

## Settlement of Civil Disputes in China: Overview

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A Practice Note providing an overview on the key aspects of settling a civil dispute in China, including statutory duties to attempt settlement, the form and formalities of settlement, how to ensure confidentiality of the settlement terms, whether negotiations are without prejudice, third-party rights, remedies for breach, enforcement of the settlement terms, and how to set aside a settlement agreement.

Litigation is expensive and can often take a long time. Courts in many jurisdictions actively encourage settlement, and some jurisdictions require the parties to attempt settlement procedures in certain types of civil litigation. Settlements, which can be reached before or during legal proceedings, can be a cost-effective alternative to engaging in protracted and costly court action.

Settlements are usually considered a form of contract to which general contract law principles apply. However, settlements can also become part of a court order, especially when litigation is ongoing. In the context of a civil dispute between two or more parties, a settlement comes about when they reach a mutually acceptable compromise to resolve their dispute. If the settlement covers the parties' entire dispute, the dispute ends, as do any ongoing legal proceedings related to the dispute. Generally, the parties cannot start a new action relating to that dispute, unless they specifically agree that the dispute can be revived in certain circumstances.

This Note covers China-specific information on all aspects of settling a dispute by negotiation, mediation, and other alternative dispute resolution mechanisms, including:

- The legal or statutory duty and obligations, if any, to attempt settlement.
- The form and formalities of settlement, including the different ways the parties can record the settlement terms.
- Whether the terms of settlement require approval from the courts.
- How to ensure confidentiality of the settlement terms.
- The application of the without-prejudice rule, that is, how parties can ensure that anything said in the

settlement negotiations cannot be held against them in any subsequent litigation.

- Whether third parties have any rights under the settlement terms.
- Remedies for breach of settlement terms.
- Enforcement of the settlement terms and how to set aside a settlement.

For information on settlement in a cross-border context, see [Practice Note, Settlements in Cross-Border Disputes: Overview](#).

### Statutory Obligations to Attempt Settlement

Chinese courts encourage settlement between parties, and settlement is sometimes a mandatory procedure for certain kinds of civil litigation (such as divorce litigation). In this case, the court is required to ask the parties if they agree to mediate with a view to reach a settlement. If any of the parties expressly object, the court will not initiate the mediation process. If a settlement cannot be reached by the parties, the court will conduct a hearing and issue a ruling. In practice, since the number of cases accepted by the courts increases every year, the courts usually set up pre-trial mediation provided that the parties agree.

If the parties agree to settle the case, they can either withdraw the case or apply to the court for a ruling to verify the settlement agreement reached. The court only charges half of its normal official fee if the parties settle the case. However, if any party refuses to settle, the court will conduct the trial and make its own judgment.

There are no adverse implications or costs sanctions for the parties that refuse to participate in settlement negotiations.

### Form of Settlement

A settlement can be recorded in a settlement agreement or court order, both are acceptable under current laws and regulations in China.

If settlement is reached by the parties once court proceedings have started, they can choose either to withdraw the case from the court or apply to the court for a ruling to verify the settlement agreement. Once the settlement agreement is recognised by the court, it is legally binding and final as a court ruling.

Since a settlement agreement verified by the court is final and the two parties cannot normally appeal it, one party can apply directly to the court to enforce the terms of the settlement if the other party breaches the settlement agreement.

Settlement agreements made outside of court proceedings are legally binding unless they are held invalid by a court.

For settlements reached outside of court proceedings, one party will have to bring a fresh claim if the other party breaches the agreement. Therefore, in practice, the parties would normally apply for the court's verification to make the agreement enforceable as a court ruling. The parties can submit the settlement agreement to the court for verification once the case has been filed with the court.

If the parties apply for a court ruling to verify the settlement terms, the court will either request that the parties submit the written and signed settlement agreement or summarise the settlement terms in mediation proceedings and request that the parties sign the summary of settlement terms.

An oral agreement is binding on the parties. However, it may be difficult to prove the existence of the agreement. Emails or letters exchanged by the parties can also be used as evidence of the parties' agreement. The court will determine whether there is a valid and binding contract in light of the parties' statements. Therefore, it is recommended to memorialise the settlement in a separate agreement.

### Formalities

A written settlement must be signed by the parties and bear a corporate chop if the parties are legal entities.

The counterparts or separate copies of the settlement agreement can be executed by different parties with each copy being considered as an original. The parties can use counterparts to complete the process of executing a settlement agreement verified by the courts.

### Terms of Settlement Subject to Court Ratification

Generally speaking, the terms of the settlement do not require court approval. However, the settlement must be submitted to the court's verification to be considered final and to be enforceable as a court order. Some judges request the parties to submit the settlement agreement to the courts. (See Form of Settlement.)

Normally, the settlement agreement will not be a matter of public record. However, if the court thinks that disclosure of the settlement agreement is necessary for the purpose of protecting national interests, public interests, and the legitimate rights and interests of others, the court can disclose both the fact and the terms of the settlement agreement (*Article 146, Interpretations of the Supreme People's Court on the Application of the Civil Procedure Law of the People's Republic of China 2022 (SPC Interpretation 11/2022)*).

### Confidentiality

Settlements in China are automatically confidential. However, for the purpose of protecting national interests, public interests, and the legitimate rights and interests of others, the court can disclose the settlement information (*Article 146, SPC Interpretation 11/2022*).

### Powers of the Parties to Compromise

There are restrictions on the powers of minors and protected parties to settle disputes. Normally, the court requires that the guardian represent minors and protected parties in settling disputes.

A legal representative, such as chairperson or general manager, can sign the settlement agreement on behalf of a company.

Legal advisers and other authorised representatives must obtain express instructions and special authorisation from their clients before settling the dispute.

The following categories of disputes cannot be settled in China:

- Cases subject to special procedures (for example, cases concerning voter qualifications).
- Procedures for urging the performance of obligations.
- Procedure for public invitation to assert claims.
- Cases for confirming marriage or other types of relationship.

- Other cases that cannot be mediated based on their nature (for example, declaration of a person as missing or dead).

### Timing of Settlement

Settlement discussions can be conducted at any time after the court accepts the case but before it issues judgement. There are no advantages to settling the case during the initial stages of the proceedings, other than the litigation proceedings coming to an end sooner. The court official fee will only be reduced when the claimant withdraws the case from court.

### Without Prejudice Rule

The “without prejudice” rule applies to settlement negotiations in China. The facts acknowledged by a party during settlement negotiations cannot be used as evidence against that party in subsequent lawsuits, unless otherwise prescribed by law or agreed upon by all the parties concerned.

It is not necessary for parties to label a document with the words “without prejudice” since the courts attach more importance to the substance of the communication between the parties when determining whether a communication is without prejudice or not.

The without prejudice privilege is considered a joint privilege and therefore can only be waived jointly by the parties. Unintentional or inadvertent use or disclosure of, or reference to, privileged materials will not cause the loss of the without prejudice privilege.

However, if a party admits in litigation proceedings the facts agreed during the settlement agreement negotiation, the without prejudice rule will not apply.

Without prejudice protection extends to any subsequent litigation between the same parties (*Article 107, SPC Interpretation 11/2022*).

### Terms of Settlement

If the settlement terms affect a third party, the court must obtain the third party’s consent to the settlement (*Article 150, SPC Interpretation 11/2022*). If the third party breaches the settlement agreement before that settlement agreement is served, the court must render the judgment in a timely manner.

The Release clause set out in [Standard Document, Settlement agreement \(civil litigation\): Cross-border: clause 5](#) is suitable for use in China.

### Taxes on Settlements

If the money is related to payments for goods, the applicable taxes must be paid (for example, value added tax). If the money is for payment of a loan or represents compensation, any applicable taxes will be waived.

### Severability

Since the settlement agreement is normally verified by the court, the settlement terms are deemed legally valid. Therefore, a severability clause is not commonly incorporated into the settlement agreement with the court’s verification.

However, for a settlement agreement made without the court’s verification, it is common to incorporate a severability clause, to avoid the entire agreement being held void or unenforceable due to the illegality, invalidity, or unenforceability of a part of the agreement.

The severability clause at [Standard Document, Settlement agreement \(civil litigation\): Cross-border: clause 11](#) is suitable for use in China.

### Third-Party Rights

Third parties cannot directly enforce their rights under the terms of a settlement. If they want to enforce their rights, they will have to bring a fresh, separate claim.

In China, if a debtor is not actively seeking to recover a debt owed to it by a third party, the creditor can petition the court to bring subrogation proceedings against the third party. In practice, if the third party wishes to subrogate the creditor’s rights under the settlement agreement, it will have to file a claim with the court.

In China, the parties would not normally incorporate [Standard Document, Settlement agreement \(civil litigation\): Cross-border: clause 17](#) since it violates the interests of the third party with an independent claim.

### Disposal of Legal Proceedings

Assuming the parties settle the case and apply for the court’s verification of the agreement, the court will issue a civil mediation statement to verify the settlement agreement and conclude the trial of the case.

### Breach of Settlement Terms

If a party breaches the settlement terms verified by the court, the other party can file an application with the

enforcement department of the court to enforce the settlement agreement.

In settlement agreements not verified by the court, the other party cannot file an application with the court to enforce the agreement directly, and will instead have to bring a fresh claim for breach of the settlement agreement.

The injured party can also seek compensation for losses directly arising from the breach. In practice, as the claimant bears the burden of proof and there is no discovery process in China, it may be difficult to prove the existence of direct losses arising from a breach of settlement terms.

The terms of a settlement agreement must not violate the laws and regulations of China, or damage national interests, public interests, or the legitimate rights and interests of others. The court will not verify settlement agreements containing such terms and will normally request the parties to delete them from the agreement.

### Legal Costs

It is common to include a clause dealing with legal costs in the settlement agreement. The parties are free to agree on arrangements regarding payment of

legal costs. If the parties do not have any arrangement, the court will decide on the payment of legal costs.

Normally, the court requires the parties to bear the official fee equally (*Article 31, Measures for the Payment of Court Fees 2006* (2006 Court Fee Payment Measures, with effect from 1 April 2007)). The parties normally bear their own lawyers' costs.

### Settlement Agreements

The following clauses may vary from those in [Standard Document, Settlement agreement \(civil litigation\): Cross-border](#):

- **Stay or dismissal of action (clause 4).** If the settlement is reached and to be verified by the court, the clause can be amended to "The parties hereby consent to, and shall take all necessary steps to, obtain a civil mediation statement from the court."
- **Costs (clause 7).** The parties can make arrangements as to how to bear the legal costs. If there is no arrangement, each party will normally equally bear the official fee.
- **Third-party rights (clause 17).** In China, the parties would not normally incorporate the third-party rights clause, since it violates the interests of third parties with an independent claim.

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