Difference between Civil and Commercial Contracts, and What is a Consumer Contract and How to Protect Consumers?

The difference between civil and commercial contracts concerns mainly whether the contracting parties are commercial manufactures and thus in a relatively equal bargaining position.⁵ This difference also recognizes that the fast-paced modern business environment makes it difficult for commercial parties to settle many of their contract terms in advance. Third, this difference appreciates that large manufactures possess additional methods to cope with risks and combat contract fraud. By way of comparison, consumer contracts, because of an asymmetrical information relationship, require greater legal attention.

On the one hand, Taiwan's Civil Code combines important civil and commercial law considerations. On the other hand, it does not include a comprehensive contract law statute. The second chapter of the Code's Obligations section refers to particular kinds of obligations. Although it regulates all kinds of contracts, the related obligations are mostly elective. As for the civil law system, the Civil Code in Taiwan does not distinguish civil and commercial contracts. It also does not cover consumer contracts, except for general principles concerning good faith. Most consumer contracts instead are regulated under the Consumer Protection Law, which was promulgated by Taiwan's Executive Yuan in 1994.

In recent years, countries have increasingly enacted new consumer protection statutes. Examples include Japan's 2000 Consumer Protection Law and the European Union's Directive on Consumer Rights. The Directive on Consumer Rights seeks to achieve a real business-to-consumer internal market, and strike the right balance between a high level of consumer protection and a competitive business environment.⁶ The developments concern mainly restrictions on

⁵ See Tzu-Chiang Chen, *Power of Agent and Manager's Right—the Combination and Separation of Civil and Commercial Codes* (Taipei, Angle 2006). Tzu-Chiang Chen, a Taiwan civil law professor, posited that the parties to a commercial contract are at the same economic and bargaining level, so it is unnecessary to protect them. Civil contracts, however, are different.

⁶ Tzu-Chiang Chen, *Modernization of Contract: the Constructions of Liability*, pages 12-13 (Taipei, Angle 2012).

consumer contracts. While most national authorities and organizations provide specific help on consumer issues, many statutes further ensure harmonization of consumer laws in areas such as information transparency, duties of disclosure, consumers' breach of good faith and standard contracts. In Taiwan, the Consumer Protection Law mandates standard contract provisions in Sub-chapter 2, provisions covering extraordinary purchases and sales in Sub-chapter 3, and regulations governing consumer information in Sub-chapter 4. In addition, the law regards protecting consumers' rights as a class-type action.

4. The Roles and Functions of Typical Contracts and How to Distinguish between Optional Rules and Compulsory Rules.

A "typical contract," also called a "nominate contract," refers to all kinds of contracts and is codified in the contract law. In the civil-law system, a typical contract is based on the obligations part and most typical contracts are particular kinds of obligations. A "typical" contract is thus a legal determination, rather than an economic or other consideration.⁷

Based on the freedom of contract principle, contracting parties must decide how to execute an agreement and what to include in it. As for the non-consideration aspects of a contract, legislators must establish rules for such provisions. In short, the so-called "typical contract" provisions seek to protect the parties' rights by eliminating arbitrary contracts that lack true agreement. The contract rules, moreover, have two functions.⁸ First, they ensure that any party can realize its right of obligation. Second, the contract law facilitates trading, enhances the parties' efficiency, and reduces the transaction costs.

The above analysis reflects that the optional rules are aimed at tightening legal loopholes and fulfilling the essential elements of a contract. Provided both

⁷ Tzu-Chiang Chen, *Content and Elimination of Contract*, pages 149-150 (Taipei, Sharing 2013).

⁸ Tez-chien Wang, *Rules of Obligations: 1st Volume*, page 79 (Taipei, 2006).

parties agree, however, they can override these optional rules. By way of contrast, any contract that violates a compulsory rule would be null and void. A right shall be exercised and a duty, for example, must be performed in good faith. This rule is the most important rule concerning good faith in Taiwan's Civil Code.

In conclusion, the freedom of contract considers both optional and compulsory rules and is based largely on the autonomy of private law.⁹

5. Contract Interpretation

1) Does the law accept the party autonomy rule?

The party autonomy rule constitutes a fundamental principle in Taiwan's Civil Code. Under private law this autonomy provides that individuals may create legal relations according to their own will.¹⁰ In Taiwan's free market economy, the Constitutional Law protects both private property and freedom of movement. The individual's freedom is realized by the autonomy of private law. For example, although Article 10 of Taiwan's Constitution protects freedom of residence and migration, the key to realizing this freedom is whether an individual may act on his or her own to form contracts, including sales, leases, and carriage agreements.

The most important part of the Obligations Law in Taiwan's Civil Code is the freedom of contract, while the Property Law's most essential part is freedom of ownership. The Taiwanese Civil Code protects people's freedom by the establishment of the autonomy of private law. Since individuals can determine their own legal relationships, moreover, they must take responsibility for their legal acts, which means the parties' trust and the safety of transactions must also be protected.¹¹

⁹ Tzu-Chiang Chen, *Content and Elimination of Contract*, pages 61-63 (Taipei, Sharing 2013).

¹⁰ Tzu-Chiang Chen, *Establishment and Execution of Contract*, pages 8-9 (Taipei, Sharing 2009).

¹¹ Tez-chien Wang, *General Provision of Civil Law: 1st Volume*, page 269 (Taipei, 2010).

2) What are the principles for contract interpretation? What is the role of transaction practices in contract interpretation?

Unlike the German Civil Law, Taiwan's Civil Code does not expressly provide basic contract interpretation principles. Nonetheless, Article 98 of Taiwan's Civil Code provides that "In the interpretation of an expression of intent, the real intention of the parties must be sought rather than the literal meaning of the words."

Although this article was stipulated for the interpretation of a party's intention, the Supreme Court has adopted this article as a basic principle for contract interpretation. Literal interpretation is the main method to interpret a contract; however, if the terms of the contract do not show the real intention of the parties or if the terms are ambiguous, the court may then look into the relevant facts and evidence to find the real intention of the parties at the time when the contract was made. This article also emphasizes that the "real intention" may be subjective, so that errors in wording do not harm the real intention of the contracting parties.¹²

In addition, the "principle of good faith", which is stipulated in Article 148 of Taiwan's Civil Code, supplements the interpretation of contracts. According to a judgment of the Supreme Court, besides the "principle of good faith," transaction practices as well as the purpose of a contract and noncompulsory rules can also be considered when seeking the parties' true meaning.

3) How are contract gaps (or loopholes) filled?

To fill contract gaps, scholars in Taiwan offer two approaches:¹³ application of non-compulsory rules and supplementary contract interpretation. If a contract falls into the category of a "typical contract" under Taiwan's Civil Law, the court can adopt the non-compulsory rules that have been stipulated by the legislature to fill such a contract's loopholes. If the contract is a non-typical contract, then

¹² Tzu-Chiang Chen, *Content and Elimination of Contract*, page 78 (Taipei, Sharing 2010).

¹³ Tez-chien Wang, *Rules of Obligations: Basic Theory and General Provisions*, page 244 (Taipei 1999).

supplementary contract interpretation is required, which means the court must fill the loophole by presuming what contractual provisions an honest and reasonable man would stipulate to achieve the purpose of the contract. The former method conforms to a stable legal system, while the latter requires a case-by-case evaluation of the contracting parties' interests while seeking the purpose of the contract and thereby fulfilling justice in particular cases.

It has been argued that courts often overlook specific contract features, and stiffly classify contracts into the typical contract category in order to apply the related non-compulsory rules stipulated in the Civil Law. This practice, however, means that court judgments do not accord with modern transaction forms.¹⁴ The courts must, therefore, classify contracts carefully, and even if the court decides that a contract is typical, before applying the non-compulsory rules, it must consider the related adequacy, efficiency, fairness, transaction practices, and comparative issues to thereby fully fulfill the contract's purpose.

6. What is the Relationship between the “Judicial Interpretation System” and the Contract Law?

Unlike Mainland China, Taiwan does not have a Judicial Interpretation system. Nevertheless, the precedents and resolutions made by the Supreme Court perform a similar function. Although these precedents and resolutions are not binding under the law, they are binding in practice. Thus, the precedents and resolutions related to contracts influence Taiwan courts' decisions on contracts.

The system of judicial precedent and resolution in Taiwan has in fact been harshly criticized. If a lower-level trial court does not follow the precedent of a higher-level court, its judgment is often reversed by the higher court, and thus some contend that the precedent system in Taiwan violates the independence of trials and decisions, as stipulated by Article 80 of Taiwan's Constitutional Law.¹⁵

¹⁴ Tzu-Chiang Chen, *Content and Elimination of Contract* (Taipei, Sharing 2010).

¹⁵ See Tzu-Yi Lin, Grand Justice of Taiwan, No.576 of Judicial Yuan Interpretation.

Furthermore, many precedents and resolutions have established requirements that exceed the statutory law, and thus courts are criticized for violating the doctrine of separation of powers which holds that only the legislature may make law. The draft of an amendment to the Court Organic Act passed in 2013 abolishes the precedent system. In the future, the Civil Grand Court Room and Criminal Grand Court Room will be established in the Supreme Court and replace the current system of judicial precedent and resolution.

7. The Relationship between Contract Law and Administrative Authorities and Public Policies

1) What is the relationship between “administrative authorities” and the contract law?

Although the autonomy of private law is a basic principle for contracts between private parties, where the parties possess unequal bargaining positions, the legislator has authorized the executive authority to interfere in the contractual terms to ensure the contract is just.

For example, Article 247-1 of Taiwan’s Civil Code¹⁶ and Article 12 of the Consumer Protection Law¹⁷ are applicable to standard form contracts and authorize executive authorities to stipulate “Mandatory Provisions to be Included

¹⁶ Taiwan Civil Law, Art. 247-1: If a contract has been constituted according to the provisions which were prepared by one of the parties for contracts of the same kind, the agreements which include the following agreements and are obviously unfair under that circumstance are void.

(1) To release or to reduce the responsibility of the party who prepared the entries of the contract.

(2) To increase the responsibility of the other party.

(3) To make the other party waive his right or to restrict the exercise of his right.

(4) Other matters gravely disadvantageous to the other party.

¹⁷ Taiwan Consumer Protection Law, Art. 12: The terms and conditions in standard contracts, which violate the principle of good faith and are conspicuously unfair to consumers, shall be null and void. Where the terms and conditions of standard contracts fall within any of the following circumstances, they shall be presumed to be unfair:

(1) Their conditions violate the principle of the equality and reciprocity;

(2) They are obviously contradictory to the legislative purport of the discretionary provisions which may be excluded by such terms and conditions; or

(3) Where the chief rights or obligations of the contract are restricted by such terms and conditions and as a result, the purpose of the contract cannot be achieved.

in and Prohibitory Provisions of a Standard Form Contract” for each kind of standard form contract. In addition, although an employment contract is considered a private contract, where an employer violates the Labor Standards Act, the competent authority may intervene between the contractual parties. For example, if an employer’s termination of an employment contract violates the Labor Standards Act, the competent authority may fine the employer.¹⁸

Controversy over limitations on private contracts imposed by executive power has arisen in recent years. Some argue that court decisions¹⁹ which regard the “Mandatory Provisions to be Included in and Prohibitory Provisions of a Standard Form Contract ” issued by the administrative agency as “legal orders” are inappropriate.²⁰ The legislators do not have the right to authorize administrative authorities to stipulate legal orders that restrict contracts between private parties.²¹

Private autonomy and freedom of contracts are at the center of people’s liberty; thus the boundary between freedom of contract and administrative control must be strict. To avoid the “visible hand” from interfering in contracts and reducing market efficiency, the freedom of contract must be a general rule, and related administrative regulation the exception.

2) What is the relationship between “public policies” and the contract law?

Regarding the relationship between national policy and freedom of contract, the “37.5% Arable Rent Reduction Act” demonstrates the competing concerns. When the “37.5% Arable Rent Reduction Act” was enacted, Taiwan was still a society based on farming, and agricultural development in Taiwan was hindered by an unreasonable land tenure system. The government thus enacted the “37.5%

¹⁸ Joyce Chen, *Relationship of Executive Power and Private Law*, page 12 (Lee and Li Bulletin, 2000).

¹⁹ Taiwan Consumer Protection Law, Art. 17: The competent authorities at the central government level may designate certain industries, and set forth by public notice the mandatory and prohibitory provisions of standard contracts to be used by them.

²⁰ See No. 745 Judgment of 2013, Taipei High Administrative Court.

²¹ Tzung-Jen Tsai, *Consumer Protection and Patriarchal Domination*, pages 19-47 (Taiwan Law Journal, No. 239).

Arable Rent Reduction Act” to push land reform, stabilize the security of the society, and promote economic growth by imposing restrictions on the contracts between landlords and tenant farmers.

The achievement of land reform through the enactment of the “37.5% Arable Rent Reduction Act” has become an important cornerstone of Taiwan’s industrialization. The nation has used restriction of freedom as the method to implement policy.

Furthermore, concerning the government’s role in restricting freedom of contract, the executive branch tends to emphasize fulfilling national policies and the needs of the society, while caring less about freedom of contract and justice; the judicial branch, on the other hand, generally upholds freedom of contract. The courts are unwilling to mandate contract terms for the parties, unless the law expressly requires them to do so.²²

8. How is the bona fide principle and due care of a good administrator exercised in the contract law?

1) The Bona Fide Principle.

The bona fide doctrine is stipulated expressly in Taiwan’s Civil Code, and is a general principle that covers the whole scope of the civil code. Scholars sometimes refer to the bona fide doctrine as the “emperor clause.”²³ In pursuit of substantive justice, the bona fide principle adjusts, interprets, and supplements the legal relations between the parties.

The bona fide principle is considered to have three functions. The first function is the supplementary function, which basically means to supplement the substance

²² Tsung-Fu Chen, *Limitation of Freedom of Contract: National Policy and Justice*, pages 119-165 (National Taiwan University Law Journal, Volume 32, 2002).

²³ Tsung-Fu Chen, *Effectiveness of Principle of Good Faith*, pages 119-165 (N Court Case Times, Volume 7, 2011).

of legal relations. For example, secondary obligations of performance may thus be created. The second function is to adjust the legal relations between parties that encounter a change of circumstances. The third function is the restriction and content control function, which means the bona fide principle is the boundary for exercising rights, and the interest of parties shall be compared to avoid an imbalance.²⁴

Regarding the exercise of the bona fide principle, Taiwanese courts and scholars have recognized the followings situations. First, the principle of proportionality may be considered when exercising the bona fide doctrine. It has been decided that a creditor is in violation of the bona fide principle if he or she refuses to accept goods because the debtor was delayed for 30 minutes or less.²⁵ Second, when a creditor interferes with the performance by a debtor, it may also be considered a breach of the bona fide principle, such as where a lessor refuses to collect rent and instead terminates the lease.²⁶ Third, when an obligee fails to exercise his or her rights within a reasonable period of time, it may cause the counter party to assume that the obligee will no longer exercise the right, and thus trigger the implementation of the bona fide principle, which would free the counter party from his or her obligations.²⁷ Fourth, the court must consider whether a party's exercising of its right is for the purpose of damaging the interest of others.²⁸ Fifth, Article 245-1 of the Taiwan Civil Code regulates pre-contractual duty, recognizing a clear duty to negotiate with care and not to lead a negotiating partner to act to his detriment before a firm contract is concluded.²⁹

2) The due care of a good administrator.

The Taiwan Civil Code has three levels in terms of degrees of negligence, gross

²⁴ Tez-chien Wang, *General Provision of Civil Law: 1st Volume*, page 597 (Taipei, 2011).

²⁵ See No. 69 Judgment of 1937, Shanghai High Court.

²⁶ See No. 1143 Judgment of 1954, Taiwan Supreme Court.

²⁷ See No. 950 Judgment of 2008, Taiwan Supreme Court.

²⁸ See No. 16 of Supreme Court Civil Decision in 2006.

²⁹ Tsung-Fu Chen, *Effectiveness of Principle of Good Faith*, pages 119-165 (N Court Case Times, Volume 7, 2011).

negligence, objective negligence, and subjective negligence.³⁰ If a party has subjective negligence, it means that he or she has violated the due care of a good administrator. The Taiwan court has defined a person's "violation of the due care of a good administrator" as a person "who possesses considerable knowledge and experience but fails to exercise such knowledge and experience under ordinary circumstances," where "a good administrator" could be equal to the concept of a reasonable person under the common law system.³¹ Negligence under the contract law, in principle, is objective negligence; however, the degree of duty of care may be adjusted in specific contracts. For example, the due care for gratuitous contracts is lowered to subjective negligence.³² Under a gift contract, moreover, the donor is responsible for non-performance only for a deliberate act or gross negligence.³³

The due care of a good administrator may also differ by categories of events, parties' occupation, the size of interests and risks in the contract.³⁴

9. What is the role of "standard form contracts" in the contract law?

The concept of "Standard Form Contracts" in Taiwan corresponds with the "Standard Contract Terms" in English Law, "Contract d'adhesion" in French Law, and "Allgemeine Geschäftsbedingung" in German Law.

A standard form contract is a contract where the terms and conditions are set by one of the parties, and the other party has little or no ability to negotiate more

³⁰ Cheng-eri Lin, *General Provisions of Civil Law about Obligation Part (First Half)*. Page 240-241,(Taipei 2010)

³¹ See No. 798 Judgment of 2013, Taiwan Supreme Court.

³² Taiwan Civil Law, Art. 535: The scope of the power of the mandatory is agreed by the contract of mandate, or, in the absence of such agreement, according to the nature of the affair commissioned. The principal may give to the mandatory one or several affairs for specific mandate, or he may give a general mandate for all the affairs.

³³ Taiwan Civil Law, Art. 410: The donor is responsible to be unable to perform the payment to the donee only for his intentional acts or gross negligence.

³⁴ Shang-kuan Shih, *General Provisions of Obligations*, page 112 (Taipei, 1990).

favorable terms and is thus placed in a "take it or leave it" position. These contracts have the potential to reduce transaction costs by eliminating the need to negotiate the many details of a contract each time a product is sold or a service is used. Hence, standard form contracts are now common, especially for business-to-consumer contracts. Because of the unequal bargaining power between enterprises and consumers, the contract terms often favor the party that drafted the contract and may damage the other party's rights. Consumers are in a relatively weak position, and because they lack the freedom to decide whether to enter into the particular contract, it can be considered that, in fact, the freedom of contract does not exist. To ensure that the consumers' freedom may be protected and that they thus have the freedom to choose, it's therefore necessary for a third party to draft the standard form contracts.

In Taiwan, Article 247-1 of the Civil Code and Chapter 2 of the Consumer Protection Law provide provisions relating to standard form contracts. The provisions ensure the justice of contracts under the system of freedom of contract and emphasize the principle of good faith, principle of equality and reciprocity, and a reasonable contract review period. They also require that when the contract terms are unclear, the contract must be interpreted in favor of consumers. This provision prevents the stronger parties with economic power from, in the name of freedom of contracts, distributing risks unreasonably to the weaker parties. These considerations must constantly seek a balance between the freedom of contract and justice of contracts by considering the development of contemporary society and interpreting legal provisions related to such standard form contracts.

10. What are the concepts governing default and different types of default?

1) Does the law distinguish between "obligation of results" and "obligation of means"? Is it the same between the obligation under a contract of sale and a contract of medical services?

Taiwanese law does not explicitly distinguish between “obligation of results” (French obligations de resultat) and “obligation of means” (French obligations de moyens). The distinction between the two kinds of obligation originated in France, and has been endorsed by some Taiwanese scholars. The distinction of the obligations helps specify the proof of evidence in a breach of contract. Regarding “obligation of results,” in order to be exempt from liability, a debtor must establish force majeure. Regarding “obligation of means,” on the other hand, a creditor must prove that the debtor has not met a duty of care to establish a breach of contract.

The obligation under a contract of sale is considered the typical “obligation of results,” which emphasizes the occurrence of a specific result and imposes a duty to achieve a promised result on the debtor. The obligation under a medical services contract falls into the category of “obligation of means,” which emphasizes the manner of performance. In terms of Taiwan law, under a medical service contract, a doctor is obligated to treat the patient by the standard of a reasonable professional man rather than cure the patient’s sickness.

2) Does the law accept the concept of “anticipatory repudiation”?

The Taiwanese contract law follows the civil law system and, unlike China, it does not expressly recognize “anticipatory repudiation”. Article 245-1 of the Taiwan Civil Code regulates pre-contractual duties, and is only applicable when contracts are not established after negotiation, and is not similar to “anticipatory repudiation.” There was a period of time, however, when the Obligations (Part II) of Taiwan’s Civil Code had a concept similar to anticipatory repudiation. Called “previously declared refusal of performance” or “not to perform,” it referred to a debtor before an obligation became due declaring that he or she would not perform the agreement. This concept was provided by Article 227 of Taiwan’s Civil Code before amendment of the Obligation Part. Although no longer provided for in Taiwanese law, under the circumstance of nonperformance, a concept similar to “anticipatory repudiation” is still necessary. Although creditors are

under no right to ask for performance before the obligation becomes due, the law must not restrict the parties from implementing security measures before the due date. In case a debtor has expressed clearly that he or she will not perform the contract, it would be inefficient to make a creditor wait until the obligation becomes due to take corresponding measures. In addition, during the period of time before this due date, the creditor may suffer greater damages. Taiwan needs to consider whether it is appropriate to exclude the “not to perform” concept from its Civil Law.

11. Under what circumstances may parties be exempt from liability for breach of contract?

1) Fault-based liability.

With respect to comparative law, the system of contract liability for damages can be divided into fault-based liability in civil law countries and strict liability (regardless of fault) in common law countries. The fault-based liability for contract has the same standard as torts, which means a party is only liable for deliberate or negligent acts. By way of contrast, under the strict liability regime, breaking a promise creates liability even in the absence of fault, and the remedies available to the victim are not dependent on the breaching party’s culpability; in short, as long as the contract isn’t carried out, since it constitutes a breach of contract, there is no need to determine the precise nature of non-performance.³⁵

Taiwan has adopted the fault-based principle of the civil law system. The general theory is that, unless otherwise regulated by law or agreed upon by the parties, there are three kinds of liability regarding non-performance of a contract, which are deliberate acts, negligence, and force majeure (constituting strict liability). A debtor is not in default so long as the non-performance is related to a factor for which he is not responsible. Whether the debtor is responsible depends on

³⁵ Tzu-Chiang Chen, *Modernization of Contract: the Constructions of Liability*, page 99 (Taipei, Angle 2012).

whether the debtor's exercise of precaution fell below the level required by the applicable laws for that kind of contract.

Negligence can be divided into gross negligence, subjective negligence, and objective negligence. Gross negligence has been described as "an astonishing degree of lack of skill or care." Regarding the subjective negligence, it means the debtor failed to exercise the same degree of care in performing the contract as he exercises in conducting his own affairs. Under the objective standard of negligence, the defendant is liable if he or she failed to show the degree of care expected of a reasonable person (or of a good administrator).

The normal standard of negligence that would hold a debtor liable is the "objective negligence," which means under most contracts, the debtor must exercise the degree of care to be expected of a reasonable person (or of a good administrator). For example, if a depository has exercised proper precautions, as a reasonable person would do, and the subject was still damaged by an unpredictable natural disaster, he or she is not liable for non-performance. Occasional exceptions to the objective standard established by law exist. For instance, the subjective standard applies to a depository who has undertaken the safe-keeping of another's property without reward, which means that a depository, when no benefit is received or promised as a consideration, is only required to exercise the same degree of care in performing the contract as he or she would exercise in the conduct of his or her own affairs. Thus, the obligor would not be liable for failure to live up to the standard of a reasonable person.

2) The principle of a change of circumstances.

A change of circumstances refers to when, after the constitution of a contract, direct or indirect facts upon which the contract is based have changed unpredictably and without the objective fault of either party.³⁶ Article 272-2 of the Taiwan Civil Code has expressly adopted the principle of change of

³⁶ Ying-fu You, *Civil Article about Changes of Circumstances—A New Version of Engineering Case.*, page 60 (Arbitration Journal Volume 98, 2013).

circumstances.³⁷ Pursuant to this principle, a party may apply to the court for increasing or reducing his or her payment, or altering the original obligations in the contract.

Generally, in long-term contracts, it is more likely that, before performance is completed, unforeseen changes may happen to objective facts upon which the contract is based. For example, in a long-term construction contract, a price rise or change of applicable law may occur. Such change of circumstances has nothing to do with the contract parties and thus no party is in default, and if the original contract obligations are upheld, one or the other party will suffer unfairly. Consequently, the principle of change of circumstances can be used to adjust the contractual obligations. If, however, the contractual parties have prepared provisions regarding how to deal with change of circumstances, pursuant to the principle of freedom of contract, Article 227 of Taiwan's Civil Code is not applicable, which means it is not necessary and the parties are therefore under no right to ask the court to alter the original obligations.

In conclusion, the principle of change of circumstances can be used as a means for a contracting party to ask the court to adjust its contractual obligation when unconscionability would occur because of unpredictable changes. By changing the contract terms, the court must seek to restore the relations under the contract back to what both parties originally expected. If the court has changed the contract terms by exercising the principle of change of circumstances, the relevant contracting party will not be in default, even if the original contractual terms are not followed, and thus not liable for any related damages.

12. Remedies for Breach of Contracts

³⁷ Taiwan Civil Law, Art. 227-2: If there is change of circumstances which is not predictable then after the constitution of the contract, and if the performance of the original obligation arising therefrom will become obviously unfair, the party may apply to the court for increasing or reducing his payment, or altering the original obligation. The provision in the preceding paragraph shall apply *mutatis mutandis* to the obligation not arising from the contract.

1) Specific performance or monetary compensation?

Under Taiwan's Civil Code Articles 213 and 215, the liability for breach of contract is monetary compensation. Such compensation must restore the injured party to the pre-injury status quo. If the person who is bound to restore such status quo does not perform his obligation within a reasonable period fixed by the creditor, the creditor may claim monetary compensation for the injury. After the 1999 Amendment, a person who is bound to make compensation for an injury must restore the injured party to the pre-injury status quo, unless otherwise provided by the law or under the contract.

2) How to calculate the amount of monetary compensation and how to deal with consequential damages?

The compensation is limited to the injury actually sustained and thus the actual damages instead of the pre-injury status quo. According to Article 216-1, moreover, any interests acquired must be deducted from the amount of the compensation claimed. The former refers to a property dispute while the latter refers to the loss of prospective value, reflecting the consequential damage's provisions in Taiwan's Civil Code.

At the same time, interests that could have been normally expected are deemed to be the interests which have been lost, according to the ordinary course of things, and include the decided projects, equipment, or other particular circumstances. This article could be said to accept the standard of foreseeability. The court seems to take a lenient view towards foreseeability.³⁸ Monetary compensation includes prospective interests that could have been normally expected and which were lost in the action.

3) The difference between the right of rescission and the termination of a contract.

³⁸ See No. 2792 Judgment of 2003, Taiwan Supreme Court.

When it comes to ending a contract, the Taiwan Civil Code distinguishes between rescission and termination. The right of terminating a contract is regulated in the general principals of the Obligations part, and includes performance and default. Additional provisions are contained in the particular kinds of obligations, such as Article 359, the buyer having the option to rescind the contract or to ask for a price reduction. As for the rescission of the contract, however, most provisions are contained in various articles about particular kinds of obligations.

The distinction between rescission and termination of a contract is generally understood as follows. Regarding the rescission of a contract, it has been considered that once a contract is rescinded, the contract is treated as never having come into existence, and thus the remaining unperformed contractual obligations also no longer exist; as for the obligations that have already been performed, since the legal basis for the performance no longer exists, any party enriched without a legal basis is required to make restitution to the other party under the doctrine of "unjust enrichment." Termination of a contract, on the other hand, refers to the discharge of future contractual performance, and the parties are not under the obligation of restitution even if the contract is "terminated". Scholars and courts both consider that³⁹ if a contract involves continuous or periodic performance, only the concept of "termination" is applicable for ending the contract, and thus the parties are merely released from future performances (whereas past performances are still valid). This provision ensures that the retroactive effect of rescission does not unnecessarily complicate the contracting parties' relationship.

13. Validity of the Liquidated Damages and Penalty Clause.

The prospective liability for a breach of contract can be divided into liquidated damages and a penalty provision. The former is agreed to by the parties, and

³⁹ See No. 394 Judgment of 1999, Taiwan Supreme Court.

generally provides that the non-performing party shall pay the total amount of such damages. On the contrary, under the latter, the debtor must pay the penalty clause and then still perform its contract obligations. It is a punishment for the delinquent party.

Taiwan's Civil Code follows the Continental legal tradition. The function of this civil law is to compensate any damages and prevent prospective injuries. Any punishments thus normally belong exclusively to the criminal law, and most scholars believe that the penalty clause is not a statutory consideration under the civil code.

According to Article 250 of the Civil Code, unless otherwise agreed by the parties, the penalty shall be deemed to be the total amount of damages as a result of the non-performance. If it is agreed that the penalty shall be paid when the debtor does not perform the obligation at the agreed time or in the agreed manner, this penalty shall be deemed to be the total amount of damages due to such non-performance. In addition, the creditor may claim for the contract performance. It is commonly accepted that the without the parties' separate agreement, a fine for breach of contract would be considered as liquidated damages.⁴⁰ In other words, the statute sets the liquidated damages as the principle and the parties must set new rules in the contract to burden a party with any punitive damages.⁴¹

It is also worthwhile to discuss the influence of the obligation of the punitive damages. There are two different views on the influence of punitive damages. On the one hand, it is said that the penalty is part of the contract and should surely terminate with the principal contract. On the other hand, most courts do not accept the elimination of the penalty clause. The reason is that the claim of penalty clause to the damages has already occurred when the obligator breaks the relevant promise.

⁴⁰ See No. 1754 Judgment of 2001, Taiwan Supreme Court.

⁴¹ See No. 2922 Judgment of 1972, Taiwan Supreme Court and No. 496 Judgment of 1999, Taiwan Supreme Court.

14. Contract Dispute Resolution.

A contract dispute normally involves contract interpretation and filling in any loopholes. Some parties may file a lawsuit, while others opt for arbitration or seek a private settlement.

Whether litigation or arbitration, both parties must comply with the law. There are two types of interpretation: contractual and statutory (the former, also called contract interpretation, and the latter, legal interpretation). In this case, the contract dispute falls under the contract law regime. It, however, takes a long time and much labor to complete evidentiary findings and oral arguments. By way of contrast, arbitration is more efficient and the party can argue for individual demands. In addition, the parties can select an arbitrator with specialized knowledge. According to Article 31 of the Arbitration Law, if expressly authorized by the parties, the arbitral tribunal may apply the rules of equity to resolve the dispute.

In addition to litigation and arbitration, the parties can negotiate to settle the dispute privately. This option is often less costly than litigation. Litigation and arbitration, moreover, are both handled by a third party. At the same time, compromising to reach a settlement generally requires a long-term relationship between the parties and trust in each other.

This part involves different types of contracts and dispute resolutions. Regular civil contract disputes are generally resolved through litigation. If the contract value is high, the parties may handle the disputes more considerately. For lower valued contracts, the Taiwan Civil Procedure Law also sets up a small claims procedure to facilitate such dispute settlement. With commercial contracts, however, the parties generally choose solutions other than litigation. The reasons are as follows. (i) In commercial transactions, most disputants choose independent solutions to facilitate continued trading activity. (ii) Owing to

commercial habits, a judge might not have the relevant knowledge and experience to decide the matter fairly. (iii) For international commercial trading, the lawsuit may involve trial jurisdiction and ability to enforce the judgment. (iv) Because of business secrets, litigation, which would take place in public, is undesirable. (v) Facing a fast changing environment, litigation would take too much time to resolve the dispute.

15. The Role of Contract Law in Economic Development.

In a contract statute legislators often establish various imperative and optional provisions. Some provisions protect vulnerable groups for policy reasons. The Consumer Protection Law is one example. It is precisely because of such legislative policy considerations that parties often cannot avoid imperative rules. The imperative rules may adjust the order of the parties and preserve justice. By way of contrast, most statutes in the Civil Code are optional provisions for regulating the contracts and can be avoided by the parties' agreement. As for commercial contracts, more and more standard contracts and model contracts are used in business transactions. Companies, moreover, disfavor turning to litigation to resolve their disputes and the optional rules in the contract law are often not a good choice.

The above comments demonstrate that the statutory contract law increasingly interferes in contracts to protect consumers. On the other hand, it is useless in complementing the expression of intent.⁴² From an economic standpoint, the former balances contractual rights and obligations. It can ensure the relative equilibrium of companies and workers or consumers. In contrast, the latter has less influence on contracts, except for some principles of law such as Article 148 (A right shall be exercised and a duty shall be performed in accordance with the means of good faith.). Most Civil Code articles about different kinds of particular

⁴² Tzu-Chiang Chen, *Taiwan Civil Law and Modernization of Japanese Contract Law*, page 316 (Taipei, Angle 2011).

obligations have not been invoked in commercial transactions since 1999.

Although most of the optional rules do not influence economic development, they deserve additional attention for their impact on informal rules. In commercial transactions, the standard contracts and model contracts enacted by the government are used more widely than the optional rules. In international trade, we should focus on the applicable law and most of the statutes cannot reflect the parties' actual needs. Consequently, most international merchants choose customary trading practices instead of the contract law.⁴³ Since World War II, some international conventions, such as the CISG and PICC, have been adopted and used around the world. Finally, the merchant does not tend to choose litigation to resolve disputes, and it is informal law that promotes economic development.

⁴³ Alan Schwartz and Robert E. Scott, *Contract Theory and the Limits of Contract Law*, pages 547-548 (Yale Law Journal, 2003).