

## bona fide principle in Chinese laws

### Description

In a leasing/occupancy dispute where I represent the owners (a couple whose names are both registered on the title deed of the property) of an apartment in Shanghai, trying to take back the apartment which had been leased out to a foreigner “tenant” by the owners’ friend who was once entrusted with the keys of the apartment.

In response to my initial attorney letter in which I on behalf of my clients urged the occupants to move out of the apartment or re-sign a legal leasing agreement with and pay rents to my clients, the attorney of the “tenant” replied by throwing in a plausible “bona fide party” argument to defend his client. According to this attorney, his client was a bona fide party because (1) the illegal lessor, the friend of the owners of the apartment, held the photocopy of the title deed of the apartment; (2) the lessor held the key to the apartment; (3) the lessor held a power of attorney granted to her by the husband owner of the property, which was forged (as my clients had never given such a POA) and (4) the leasing transaction was done through a realty firm. Sounds reasonable, right?

What this attorney is really up to is to establish at law that his client, the occupant, as a bona fide party, had reasons to believe that the lessor was acting with authority as the property owners’ agent or representative, so that pursuant to Article 49 of China Contract Law, the leasing agreement was valid and binding on the property owners.

Well, to me who have been practicing real estate laws for years in Shanghai, the argument put forward by occupant’s attorney is not well grounded. Let us leave aside whether that argument will stand to reason at court, I am more interested to introduce the concept of bona fide (third) party and its application in Chinese laws.

### 1. Bona Fide (Third) Party

Bona Fide means “in good faith” in legal jargon. There is no clear or authoritative definition of the term. Generally speaking, it denotes the mental and moral states of honesty and conviction regarding either the rectitude or the depravity of a line of conducts of one’s own or others’. At laws, a bona fide actor should not be culpable and shall be protected in many situations, with a view to upholding social righteousness and boosting market transactions (to be elaborated below)

### 2. Prominent Application of Bona Fide Principle

(1) in the case of agency (agent-principal) relationship

Article 48 of China Contract Law:

Absent ratification by the principal, a contract concluded on his behalf by a person who lacked agency authority, who acted beyond his agency authority or whose agency authority

was extinguished is not binding upon the principal unless ratified by him, and the person performing such act is liable.

The other party may demand that the principal ratify the contract within one month. Where the principal fails to manifest his intention, he is deemed to have declined to ratify the contract. Prior to ratification of the contract, the other party in good faith is entitled to cancel the contract. Cancellation shall be effected by notification.

#### Article 49 of China Contract Law:

Where the person lacking agency authority, acting beyond his agency authority, or whose agency authority was extinguished concluded a contract in the name of the principal, if it was reasonable for the other party to believe that the person performing the act had agency authority, such act of agency is valid.

Bona fide doctrine is often triggered or brought into play when the validity of a contract is challenged because one contracting party's authority or power to enter into the contract is called into question, as in the case outlined in the beginning of the post. In such situations, the most frequently cited law provisions are the two clauses above quoted from China Contract Law, in particular Article 49.

Though not explicitly stated in this Article 49, the other party contending the contract in question is valid must be a "bona fide" party who does not know or ought not to be deemed to know that its counterparty did not have the authority to conclude the contract at the time execution thereof. As result, the contract will be held to be valid and binding on the principal who was not properly represented by his or her agent. Otherwise, the contract shall be deemed as not binding on the principal, leaving the signing parties to the contract in dispute which shall be settled between them.

In my case, the occupant's attorneys tried to make use the bona fide doctrine to protect their client, which is least likely to succeed, because the tenant ought to know that the owners, Singaporean couple, may not be able to write a power of attorney in Chinese, and furthermore, only the husband's name appeared on the forged POA. In this sense, this tenant shall not be regarded as bona fide party.

#### (2) good faith/bona fide acquisition of properties

China Property Law (effective as of Oct 1, 2007) for the first time provides for the good faith acquisition legal systems under which a bona fide purchaser of property, real or personal, is able to acquire the title to the properties even though the seller may not have the right or power to dispose of the properties.

According to Article 106 of China Property Law, where a seller sells property when having no right or power to do so, the purchaser is generally unable to acquire the title of the said properties unless the following conditions are simultaneously met:

(1) the purchaser is in good faith at the time of purchase;

(2) the property is sold at reasonable price; and

(3) the property has been duly registered (in regard of real property) or handed over (in regard of personal property), as the case may be, as required by laws.

In practice, many cases arise where one spouse sells their co-owned house or apartment registered in his or her name only without the consent or permission of the other spouse. Chinese family laws generally treat properties acquired by one spouse in the life of their marriage as community property disposal of which shall be subject to mutual consents of both spouses, but on the other hand, many such houses and apartments are registered in one spouse's name only. To the outsiders, though co-owned community property, such houses and apartments can be effectively sold by one spouse without the consent or knowledge of the other spouse whose name does not appear on the title deed of the property. In many cases, the non-disposing spouse attempts to petition to court to nullify the sale and purchase transaction for the reason of violating his or her rights in the property, however such attempts will fail for sure provided that the purchaser is bona fide at the time of transaction, has paid reasonable price and has had the property registered in his name. Courts are generally reluctant to annul such completed transaction unless it is proved that the purchaser is clearly not in good faith.

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