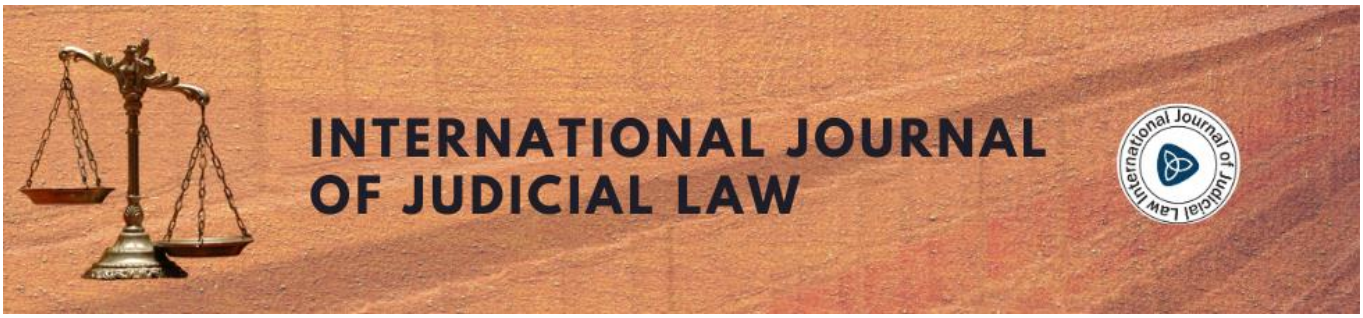




Reducing Late Payment Penalties under Mongolian Law with Reference to Chinese Law

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Article Info

ISSN (online): 2583-6536

Volume: 05

Issue: 05

Received: 13-07-2026

Accepted: 12-08-2026

Published: 11-09-2026

Page No: 74-78

Abstract

Background. Mongolian law caps both the daily rate and the total amount of penalties for delayed performance, but permits a further reduction where an amount within those limits is manifestly excessive.

Objectives. This article examines the grounds for reducing late-payment penalties after the statutory cap has been applied, with reference to Chinese law.

Methods. The study combines statutory interpretation with close reading of three purposively selected decisions of the Supreme Court of Mongolia. Chinese legislation and Guiding Case No. 166 provide the comparative materials.

Results. Corrections to calculations, findings of payment liability, and discretionary reductions perform different functions. Supply negotiations and disruption of a company's business may support a reduction without excusing payment. Their separate relevance and their connection to the amount reduced nevertheless require explanation. Mongolia's caps and China's loss-based standard regulate different matters and cannot be compared as interchangeable percentages.

Conclusion. Courts should identify the person affected by each circumstance, its timing and legal relevance, any effect already accounted for elsewhere, and its connection to the extent of reduction. The proposed analysis concerns the reasoning in the selected decisions and does not establish a general rate of reduction.

DOI: <https://doi.org/10.54660/IJL.2026.5.5.74-78>

Keywords: Judicial reasoning, Late-payment penalties, Loss-based standard, Mongolian civil law, Statutory caps

1. Introduction

Article 232 of Mongolia's Civil Code sets caps on the total amount of contractual penalties and the daily rate of penalties for delayed performance. It also permits courts to reduce amounts that are manifestly excessive. Thus, even where the creditor has limited the claim to 50% of the value of the unperformed obligation, the court may make a further reduction. This article asks why an individual assessment remains necessary after the cap has been applied, and why circumstances insufficient to excuse liability for late payment may nevertheless support a reduction ^[1].

The analysis is confined to the delayed payment of a price or remuneration in business transactions. It does not provide a general account of contractual liability in Mongolia and China or address penalties for breach of non-compete obligations. Employment contracts, consumer contracts, lending rates, and administrative late-payment surcharges also fall outside its scope. For Chinese traders, these limits help distinguish the functions of statutory caps and reductions in individual cases: an amount below the cap may not be awarded in full, while business difficulties may not be sufficient grounds for reducing it.

Chinese scholarship has already examined the adjustment of agreed damages extensively. Wang Liming discusses the constraints imposed by the loss-based approach, the requirement of a party's application, and the function of securing performance. Guan Yunbiao distinguishes the legal assessment of excessiveness from its factual basis and examines the burden of proof. Yao Mingbin has also considered whether an agreed amount within a statutory range may be reduced at the court's discretion. The

coexistence of a cap and a power to reduce is therefore not a new discovery. This article examines the further question of why circumstances surrounding performance may retain independent significance once the cap has operated, and how they can justify the eventual extent of reduction ^[2-4].

2. Materials and Methods

The judicial materials comprise three decisions of the Supreme Court of Mongolia: a 2022 construction remuneration case, a 2025 diesel supply case, and a 2025 share purchase price case. They respectively concern refusal of a further reduction, reduction of an amount within the cap, and reduction of the capped amount by half. The term “commercial” refers here to the business nature of the transactions. Both parties were companies in the first two cases, whereas the share transaction involved individual shareholders. The method combines statutory interpretation and close reading of judicial reasons; it does not use three purposively selected cases to estimate a national rate of reduction. The comparison with China draws on current legislation and Guiding Case No. 166 and does not constitute a symmetrical empirical sample of judgments from the two countries.

3. Results

3.1. The Different Objects of Monetary Control in The Two Legal Systems

In Article 232 of Mongolia’s Civil Code, *анз* is the general category of contractual penalty, encompassing *торгууль* and *алданги*. The latter accrues by the day of delay and is referred to here as a penalty for delayed performance. Paragraph 4 limits the total amount to 50% of the value of the unperformed obligation. Paragraph 6 caps the daily rate at 0.5%. Paragraph 8 permits the court, having regard to the circumstances of the case, to reduce a penalty that is manifestly excessive. The aggregate limit, the rate of accrual, and the burden in the individual case are distinct objects of review ^[1].

The rate of 0.5% does not apply automatically where the parties have agreed no rate. Article 232(7) separately addresses cases in which no penalty for delay has been agreed; a right to claim cannot be inferred simply from the maximum permitted rate. Nor is the denominator for the 50% cap necessarily the total contract price. Amounts already paid, not yet due, or outside the payment obligation must first be properly accounted for in the calculation. A resulting decrease concerns entitlement or calculation and is not necessarily a discretionary reduction.

Article 585 of China’s Civil Code permits an appropriate reduction, on a party’s application, where the agreed damages are excessively high relative to the loss. Loss under Article 584 includes the expectation interest and is subject to the foreseeability limitation. Article 65 of the Supreme People’s Court’s Interpretation on the General Provisions of the Contract Book of the Civil Code builds on that basis, while also considering the parties, the type of transaction, performance, fault, and the circumstances surrounding performance. Its general benchmark of an amount exceeding the loss by 30% compares agreed damages with loss, not with the contract price. Nor does it require the amount in every case to be reduced to 1.3 times the loss ^[5, 6].

Mongolia’s 50% and China’s 30% therefore cannot be used directly to rank the strength of creditor protection. The former is an aggregate cap calculated by reference to the value of the

unperformed obligation; the latter is a general benchmark for excessiveness measured against loss. Under Chinese law, other discretionary factors cannot displace the loss-based foundation. Under Mongolian law, the absence of an itemized loss standard in Article 232(8) does not establish that the creditor’s loss and interest in performance are irrelevant.

An agreed penalty can relieve the creditor of the burden of proving each item of loss and secure timely payment. Yet the absence of a requirement to prove the entire loss precisely when making the claim does not eliminate the need to explain the interest protected once excessiveness is in issue. Trade credit periods, instalment arrangements, and concessions by the creditor concerning security may all affect that interest. Considering them does not authorize an arbitrary enlargement of recoverable loss. It explains why the agreed liability took its particular form and what the excessiveness assessment concerns.

3.2. The Reasons in Three Decisions and Their Limits

3.2.1. Construction Remuneration and The Distinction Between Correction and Discretionary Reduction

In Decision No. 001/XT2022/01196 of 1 December 2022, the Supreme Court of Mongolia considered unpaid construction remuneration of MNT 75,000,000 and an agreed daily penalty rate of 0.05%. The claimant sought a penalty of MNT 22,087,500, and the first-instance court awarded MNT 19,162,500. The defendant continued to argue that no penalty was payable. The Supreme Court upheld the disposition ^[7].

A comparison of the amount claimed with the amount awarded could misleadingly classify this case as a discretionary reduction. Paragraph 15 of the reasons, however, explains the final amount as the result of applying the correct period, base amount, and agreed rate, with reference to Article 232(6). Paragraphs 17 and 18 separately apply Article 232(8) and find no specific circumstances supporting a further reduction. The difference between the claim and the award therefore cannot simply be treated as the extent of judicial discretion exercised.

The decision also expressly recognizes that an amount within the statutory cap may still be manifestly excessive, but requires the parties to address the reduction in adversarial argument and the court to give factual and legal reasons. The defendant had not proved facts sufficient to support its position. The mere existence of a judicial power to reduce did not entitle it to a reduction. The decision thus preserves both the possibility of reduction and the agreement’s status as the starting point.

3.2.2. Diesel Supplies and Negotiations That Do Not Excuse Payment

Decision No. 001/XT2025/00133 of 27 June 2025 concerned diesel supplies between companies. The amended claim for the purchase price was MNT 2,539,204,020. Penalties calculated cumulatively at the rates agreed in two contracts totalled MNT 5,876,676,730.60, but the claimant sought only the capped amount of MNT 1,269,602,010. The first-instance court reduced that amount further to MNT 1,000,000,000. The appellate court rejected the penalty claim in its entirety, and the Supreme Court reinstated the first-instance disposition ^[8].

The dispute arose against a background of fuel theft, reconciliation of deliveries, and payment negotiations. In paragraphs 16 and 17 of its reasons, the Supreme Court noted that some fuel had been returned to the buyer and that other

disputed supplies and the corresponding claims had been excluded. Payment was already overdue before the relevant events. Although the parties discussed settlement of their accounts, they did not agree to alter the payment arrangements, and the creditor continued to demand payment. These findings show that a dispute over part of the supplies, or continuing negotiations, does not automatically relieve the debtor of liability for delay on the entire purchase price.

While upholding payment liability, the Supreme Court also maintained the first-instance court's further reduction of the capped amount. The outcome can be understood as recognizing that the same circumstance may affect the amount of liability without excusing liability itself. The published reasons do not, however, fully explain which period, disputed supplies, or interest accounts for the difference between the cap and the award of MNT 1 billion. That leaves room to question the adequacy of the reasons. It does not establish that the judges failed to examine the evidence, nor does it justify treating the percentage reduction as a general standard for supply contracts.

The case also requires two effects to be distinguished. Removing disputed supplies had already corrected the debt base. Further reliance on the background negotiations required an explanation of an effect not already accounted for by that correction. If that effect concerned the degree of responsibility rather than the base amount, the same circumstance could remain relevant. Repeating that "a dispute existed" would not, by itself, explain the further reduction.

3.2.3. Business Difficulties in The Share Purchase Price Case

Decision No. 001/XT2025/00200 of 13 November 2025 concerned a sale of shares between individual shareholders. The price of MNT 89,000,000 was payable in three instalments, the last falling due on 1 October 2024. The agreed daily penalty rate was 0.5%. The claimant sought MNT 44,500,000 in penalties. The first-instance court reduced that amount by half to MNT 22,250,000, and the Supreme Court upheld the reduction^[9].

Paragraph 14 of the reasons approves the first-instance court's consideration of the termination of a franchise agreement and the disruption of the company's business as grounds for reduction. Paragraph 15 simultaneously states that the deterioration in the business was not attributable to the claimant and did not excuse the defendant's obligation to pay the share purchase price. The different uses of business difficulties in determining liability and its amount are therefore particularly clear. Two connections nevertheless require explanation.

First, the business disruption affected the target company, whereas the person obliged to pay the price was the individual acquiring the shares. A decline in the company's earnings may affect the value of the shares, but it does not necessarily establish the purchaser's inability to pay. The court should identify whether it is considering a change in the value of the subject matter or the debtor's payment capacity, and state the factual basis for each. Second, the franchise agreement was terminated on 13 October 2024, after the final instalment had fallen due. That later event cannot retrospectively explain all the delay that had already occurred. If business obstacles arose earlier, the court should

identify when they arose and became known. If it is considering the burden at the time of judgment, it should acknowledge that this is not the original cause of delay.

This does not mean that subsequent business conditions can never be relevant under Article 232(8). Their relevance must, however, be explained. Nor does halving the capped amount in one case create a new cap of 25% of the unpaid price. Applying the same reduction without comparing the facts would mistakenly turn a discretionary outcome into a percentage rule.

4. Discussion

4.1. Explaining A Reduction After the Cap Has Been Applied

4.1.1. Identifying the Stage at Which the Amount Changes

The review should distinguish calculation under the law and contract, application of the aggregate cap, and assessment of manifest excessiveness. Where the base amount remains unchanged, there is a single debt, and only one penalty for delay has been agreed, the amount entering the discretionary review can be expressed as $K = \min(P \times r \times t, 0.5P)$, where P is the value of the unperformed obligation, r is the applicable daily rate, and t is the number of chargeable days. Part payments, instalments falling due at different times, or differing rates require calculation in separate segments. This expression is not a formula for discretionary judicial reduction.

Suppose the principal is 100, the daily rate is 0.5%, and the calculation period is 200 days. The accrued contractual amount is 100, and the cap is 50. Even if twenty days are removed from the calculation, the accrued amount remains 90 and the cap remains 50. If the court ultimately awards 40, it cannot explain the result merely by referring to the exclusion of twenty days. It must also explain the further reduction of 10 within the cap. This is a hypothetical example, not a reconstruction of the calculation in the diesel supply case.

It follows that not every circumstance favourable to the debtor must produce an additional allowance. The cap may already absorb the monetary effect of a correction, and a discretionary reduction should not be made merely to give that correction a visible effect. Conversely, the cap does not necessarily resolve every question of excessiveness in an individual case. Any further reduction starts from the legally supportable amount within the cap and concerns the burden that remains.

4.1.2. Explaining the Independent Use of The Same Circumstance

Negotiations that do not result in an agreed extension of time may still be relevant to the degree of responsibility for a particular period of delay. Likewise, business disruption that does not excuse payment is not necessarily irrelevant to the additional amount payable. The court must nevertheless explain why the circumstance matters for that further purpose. Repeated reference to the same fact is not necessarily impermissible double counting. The problem arises where its adverse effects have already been addressed through the base amount, the period, or another aspect of liability, yet it supports a further reduction without a new reason.

The rules on delay and creditor delay in Articles 222–224 of

Mongolia's Civil Code also show why facts must be addressed at the appropriate stage. A creditor's failure to provide necessary cooperation may first affect whether the debtor is liable for delay at all. Such a failure should not invariably be reserved for a discretionary discount on grounds of fairness under Article 232(8). The rule directly governing the circumstance should be applied first; the court can then assess whether a manifestly excessive penalty burden remains ^[1].

For business difficulties, the analysis should at least distinguish who bears the risk, when the difficulty arose, how the contract allocates that risk, and any relevant conduct of the creditor. A purchaser's unilateral intention to pay for shares out of the company's earnings differs from an agreement making payment conditional on those earnings being realized. Articles 533, 590, and 593 of China's Civil Code address substantial changes in circumstances, force majeure, and third-party causes respectively. Although they do not determine the position under Mongolian law, they provide a useful comparative check: discretionary reduction should not become an unexplained means of bypassing the rules establishing liability and reallocating ordinary business risks ^[5].

4.1.3. Connecting A Relevant Circumstance to The Extent Of Reduction

Accepting that some reduction is appropriate does not explain why the amount should be halved. Where loss cannot be calculated precisely, the court need not supply a single definitive formula. It can still identify the interests that should be protected, the factors that genuinely justify relief, and why a smaller or larger reduction would be inappropriate. Explaining the appropriate range permits closer scrutiny than an abstract appeal to fairness without eliminating judicial discretion.

This article therefore proposes that judgments separately identify the amount claimed, the amount calculated under the law and contract, the amount within the statutory cap, and the final award. For any further reduction, the reasons should identify the facts relied on, their legal purpose, the effect not already accounted for at another stage, and the basis for the extent of reduction. Some of the four figures may coincide. The purpose is to identify where any difference arises. This is an interpretive proposal, not a claim that Mongolian legislation expressly prescribes this checklist.

4.2. Comparative Implications of Chinese Law and Their Limits

In Guiding Case No. 166, the creditor applied for the discharge of asset preservation measures in accordance with a settlement agreement. The debtor then failed to make the promised subsequent payments and sought a reduction of the agreed damages of CNY 800,000. The court refused the reduction, emphasizing the conduct contrary to good faith. The case predates the entry into force of China's Civil Code, but the Supreme People's Court identified Articles 7 and 585 as the corresponding current provisions when publishing it ^[10].

The facts are not the same as those of the diesel supply case, so the different outcomes do not show which country is more protective of creditors. The meaningful comparison is that negotiations do not inherently favour a reduction. Where one party has relinquished asset preservation in reliance on a

promise to pay, a subsequent breach may strengthen the case for enforcing the agreement. The content of the negotiations and the parties' acts of reliance require examination; "negotiation" should not be assigned a fixed effect. Nor can the loss standard in this case be inferred merely from the ratio between the unpaid debt and the agreed damages. Principal, interest already accrued, and additional loss from subsequent delay are different matters.

Article 64 of the Interpretation on the General Provisions of the Contract Book requires the party in breach seeking a reduction to prove that the agreed damages are excessive. The non-breaching party asserting that the amount is reasonable must also submit corresponding evidence. Article 66 provides for judicial clarification so that, when a defence denying liability is rejected, the party can make clear whether it seeks adjustment in the alternative. Both parties need to supply the facts on which the assessment rests. The debtor should explain and prove the alleged negotiations, payments, or changes in business conditions. The creditor should also address matters within its knowledge, such as financing costs and arrangements securing performance ^[6].

These provisions cannot be used directly to determine the burden of proof under Mongolian law. The construction remuneration case requires evidential support, argument from both parties, and judicial reasons. It establishes that a reduction cannot rest solely on abstract fairness. A further comparison of whether the two countries share the same procedural structure would require examination of Mongolian procedural law and additional decisions.

The three Mongolian decisions obtained for this study do not fully develop the calculation of loss. This does not prove that the creditors suffered no loss or that the case files contained no relevant evidence. The article therefore evaluates only how the published reasons connect the statutory provisions to the amounts awarded. It does not speculate about the parties' actual ability to pay or attempt to quantify judicial error. The practical recommendations for transactions involving China and Mongolia are likewise confined to specific arrangements: clarify when each delivery or instalment becomes payable, distinguish disputed from undisputed amounts, record whether negotiations produced an agreement to extend time, and retain evidence of credit arrangements and loss.

Comparing domestic judgments from the two countries does not mean that Mongolian law applies automatically whenever a Chinese party participates. A cross-border dispute still requires prior identification of jurisdiction, the method of dispute resolution, and the governing law. Nor can three cases establish that reduction rules have affected the volume of bilateral trade or investment flows. Their direct value lies in making contractual liability and evidential arrangements more intelligible.

5. Conclusion

A statutory cap fixes the upper boundary of a penalty claim, but whether an amount within that boundary should be reduced still depends on the individual case. A judicial power to reduce does not permit the court to disregard a valid agreement within the cap. The three Mongolian decisions illustrate the distinct roles of corrections to calculations, negotiations, and subsequent changes in business conditions. Where a further reduction is made, the court should explain why the relevant circumstances retain independent significance and how they support the extent of reduction

chosen.

Chinese law takes loss as its foundation, while Mongolian law limits accumulated liability through fixed caps. The same percentage cannot serve both systems. What can usefully be compared is how courts explain the process by which an amount is determined. Although no precise formula is required for every case, the court should explain how review of the agreed amount leads to the award. Business risk, negotiations, and interests in performance become assessable reasons for reduction only when connected to the specific facts.

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How to Cite This Article

Donoloi B. Reducing late payment penalties under Mongolian law with reference to Chinese law. *International Journal of Judicial Law*. 2026;5(5):74-78. doi:10.54660/IJL.2026.5.5.74-78.

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