

# Electronic Transaction of Insurance Business – “Self-Service Insurance Card” in China

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## Introduction

With the rapid development of the internet technology, online commercial transactions, known as e-commerce,<sup>1</sup> have become very popular in recent years. E-commerce is by its nature best suited to standardised products and processes. Most insurance contracts are standard term contracts, so online insurance transaction has become a new way for selling insurance products in China. In order to accelerate the development of e-commerce, the “Electronic Signature Law of the People Republic of China” was enacted on 28 August 2004, and became effective on 1 April 2005.<sup>2</sup> The Act regulates matters on electronic signatures, establishes the legal validity of electronic signatures, and safeguards the lawful rights and interests of all relevant parties of online transaction. On the same day when the legislation became effective, the People’s Property Insurance Company of China issued the first electronic policy in China and the whole procedure of the transaction was completed online, which marked the beginning of online insurance business transaction in China’s insurance market.<sup>3</sup> Since then more and more insurance companies have employed this new form of insurance transaction.<sup>4</sup>

Generally, there are two types of online insurance business in China: direct insurance business transaction and “self-service insurance card” transaction. The paper will briefly outline the direct insurance business transaction, and then examines in detail the “self-service insurance card” transaction by discussing its advantages from practical point of view and difficulties from legal point of view. The Electronic Signature Law only governs the matters of electronic signature. There is lack of rules of law governing other aspects of online insurance transaction. It is not surprising that a lot of disputes have arisen in industrial and judicial practice in relation to formation of insurance contracts and other matters in online transaction, particularly where a “self-service insurance card” is used. Of many issues on the matters of formation of insurance contracts via “self-service insurance card”, four are particularly important, (1) the issue when the contract is considered to be concluded, (2) the issue who is regarded as the proposer in an insurance card transaction, (3) the issue on the performance of the duty of good faith in an insurance card transaction, (4) the issue on whether an insurance card is returnable. This paper focuses on examining these four major issues. Chinese Insurance Law 2009 requires the proposer to disclose material facts and information to the insurer,<sup>5</sup> and the insurer to explain the terms of insurance contract and particularly the exclusion clauses to the proposer at the time of the contract is entered into.<sup>6</sup> Without identifying the proposer and ascertaining the time point when the insurance contract is entered into, it would be difficult for the insurer to say that he has performed his pre-contract duty to explain the terms of the contract to the proposer, and it would also be difficult to prove that the proposer has performed his pre-contract duty of disclosure.

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<sup>1</sup> E-commerce has been developed rapidly in many countries such as the UK. As it was commended by some writers “The development of digital signature technology has been mainly driven by the banking sector, but it clearly also has potential applications to the life insurance industry.” See Robert Surridge, Brian Murphy, Noleen John and Colin Griffin, *Housemen*’ (14<sup>th</sup> edn, Billomsbury Professional, 2011), p25.

<sup>2</sup> The Electronic Signature Law of the People’s Republic of China was promulgated on 28 August 2004, and became effective on 1 April 2005. By virtue of art.1, “This Law is formulated in order to regulate electronic signatures, to establish the legal validity of electronic signatures, and to safeguard the lawful rights and interests of all relevant parties.”

<sup>3</sup> Jing Wang, *Insurance Cases, Rules of Judgement and Application of laws*, (2013) People’s Court Press, p42.

<sup>4</sup> *Ibid.*

<sup>5</sup> Art. 16(1) of the Insurance Law 2009.

<sup>6</sup> Art. 17 of the Insurance Law 2009.

Before discussing the insurance card transaction, it is appropriate to briefly outline the online direct insurance business transaction.

### **Online direct insurance business transaction**

Like other online transactions, online direct insurance business transaction is such a form of transaction that the whole procedure for the formation of an insurance contract is completed online. The application (the offer) for insurance by the proposer, the examination of the application and the acceptance by the insurer, the payment of the premium and the issue of the policy are all carried out online.

Under this form of transaction the insurer advertises its insurance products on its website to invite people to make offer; this is analogous to online advertisements of goods and constitutes an invitation to treat. If a person, after visiting the insurer's website, is interested in an insurance product advertised by the insurer, he can make an online application by filling up an e-proposal form following the procedure designed by the insurer and submitting it online<sup>7</sup>. This amounts to an offer by the proposer. If the insurer, upon examining the proposal, agrees to accept the application, he will request the proposer to pay the premium. The proposer pays the premium online by providing the insurer with his bank details so that the premium can be transferred from the proposer's account to the insurer's account. After having received the premium, the insurer will issue an e-policy to the proposer.<sup>8</sup> The contract is then concluded and becomes effective at the same time. The insurer begins to undertake risks in accordance with the agreements specified in the contract.<sup>9</sup>

The process for making an insurance contract online is very similar to that of the traditional paper transaction of insurance business. There are fewer disputes arising from online direct insurance transaction in relation to formation of the contracts. This article does not intend to discuss this form of online transaction in detail, but focuses on the second type of online insurance transaction, namely, the "self-service insurance card" transaction.

### **"Self-service insurance card" transaction**

#### ***What is a "self-service insurance card" transaction?***

Like online direct insurance transaction, insurance card transaction is also a paperless transaction; the formation of an insurance contract will be completed online without any paper document except the insurance card. It is called "self-service insurance card" because it is a self-helped transaction; the purchaser of the card or the card-holder<sup>10</sup> needs to complete the online transaction himself.<sup>11</sup>

The insurance companies sell "self-service insurance cards" to any person who is 18 years old or over with full civil capacity and who is interested in insurance card transaction. In recent years many insurance companies have opened insurance card business.<sup>12</sup>

The procedure for making an insurance contract by using an insurance card is simple. First, the insurer's employees and/or his agents introduce the "self-service insurance card" to the customers face to face to invite them to buy the card. Any person who wants to take out insurance this way can buy a "self-service insurance card". The card can

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<sup>7</sup> To seek to avoid potential problems, the insurer should clearly set out the procedure to be followed for a binding insurance contract to come into existence so that customers have clear knowledge that the contract will not be concluded until that procedure is completed.

<sup>8</sup> In the e-proposal form the proposer is required to put his/her email address in order that the e-policy could be sent to him/her through email. If no email address is provided, the policy will be sent to the proposer's home address if required by the proposer.

<sup>9</sup> Tian Yin and Zili Ren, *Insurance Law Review*, (2012), Law Press, China, p272.

<sup>10</sup> Here the card-holder refers to the person who receives a "self-service insurance card" from the purchaser of the card as a gift. The card-holder has the right to activate the card on the insurer's website.

<sup>11</sup> He can also ask the insurer or the insurer's agent to help him to complete the transaction.

<sup>12</sup> Such as The People's Property Insurance Company of China, the People's Life Insurance Company of China, Ping An Life Insurance Co. Ltd, Hua Xia Life Insurance Company, An Bang Insurance Company and Zi Jin Property Insurance Company and so on.

also be sold on insurer's websites,<sup>13</sup> in a shop, a travel agency, at a railway/bus station, an airport, or in a bank or a post office, or other places.

After purchasing the card, the purchaser must activate the card on the insurance company's website<sup>14</sup> following the procedure designed by the insurer. There are a card number and a PIN on the card. The purchaser of the card can visit the insurance company's website to activate the card by inputting the card number and the PIN. He must do it following the online instructions provided by the insurance company. He can also phone the insurance company and ask the insurer to help him to activate the card. When the process of activation has been completed, an e-policy will be produced which becomes effective immediately.<sup>15</sup> Alternatively, the parties may determine a date on which the policy will become effective.<sup>16</sup>

A person may also buy an insurance card and give it as a gift to a friend or other members of his/her family. The person who receives the card (the card-holder) can activate it on the insurance company's website.<sup>17</sup>

This form of insurance transaction is designed specifically for some simple types of insurance such as household insurance and short-term personal accident insurance. The options include accident insurance for travel by air, public transport accident insurance and motor vehicle accident insurance etc. The durations of insurance cover for different products vary from several days, several months, and half year to one year. The shortest period is 7 days and the longest is one year. The premium is relatively cheap and varies from ¥10, ¥50 to ¥100. The highest insured amount can be up to ¥1,000,000.<sup>18</sup> The premium and the insured amount are fixed.

Insurance card transaction has many advantages. The insurer's running cost is low; the premium is low; the procedure of making a contract is simple and quick. These advantages make this form of transaction popular.<sup>19</sup> It is attractive to some certain groups of people. For example, people who often travel are interested in this transaction because the procedure for making the insurance is simple and quick. They just need to buy a card and activate it on the insurance company's website. People from rural area who have low income are interested in the products because they are cheaper.<sup>20</sup>

Practically, it is convenient to sell and buy insurance through insurance cards, but many legal issues have arisen and may continue to arise from this type of transaction. The most important issues are those relating to the time at which the insurance is concluded, who the proposer is for the contract where a person buys an insurance card as a gift and

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<sup>13</sup> For example, the China Life Insurance Company's website is [www.e-chinalife.com](http://www.e-chinalife.com); Ping An Life Insurance Company's website is [www.pingan.com](http://www.pingan.com).

<sup>14</sup> For example, the activating website of Ping An Insurance Company of China is <http://shop.pingan.com/baoxianka/baoxiankajihuo.shtml>

<sup>15</sup> Some people suggest that the words "to register" should be used instead of the term of "to activate" the card on the particular insurance company's website, because the procedure of activating is in fact a procedure of registration. See Xin Chen's comment which was cited in the book of *Insurance Law Review* edited by Tian Yin and Zili Ren (2012), Law Press China, p273. He said that it is not appropriate to use the words of activate the card, because activation is a moment, but registration is a process during which the proposer needs to provide information the insurer wanted.

<sup>16</sup> For example, Ping An Insurance Company provides that the proposer may choose a date for the policy to be effective but the date must be on day 6 or later from the date when the proposer activated the card. The information is available on <http://shop.pingan.com/changjianwenti/zizhukachangjianwenti.shtml> (Accessed on 27 June 2014).

<sup>17</sup> If the purchaser buys an insurance card for another person or transfers the card to a friend as a gift, the person who receives the card (card-holder) should activate the card.

<sup>18</sup> The information is available on <http://news.163.com/09/0807/06/5G3GBN19000120GR.html> (Accessed on 10 June 2014).

<sup>19</sup> Jian Xu, the deputy manager of Hua Xia Life Insurance Co Ltd., Jiangsu Branch, said, "the insurance card transaction is welcomed by insurance consumers because of its advantages. Since 2008 when the company began to run the card transaction, more than 30 types of insurance products had been provided online by 2012. 500,000 people have been covered by this transaction; a person spends only ¥100 to buy a card, but may get ¥50,000 payment upon the occurrence of the insured event." He talked this on the seminar on "China Electronic Policy – Law and Practice" held on 9-10 June 2012 in Nanjing, Zhejiang Province, China.

<sup>20</sup> However, there are problems for the rural area people to take out insurance this way, because most of them do not have computer and no internet system and they cannot activate the card online themselves, they need insurer's help to activate the card. Detailed discussion on this point will be given later.

transfers it to a friend, and how the parties perform their duties of good faith in a card transaction. Completion of an insurance card transaction includes two stages: first stage is buying an insurance card and the second stage is to activate the card online. So it is disputable at what stage the contract is deemed to be concluded. Because an insurance card can be transferred to another person, the person who buys the card and the person who activates the card may not be the same person, so there is no clear answer to the question who is the proposer. Moreover, in a card transaction, unlike traditional insurance transaction, the parties will perform their duties of good faith in a different way. Because of lack of rules of law to govern such a transaction, many different views on these issues have been expressed from academics, judges, legal practitioners and industry professionals. In the following sections, these issues are discussed.

### ***When an insurance contract is concluded under an insurance card transaction?***

This is a controversial issue. There are a number of different views on the issue:

The first view is that the insurance contract is concluded when the sale of card transaction is completed. By this view, the person who pays the money to purchase the card is to make an offer, and the insurer or his agent who receives the money and passes the card to the purchaser is to accept the offer.<sup>21</sup> A scholar was of the view that buying an insurance card is analogous to buying a mobile phone card.<sup>22</sup> He said when a person buys a mobile phone card, the contract is concluded and the card becomes effective when it is activated. Similarly, when a person buys an insurance card, the contract is concluded, and it also becomes effective when it is activated. The author disagrees with the view for the following the reasons.

- (1) The nature of purchasing an insurance card is different from the purchase of a mobile phone card. Although both cards need to be activated before it becomes effective, the procedure for the later involves only simply inputting the card number in the mobile phone and the card is then activated. However, the procedure is more complicated for activating an insurance card. The proposer needs to input information and disclose material facts to the insurer by answering the questions raised in the proposal form online, and the insurer must explain the policy terms, especially the exclusion clauses of the policy to the proposer by putting notices online to draw attentions of the proposer to the exclusion clauses during the process of the activation. Moreover, sometimes the proposer's application may be rejected online because the proposer does not meet the conditions of the insurance. For example, where the proposer's occupation falls outside the category of the insurance, the card cannot be activated. Thus it is submitted that the insurance card transaction is essentially different from the mobile phone card transaction, and that the view is incorrect that the insurance contract is concluded at the time of purchasing the card.
- (2) The critical elements for formation of an insurance contract include (a) the parties; (b) the agreement; (c) the subject matter. In an insurance card transaction, the contract cannot be concluded at the time when the person buys the card, because at that moment, none of the above elements are existed. First, the proposer has not been determined, as mentioned above, the purchaser of an insurance card is not necessary the proposer, he/she may buy the card for another person. Secondly, the subject matter of insurance (the insured) has not been determined.<sup>23</sup> Thirdly, no agreement between the parties has been reached on the

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<sup>21</sup> That is the view of the Intermediate People's Court of Gulou District of Nanjing City, Jiangsu Province. Sha Yinhua agrees with the view, see the book of *Insurance Law Review*, edited by Tian Yin and Zili Ren (2012), p275. See also the case of *Mr Zhang and others v Huaxia Life Insurance Company Jiangsu Branch*, which will be discussed in details later. This case was cited by Jiadong Xing in the book of *Insurance Law Review*, edited by Tian Yin and Zili Ren (2012), Law Press, China. See p143.

<sup>22</sup> Yinhua Sha, *Insurance Law Review*, edited by Tian Yin and Zili Ren (2012), Law Press, China, p275.

<sup>23</sup> For an online insurance transaction, including an insurance card transaction, due to the fact that it is difficult to check whether the proposer and the beneficiary has an insurable interest on the life insured, in order to prevent the moral hazard, the insurance companies which have opened online insurance business, provide that the proposer and the life insured must be the same person and the beneficiary must be the life insured's legal successor, so that the requirement of the insurable interest can be satisfied. (See the opinion of Wen Wei, The General Manager of the Legal Department of the Peoples Property Insurance of China, Jiangsu Branch, which was expressed on the seminar on "China Electronic Insurance Policy: Law and Practice" held 9-10 June 2012 in Nanjing, Zhejiang Province, China. The opinion was cited in the book of *Insurance Law Review*, edited by Tian Yin and Zili Ren, (2012), Law Press, China, pp271-272.

major terms of an insurance contract at that stage, because the major terms of the policy are placed on the insurer's website which can only be read by the proposer when he/she activates the insurance card.

- (3) According to the Insurance Law 2009,<sup>24</sup> the pre-contract duties of good faith imposed on both parties should be performed before or at the time of concluding the contract. However, under an insurance card transaction the parties cannot perform their duties at the time of purchasing the card. The purchaser can only read the brief explanation of the insurance product which is attached to the card after the completion of the buying of the card,<sup>25</sup> and the detailed policy terms and conditions can be read only during the procedure of activating the card.<sup>26</sup> The proposer (if the purchaser and the proposer is the same person) will perform his duty by answering questions on online during the process of activation. If the view that the contract is concluded at the time when the person buys the card were to be correct, it would mean that the duties of good faith are performed after the conclusion of the contract. This therefore contradicts with the insurance law which requires the parties to perform their pre-contract duties of good faith before or at the time when the contract is concluded.<sup>27</sup>
- (4) If it is deemed that the insurance contract is concluded at the time of buying the card, the purchaser should be regarded as the proposer. Where the card is transferred to another person who activates the card, the other person should be the insured of the contract. In this situation, the proposer and the insured are different persons. However, the insurance companies which run the card insurance business require that the proposer and the insured must be the same person, and the beneficiaries must be the insured himself or the insured's legal successors.<sup>28</sup> So this requirement cannot be satisfied if the contract is deemed to be concluded at the time of purchasing of the card.

Upon the above analysis, it can be concluded that the view that the insurance contract is concluded at the time of buying the card is wrong.<sup>29</sup>

The second view is that, in an insurance card transaction, the payment for the card can be regarded as the pre-paid premium and the insurance contract will be concluded at a later stage, that is, at the time when the insurance card is activated. At that time the proposer, the insured and the insurance period are determined. The e-proposal form is filled by the proposer, and the insurer accepts the risk if the requirements for the insurance are met, an e-policy is issued, the contract is then concluded.<sup>30</sup> By this view, an insurance contract cannot be concluded before the insurer agrees to take the risk. By virtue of article 13 of the Insurance Law,<sup>31</sup> an insurance contract shall be formed when

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<sup>24</sup> See art.16 and art.17 of the Insurance Law 2009.

<sup>25</sup> Although sometimes the insurer or its agent may briefly explain some terms and exclusion clauses to the customers when they introduce the card to them or to persons who buys the card, in most situations they do not do so at that stage, especially when the person buys a card in a shop or at a railway station, it is doubtful that the agent is able to explain the terms to the purchaser. It is probably that the agent himself does not understand the complex terms.

<sup>26</sup> So far as the methods of performing the duties online is concerned, art.12 of the Supreme People's Court's Interpretation on Insurance Law provides "Where the insurance contracts are concluded through internet, telephone or other similar ways, if the insurer performs his duty of explaining exclusion clauses by webpage, audio or video or other similar ways, the People's Courts should deem that the insurer has performed his duty"

<sup>27</sup> See art.16 and art.17 of the Insurance Law 2009.

<sup>28</sup> Wen Wei, The General Manager of the Legal Department of the Peoples Property Insurance of China, Jiangsu Branch, expressed his view on the e-policy which was incorporated in the book of *Insurance Law Review*, edited by Tian Yin and Zili Ren. (2012), Law Press, China, pp271-272.

<sup>29</sup> Chengli Liu, judge of the Supreme People's Court, also has the opinion that the contract cannot be formed when the person buys the card. See Chengli Liu, *Insurance Law Review*, edited by Tian Yin and Zili Ren, (2012), Law Press, China, p274.

<sup>30</sup> See Jing Wang, *Insurance Cases, Rules of Judgement and Application of Laws*, (2013), People's Court Press, p43. See also Chengli Liu, judge of the Supreme People's Court, express his view on the Seminar on "China Electronic Policy, held on 9-10 June 2012, in Nanjing, Zhejiang Province, China. See also Zhengqin Lu, who expressed his view on the same Seminar.

<sup>31</sup> Art.13 of the Insurance Law 2009 provides: "An insurance contract shall be formed after a proposer has made an insurance offer and an insurer has agreed to accept such offer. The insurer shall issue a policy or other insurance certificate to the proposer in a timely manner and specify the contents of the contract as agreed between the parties in the policy or other insurance certificate."

the insurer accepts the offer made by the proposer. In a card transaction, the issue of an e-policy amounts to the insurer's acceptance of the insurance. The e-policy can only be produced when the procedure of the insurance card activation is completed, so the contract is concluded at that time. During the procedure of activation, the person needs to answer the questions raised in the e-proposal truthfully to meet the requirement of the duty of good faith. Similarly, the insurer must explain the policy terms especially the exclusion clauses to the proposer by highlighting them online. After completing the procedure, the insurance card is activated and the e-policy is produced, and the contract is concluded and becomes effective at the same time. The parties can also agree for the insurance to become effective on a certain date.<sup>32</sup>

This view seems more logical than the first one, but still may cause problems. As a judge argues<sup>33</sup> if this view was adopted, two problems would be caused. First, after buying of the card and before it is activated, the purchaser of the card is the offerer to the insurance contract before the acceptance (the card is activated) is made. According to Contract Law, an offer can be withdrawn at any time before the acceptance is made.<sup>34</sup> So the purchaser can return the card at any time before the card is activated. The purchaser is not legally barred to return the card, so the insurer's notice that the card is non-returnable has no legal force. Secondly, it seems unfair and lack of legal basis to request a person to pay fees (as a premium) for the card before the conclusion of an insurance contract. This is in fact about the question on the nature of the purchasing of the card. The following two views (the third and the fourth views) are related to the question.

The third view holds that two contracts are concluded in completing an insurance card transaction, one is the sale of card contract and the other is the insurance contract. When the person purchases the card, the sale contract is concluded. The insurance contract is concluded when the purchaser or the card-holder activates the card.<sup>35</sup>

It is submitted that the third view still has problems. For any binding contract, one of the important elements is consideration; each party must provide consideration to the other. In an insurance card transaction, assuming that the sale of card contract is a separate contract, the purchaser pays the cost for the card, but what is the consideration for the purchaser's cost? Similarly, if the activation of the card is deemed as another separate contract, the insurer promises to undertake the risk, but what is the card-holder's consideration for the insurer's promise. He does not contribute anything for the second contract, because the cost of the card is the consideration of the first contract. Moreover, if the purchaser of the card transfers the card to another person who eventually activates the card, the second contract is concluded, then the insurer starts to bear the risk for the person, but what is the person's consideration? He/she did not contribute to the contract. So the view that there are two separate contracts is difficult to accept.

The fourth view presumes that, in an insurance card transaction, the purchase of an insurance card is a preliminary contract which is formed at the time of the purchasing of the card with the purpose to conclude a main contract (the insurance contract) by activating the card. When the card is activated, the main contract is concluded.<sup>36</sup> It should be noted that this view is different from the third view (the view of "two main contracts"). This view refers to one preliminary contract and one main contract. It is submitted that this view could essentially explain the nature and the characters of an insurance card transaction. It seems more logical for the following reasons.

A preliminary contract is a contract,<sup>37</sup> in which the parties reach an agreement for concluding another contract - the main contract.<sup>38</sup> The main purpose of the parties to make a preliminary contract is to reach an agreement for making

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<sup>32</sup> The parties can agree a fixed time at which the contract will become effective. Para.3 of art.13 of the Insurance Law 2009 provides "A lawfully formed insurance contract shall take effect upon its formation. The proposer and the insurer may attach conditions or a term for the contract to take effect."

<sup>33</sup> See Jiadong Xing, *Insurance Law Review*, edited by Tian Yin and Zili Ren, (2012), p151.

<sup>34</sup> Art.18 of the Contract Law 1999.

<sup>35</sup> This view is expressed by Zili Ren on the seminar on "China Electronic Insurance Policy: Law and Practice" held on 9-10 June 2012 in Nanjing Province, China. This view was cited in the book of *Insurance Law Review*, edited by Tian Yin and Zili Ren, (2012), Law Press, China, p275.

<sup>36</sup> Zhang Xiuquan and Liu Xuesheng have the same opinion. They expressed their view on the seminar on "China Electronic Insurance Policy: Law and Practice" held 9-10 June 2012 in Nanjing Province, China. Their opinions were cited in the book of *Insurance Law Review*, edited by Tian Yin and Zili Ren, (2012), Law Press, China, p274.

<sup>37</sup> It is also known as a preliminary agreement.

another contract. A preliminary contract has an expressed binding effect. It does not yet contain all conditions of the main contract, however, it has to include as much as possible of the content of the main contract to enable the contractual parties to legally pursue the conclusion of the main contract, if necessary.<sup>39</sup>

Preliminary contracts are used by the parties to arrange the conclusion of another contract under the circumstance where the conditions to make the main contract are not ready.<sup>40</sup> In modern days, in China, a preliminary agreement is often signed in the sale of real property, but it is not often used in other areas. The purpose of making a preliminary agreement is that some conditions for making a final formal contract are yet to be satisfied, for example, In the case of the sale of a flat unit in a building that is under construction, a preliminary contract must be concluded between the developer and the individual who wishes to buy the unit when the construction of the building is finished and the developer obtains the license for sale of the building. This contract, signed by both of these parties, is the first step leading to the purchase of the unit.

Although a preliminary agreement has never been used in a traditional insurance transaction, it is submitted that the preliminary contract approach can well describe the nature and the purpose of buying an insurance card, that is, buying an insurance card is an arrangement for making an insurance contract by activating the card. Buying an insurance card is buying a right to submit an application for the insurance on the insurer's website. It is the first step to make the main contract (the insurance contract). The payment for the card could be deemed as deposit for making the formal insurance contract, and the insurer's promise to enable the card-holder to access the online system (by giving a card number and PIN) for making the insurance contract is the consideration for the preliminary contract.

However, in China, there is no legislation on preliminary contract.<sup>41</sup> The Supreme People's Court (SPC) published its "Interpretation on the Questions concerning Applicable Law for Hearing Cases for Sales Contract Disputes" in 2012<sup>42</sup> which includes, *inter alia*, elements of preliminary contract for the formation of a sale of goods contract. Article 2 of the SPC's Interpretation provides: "Where the parties who has signed a subscription agreement, order agreement, booking agreement, letters of intention, memorandum or other reservation contract, has agreed to enter into the contract of sale within a certain period of time in the future, if one party does not fulfil the obligations for making a sales contract, the other party can requests the defaulting party to assume contractual liability for breach of its commitments in the preliminary agreement or requests to rescind the preliminary contract and to claim damages, the People's courts should uphold such request." The SPC's prevision indicates that for making a main sale contract, the parties may sign a preliminary contract in advance in which the parties may reach an agreement for the concluding the main contract in the near future when the conditions for concluding the main contract are met. The parties are bound to conclude the main contract in a specified period. Any party who breaches the preliminary agreement must assume liability for the breach or pay damages for the breach. The SPC's Interpretation means that the concept of preliminary contract has been recognised in Chinese legal system.<sup>43</sup>

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<sup>38</sup> According to the Black Law Dictionary, a preliminary contract is a contract, in which the parties agree to conclude another contract, i.e. the main contract. See also Macao Civil Code, s.404.

<sup>39</sup> Linlin Zhu, "Brief Analysis on the Principals of Preliminary contracts", [www.google.co.uk](http://www.google.co.uk) (accessed on 26 July 2014)

<sup>40</sup> For example, for a sale of goods transaction, where the goods are not ready for delivery; in the preliminary contract parties agree that they will conclude a main contract when the goods are ready, and detailed conditions and terms will be contained in the main contract. Nowadays, preliminary contract are rarely used for sale of goods, parties prefer to make a single main contract, even if the goods are not ready for delivery when the contract is concluded, they can attach additional conditions to be met in the future, such as to deliver the goods or pay the price on a fixed date.

<sup>41</sup> Many other jurisdictions' civil codes include provisions on preliminary contract, such as French Civil Code (S.1589); Austrian Civil Code (s.936); Russian Federal Civil Code (ss.429 and 445) and Macao Civil Code (ss.404, 405 and 211).

<sup>42</sup> See The Supreme People's Court's "Interpretation on the Questions concerning Applicable Law for Hearing Cases for Sales Contract Disputes" [2012] No 8.

<sup>43</sup> See Xinghui Liang, *The Principles for the Interpretation of Preliminary Contract*, <http://article.chinalawinfo.com> (Accessed on 11 July 2014). In his article the author explained the nature and the effect of a preliminary contract.

From the SPC's Interpretation, it is clear that the preliminary contract can be adopted in sale of goods cases. It is not clear whether it can be used in other areas. There are different opinions on this point. Some scholars are of the view that a preliminary contract can be applied only for making the main contracts for sale of goods or sale of real property or other contract which requires formalities for the formation of the contract, but not for a contract which does not require special formalities, such as an insurance contract.<sup>44</sup> However, some writers suggest that the preliminary contract can be used for making all kinds of contracts.<sup>45</sup> Despite the different opinions, in practice, the preliminary contracts are used in many areas.<sup>46</sup>

For traditional insurance business transaction, there is no need to make a preliminary contract first and then make a main contract to complete the transaction. An insurance card transaction is, however, a special form of insurance transaction, the procedure for making a contract is different from that for a traditional insurance contract. It is more logical using the approach of "preliminary contract and the main contract" to explain the special form of insurance transaction. The preliminary contract and the main contract are two interdependent contracts. The formation of the former is the preparation for making the latter, and the formation of the latter is based on the former.

The preliminary agreement is binding on both parties. If the buying of an insurance card is regarded as a preliminary contract, the purchaser of the card and the insurer who sold the card must be bound to make the main contract – the insurance contract. This means that the purchaser must activate the card.<sup>47</sup> The failure to activate the card is equivalent to giving up the right to take out insurance online so no remedies will be available. The insurer must accept the risk if the information of the proposer/insured meet the conditions for the formation of the insurance contract.

In addition, the contractual right of the preliminary contract can be assigned to a third party. The person who buys the insurance card can assign, as agreed by parties in the preliminary contract or by virtue of law,<sup>48</sup> to a third party his right of activating the card and obtain the e-policy. Therefore, it could be said that the buying of an insurance card can be regarded as a preliminary contract and the activation of the card is the main contract; the two-stage transaction can be completed by concluding the two interdependent contracts.

Because there are no rules of law to follow, Chinese courts have different approaches on hearing cases relating to insurance card transaction. After having discussed different academic opinions, it is appropriate to see how the courts deal with such cases.

In *Mr Zhang and others v Huaxia Life Insurance Company Jiangsu Branch*,<sup>49</sup> Mr Zhang spent ¥150 to buy a "self-service insurance card" for accident insurance from the agent of Huaxia Insurance Company. The insurance covers all family members of the proposer. The insured amount was ¥150,000 for personal injury or death, and ¥5,000 for medical treatment. The card was not activated in due course. On 20 Oct 2010, Mr Zhang and his wife were injured in a traffic accident, his wife died in hospital during treatment. After the accident, on 30 Oct, Zhang asked the insurer's agent to activate the card. The card was not expired so it was successfully activated. Zhang's claim was rejected by the insurer. The Nanjing Trial Court held that the insurance contract was concluded and entered into effect when the proposer paid the fee for buying the card and the insurer or his agent accepted the money. The insurer would begin to undertake liability from the time when the card was activated. Because the card was not activated when the insured event occurred, so the insurer was not liable for the loss. Zhang appealed. The Nanjing

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<sup>44</sup> Senyan Sun, *Introduction to Civil Law Obligation*, (1999), Taipei, Sunmin Book Press, p45. See also Yulin Qian, "Introduction to Preliminary Contract" published on [www.civillaw.com.cn](http://www.civillaw.com.cn) (Accessed on 26 July 2014).

<sup>45</sup> Yubo Zheng, *Introduction to Civil Law Obligation*, (1990), Taipei, Sunmin Book Press, p32. See also Yulin Qian, "Introduction to Preliminary Contract" published on [www.civillaw.com.cn](http://www.civillaw.com.cn) (Accessed on 26 July 2014).

<sup>46</sup> Such as the booking of a ticket, the booking a hotel and so on.

<sup>47</sup> If he transfers the card to another person, that other person must activate the card.

<sup>48</sup> Because a preliminary contract is one kind of contract, so some provision of Contract Law may govern the preliminary contract, for example, the assignment of the contractual right to other persons. According to art.79 of the Contract Law, "The creditor may assign to a third party all or part of his rights under the contract." Macao Civil Code also has provisions regarding assignment of a preliminary contractual right to a third person, see s.571 and s418 of Macao Civil Code.

<sup>49</sup> This case was cited by Jiadong Xing in the book of *Insurance Law Review*, edited by Tian Yin and Zili Ren (2012), Law Press, China, on p143.



Intermediate Court upheld the trial court's decision but dealt with the dispute through mediation and asked the insurer to pay part of the insured amount to the proposer.<sup>50</sup> Both parties accepted that decision.

From this case, it is clear that the courts held that in an insurance card transaction, the contract is concluded and becomes effective at the time of buying the card. The insurer begins undertaking the risk from the time when the card is activated and the e-policy is issued.

In *Mr Li v Life Insurance Co Ltd*,<sup>51</sup> a case concerning the formation of an insurance contract in a card transaction and the issue of whether the card is returnable, Mr Li bought a "self-service insurance card" in Oct 2011. He was seriously injured in March 2012, but by then he had not activated the card. The insurer rejected his claim on the ground that the insurance contract had not been formed and the policy had not become effective when the insurance event occurred. The court held that the card must be activated within the period specified on the card, beyond that period, the card would become invalid and could not be activated. The insured had not activated the card before the accident occurred, the insurance contract was not concluded, so the insurer was not liable.<sup>52</sup>

Some people suggest that the card should be activated by the insurer's employee when the person buys the card in the insurance company. The process for formation of an online insurance contract should be completed in front of the purchaser of the card, and the contract can be concluded upon the activation of the card.<sup>53</sup> It is a good idea but only feasible for the case where the person buys the card for himself. There are still problems where the card is transferred, or the person buys the card in some other places. It is not convenient to activate the card at such other places, say in a post office, in a railway station or in an airport. Under these circumstances, the card-holder can either activate the card online at home or go to an office of the insurance company to activate the card with the help of an employee of the company.

In *Gu Jianhua v Huaxia Life Insurance Co Ltd, Jiangsu Branch*,<sup>54</sup> Mr Gu bought some insurance cards for himself and his employees for personal accident insurance in April 2010.<sup>55</sup> The duration of the risk was from 4 April 2010 to 3 April 2011. Mr Gu gave a card to Mr Bihua Shi, one of his employees. Mr Shi activated the insurance card in due course. On 21 Dec 2010, Mr Shi was injured when he was working on a tower and died a few days later. Mr Gu, as Shi's employer, paid ¥290,000 for Shi's medical cost for hospital treatment and ¥590,000 to his family after Shi died. Shi's family assigned the insurance claim right to Mr Gu. After obtaining the assignment letter, Gu claimed against the insurance company within the insurance amount shown on the insurance card. However, the insurer rejected Gu's claim on the ground that Gu was neither the proposer nor the beneficiary of the contract.

The court held that although Gu was not the proposer but Shi was. The contract was a valid contract. Gu, as Shi's employer, had paid the costs for Shi's hospital cost and paid moneys to Shi's legal successors after Shi died. The right of claim against the insurer was assigned by Shi's successors to Gu, so Gu has the right to claim and the insurance company was liable for paying Gu the amount as specified under the contract.

In this case, the issue seemingly is who has right to claim, the person who purchased the card or the person who actually activated the card? The issue, in fact, is an issue of assignment of a creditor's right of claim. It is submitted that Mr Gu should be allowed to claim, not because he was Shi's employer or was the purchaser of the card, but because he was the assignee of the beneficiaries' right of claim. Gu is entitled to claim by the Contract Law. According to article 79 of Contract Law, the creditor may assign to a third party all or part of his rights under the

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<sup>50</sup> In Chinese judicial system, the courts have a function of mediation in settling civil disputes. So the case was eventually solved through mediation by Nanjing Intermediate Court, and the insurer paid ¥3,500 to the insured.

<sup>51</sup> <http://www.cybxh.com/newshow.asp?id=3760&mnid> (Accessed on 10 June 2014).

<sup>52</sup> The card-holder must beware and not forget to activate the card in the specified time. It is also important that the insurer or his agent must tell the purchaser of the card to activate the card. If the insurer or his agent failed to tell the purchaser of the card about the activation, the question is who should be liable. Does the insurer or his agent have a duty to tell the purchaser or to remind him, or should it be deemed that the purchaser is aware of the procedure? What is the duty of proof? All such issues should be discussed, but not in this paper.

<sup>53</sup> <http://www.taoche.com/zhuanti/chexian/renbao/17913.shtml> (Accessed on 10 June 2014).

<sup>54</sup> [http://article.chinalawinfo.com/Article\\_Detail.asp?](http://article.chinalawinfo.com/Article_Detail.asp?) (Accessed on 10 June 2014)

<sup>55</sup> In China, some employers buy insurance cards and give them to their employees as welfare of his company.

contract.<sup>56</sup> In this case the right of claim was assigned to Gu by the life insured's beneficiaries, so his claim was supported by the court.

The case raises another issue, *i.e.* whether Mr Gu as the purchaser of the card has the right to claim against the insurer if the claim right is not assigned to him? The answer is negative. First, where a person buys a card as a gift for another person, all the contractual rights (including activating the card online and the right to claim) are transferred to the other person. The other person who activates the card is the proposer and the insured, and the beneficiary must be the insured himself or his legal successors. The person who buys the card is neither the proposer nor the life insured's beneficiary, therefore has no right to claim.

### ***Issues on the duty of disclosure in an insurance card transaction***

Because the online insurance transaction and card insurance transaction involves no paper documents, the whole procedure is completed online. It is therefore impossible for an insurer or his agent to provide a paper explanation of exclusion clauses and ask the proposer to sign the document to prove that the insurer or his agent has performed the duty.<sup>57</sup> This has caused a lot of disputes on whether or not the insurer has performed his duty of the explanation of the terms, especially where the insurance card is activated by an insurer's employee or an agent. The following two cases illustrate the problem, in both cases the cards were activated by agents.

In *Longmei Han and Na Liu v Yangguang Life Insurance Co Ltd*,<sup>58</sup> Mr Liu, from a small village of Jiangsu Province, bought a self-service insurance card from the insurer's agent in March 2009.<sup>59</sup> Liu did not have a computer and could not access to the insurer's website, so he asked the agent to activate the card on his behalf. When the agent was helping Liu to fill the e-proposal form on the insurer's website, he put "farmer" in the box of "Insured's Occupation" without asking Liu about his occupation. The agent wrongly believed that Liu was a farmer in the village. In fact Liu was a lorry driver for transport business by using his own lorry. The card was successfully activated by the agent and the insurance contract was concluded with the issue of an e-policy. The duration of the insurance was between 16 March 2009 and 15 March 2010. On 20 April 2009, Liu was killed in an accident. His beneficiaries claimed against the insurer but the insurer rejected the claim on the ground of non-disclosure of material information by the proposer. If the fact that he was a lorry driver had been disclosed the insurer would not have accepted the risk and the internet system itself would reject the application automatically.<sup>60</sup>

The court held that the insurer cannot reject the claim because the proposer did not breach the duty of good faith. According to the Insurance Law, the proposer's duty of disclosure is to truthfully answer the questions raised by the insurer or his agent.<sup>61</sup> In this case the agent did not ask the proposer about his occupation, the mistake was made by the agent's negligence.

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<sup>56</sup> According to art.79 of the Contract Law, "The creditor may assign to a third party all or part of his rights under the contract, except in one of the following circumstances:

- (1) The assignment is not permitted by virtue of the nature of the contract;
- (2) The assignment is not permitted by virtue of the agreement of the parties;
- (3) The assignment is not permitted by virtue of provision of law."

In this case Mr Gu was assigned with the right of claim by the life insured's beneficiaries, his right is not covered in any of the above exceptions. So his claim was supported by the court.

<sup>57</sup> It is the practice in traditional insurance transaction that, in a proposal form, there is a declaration which states, *inter alia*, that "... the insurer explained the policy terms and exclusion clauses..." The proposer is asked to sign a proposal form and the declaration. That is evidence that the insurer performed his duty.

<sup>58</sup> This case was cited by Jing Wang in her book. See Jing Wang, *Insurance Cases – Rules of Judgement and Application of Laws*, (2013), p46.

<sup>59</sup> The cost of the card was ¥100, the insured amount for medical treatment was ¥10000 and for death payment was ¥60000.

<sup>60</sup> The insurance covers only those people whose occupations fall into the categories 1, 2, 3, 4, in the occupation classifications form, but not those whose occupation fall into the categories 5 and 6. A lorry driver was classified into category 6.

<sup>61</sup> Art.16 of the Insurance Law 2009 provides: "When concluding an insurance contract, an insurer may make inquiries concerning relevant details of the insured subject matter, or of the insured. The proposer shall truthfully disclose such details to the insurer."

In another case of *Jinglong Dai v Huaxia Life Insurance Company Jiang Su Branch*,<sup>62</sup> Jun Dai, the son of Jinglong Dai (the plaintiff), bought an insurance card for accident insurance on 15 Feb 2010. The card was activated by the agent who sold the card to Dai. The insurance contract was concluded and became effective immediately for one year. On 20 Sept 2010, Dai was killed in an accident when he was riding his motor bicycle. The certificate issued by the Traffic Police Officer shown that the accident was caused by Dai who was riding an old motor bicycle without valid safety technical inspection (equivalent to MOT). The insured's father claimed, but was rejected by the insurer on the ground that the risk was excluded. The court made judgement for the insurer.

Several issues have arisen from the above two cases (1) how the parties perform their duties of good faith in a card transaction; (2) how they perform their duties if the card was activated by the insurer or his agent on behalf of the proposer.

In the judgement of the second case (*Jinglong Dai*), the court held that the insurer placed all policy terms and exceptions on the website and the activation system, the major terms especially the exclusion clauses were highlighted with "BOLD" words, that design was sufficient to indicate that the insurer performed the pre-contract duty to explain the terms of the contracts. If the proposer himself completes the activation, he must read the terms first and click "Agree" and "Confirm", then he can access into the activation system. If the activation is successful, that means that the proposer has read and accepted all policy terms including the exclusion clauses.

The Supreme People's Court's Second Interpretation on Certain Questions Concerning the Application of the Insurance Law of the Peoples' Republic of China<sup>63</sup> has recently provided an answer to the question about the proof of insurer's performance of his pre-contract duty of explanation insurance terms and exclusion clauses to the proposer. Article 12 of the SPC's Interpretation provide "Where the insurance contracts are concluded through internet, telephone or other similar ways, if the insurer performs his duty of explaining exclusion clauses by webpage, audio or video or other similar ways, the People's Courts should deem that the insurer has performed his duty".

The problem is that where the card is activated by an insurer's employee or its agent, it is difficult to determine whether the employee or the agent has performed his explanation duty properly. It is suggested that (1) if an employee or an agent helps the proposer to activate the card in front of the proposer, during the process of activating, the employee or the agent should read and explain the terms for the proposer who is illiterate, or should ask the proposer to read the terms and exclusions clauses if the proposer is literate. A written declaration should be signed by the proposer saying "the policy terms have been clearly explained to me". (2) If the activation is completed by telephone communication between the proposer and the insurer, a recorded message should be taken to prove that the parties performed their duties during the process of activating the card.

### ***Whether the card is returnable?***

Another issue with the insurance card transaction is whether the card can be returned to the insurer if the card becomes invalid due to the card-holder's failure to activate the card within the specified period. Some insurance cards contain a vague term that the card is non-returnable,<sup>64</sup> but does not explain under what circumstances the card cannot be returned. The term seems to indicate that the card cannot be returned by any reason.

It could be suggested that whether the non-returnable term is fair for the card-holder depends on different situations. If, for instance, the card is not activated within the specified period due to the card-holder's own fault, it is reasonable to make the card non-returnable. However, what is the consequence if there is no fault on the part of the card-holder for not activating the card? for example, the purchaser of the card is not told by the seller (the insurer or his agent) that the card must be activated before it becomes expired; or if the insurer rejects the application because the proposer does not meet the conditions of the insurance; or if the proposer is not happy with the exclusion clauses

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<sup>62</sup> See Tian Yin and Zili Ren, *Insurance Law Review*, (2012), p147.

<sup>63</sup> The Supreme People's Court Second Interpretation on Certain Questions Concerning the Application of the Insurance Law of the Peoples' Republic of China was passed by the Judgement Committee of the Supreme People's Court on 6 May 2013 and became effective on 8 June 2013.

<sup>64</sup> <http://icard.chinalife-p.com.cn/i-card/longToJumpAction> (Accessed on 27 June 2014).

and does not want to go ahead to complete the activation procedure. Under these situations, should the insurer return the cost of the card to the card-holder?<sup>65</sup> It is submitted that the person should be allowed to return the card if there is no fault of the purchaser of the card or the card-holder.<sup>66</sup>

The above questions are, in fact, about the matter of the effectiveness of the preliminary agreement. It is submitted that because a preliminary contract is binding, the card cannot be returned if it is the purchaser's own fault for not activating the card negligently or knowingly within the period as specified on the card. It should be deemed that the proposer gives up the right to apply for the insurance, so the card cannot be returned.<sup>67</sup> For the other situations as mentioned above, the card should be returnable. Otherwise it is unfair to the proposer who pays the money for the card but does not have the opportunity to be covered by the contract.

### ***Who is the proposer in the insurance card transaction?***

In most situations a person buys an insurance to insure himself, so the purchaser of the card is the proposer and also the insured of the insurance contract. However, sometimes a person may buy an insurance card as a gift and give it to a friend or other family members, or he may buy an insurance card on behalf of another person.

A proposer is the person who enters into an insurance contract with the insurer. It is important to determine who the proposer is, because it relates to the performance of pre-contract duties by the proposer and also the insurer. The Insurance Law 2009<sup>68</sup> requires the proposer (not other person) to perform the duty of disclosure, and the insurer to explain the policy terms to the proposer (not to other person). This issue should be discussed in conjunction with the issue when the insurance contract is deemed to be concluded. To determine who the proposer is equivalent to determine who enters into the contract with the insurer. In the insurance card transaction, to identify who is the proposer depends on the determination of the stage when the contract is concluded – namely at the time of buying the card or at the time of activating the card. This also depends on whether a person buys a card for himself or for another person. If the purchaser is also the person who activates the card, he is of course the proposer. If the purchaser of the card and the person who activates the card are different persons, the person who activated the card is the proposer. The policy terms and the exclusion clauses can only be read online by the person who activates the card during the process of activating the card, by this way the insurer explains the terms to the proposer and at the same time, the proposer is required to answer questions raised by the insurer online, he performs his duty of good faith by truthfully answering the questions.

### **Conclusions**

Electronic transaction of insurance business has become increasingly popular in China's insurance market in recent years due to its advantages (simpler, quicker, and cheaper) than the tradition way of insurance transaction. But the lack of rules of law to govern this kind of insurance activities gives rise to difficulties and many disputes in

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<sup>65</sup> Xuesheng Liu raises the same issue and argues that if the view of “a preliminary contract and a main contract” is deemed as a good way to explain the insurance card transaction, a problem should be solved, namely whether the purchaser may return the card and get the money back in the following situations:

- (1) if the purchaser does not activate the card within the period specified on the card; namely whether the purchaser is binding to activate the card;
- (2) if the activation is not successful due to the fact that the proposer's application is rejected by the insurer after the examination of the online proposal;
- (3) if the proposer does not want to take out the insurance after reading the terms of the policy, especially the exclusions, during the process of activating the card.

See Xuesheng Liu, *Insurance Law Review*, edited by Tian Yin and Zili Ren, (2012), p275.

<sup>66</sup> Xiaohua Xu, Manager of Internal Management Department of China Life Insurance Company, Jiangsu Province, pointed out that the proposer can return the card if it is not successfully activated online. Xu gave a talk on the seminar on “China Electronic Policy - Law and Practice, held on 9-10 June 2012 in Nanjing, Zhejiang Province, China. His comment was cited in the book of *Insurance Law Review*, edited by Tian Yin and Zili Ren, (2012), p270.

<sup>67</sup> See also Xuesheng Liu, *Insurance Law Review*, edited by Tian Yin and Zili Ren, (2012), p275.

<sup>68</sup> Arts.16 and 17 of the Insurance Law 2009.

industrial and judicial practice. This paper has examined a number of issues relating to the “self-service insurance card” transaction, focusing on the matters of formation of insurance contracts via “self-service insurance card”, the issue of the performance of good faith in online insurance business.

There are many different views on the formation of insurance contract. It seems that the view about the two interdependent contracts (preliminary contract for purchasing the insurance card and the main contract for activating the card) offers an appropriate explanation about the formation of the insurance contract in the insurance card transaction, but the view is still in need of further development. The performance of pre-contract duty of good faith by the two parties in online insurance business is different from that in the face-to-face formation of insurance contracts. To show the proof of performance of the duty is an area of difficulty. A number of suggestions have been made in relation to the performance of good faith in online insurance transaction.

To keep pace with the rapid development of insurance card business in China, it is necessary to develop new legal rules to govern the activities in order to facilitate a healthy development of the business.