

Determining Rights and Obligations

By Peiming Yang and Eve Zhang

The principal purpose of establishing a contract is for the parties to agree on their rights and obligations. Disputes frequently arise in practice as to the parties' understanding of whether a contractual term enshrines a party's right or obligation.

Two Case Studies

(i) A and B signed a real estate exclusive sales contract, where A commissioned B as a general agent, for the sale of real estate of malls developed by A. Article 4 of the contract, titled "measure of sales warrant", stipulated that "B shall achieve the sales target within the determined sales period. If B fails to achieve the sales target within the determined sales period, B shall purchase the designated property from A within seven days after the end of the sales period as compensation for failing to meet the sales target, and B shall pay the amount in full." A subsequently released a notice of discharge, pursuant to B's alleged breach of another obligation under the contract. Half a year later, A removed B's sales personnel from the sales sites. B denied the alleged breach, and requested that the court order A to sell all remaining unsold stores to B at the price which compensates B for the failure to meet the sales target, arguing that A made it impossible for B to sell.

(ii) C and D signed a plant leasing contract, where D agreed to rent a plant owned by C. Article 3 of the contract stated "term of lease: from 1 April 2010 to 31 March 2013. Following expiration of the contract, D has the right to renew the lease for three years as necessary. The annual rental is RMB X Yuan/m² floorage. The option to renew was to be requested at least a month prior to the expiry of the tenancy. On 17 February 2013, D exercised the option to renew, pursuant to Article 3. C argued that the renewal was not part of the contract, and should be mutually agreed upon by the parties. After C refused D's attempt at renewal, D requested that court order C to continue to perform the plant leasing contract, in accordance with Article 3.

如果您需要本出版物的中文本，请与下列人员联系：

郭建良: (86 21) 3135 8756
Publication@llinkslaw.com

If you would like other Llinks publications, please contact:

Roy Guo: (86 21) 3135 8756
Publication@llinkslaw.com

Llinks Law Offices
www.llinkslaw.com

Determining Rights and Obligations

The Decisions

The above two cases pose a common question: whether the relevant contractual terms are terms of right or obligation.

- In the first case, Article 4 states that If B fails to achieve the sales target within the determined sales period, B shall purchase the designated property from A within seven days of the end of the sales period. This provision is to be read in conjunction with the title of the article, “measure of sales warrant”. This suggests that the article was originally intended to be a measure of the sales warrant, allowing A to restrict B. B is under the obligation to perform, should B fail to achieve the sales target within the determined sales period. Correspondingly, Article 4 is a term of right, rather than obligation, for A, which entitles A to request B to purchase relevant estate. B has no right to claim purchasing against A based on Article 4, which is a term of obligation for him, rather than a term of right. At first instance, the court rejected B’s claim based on reasoning consistent with the writer’s opinion.
- In the second case, although the first sentence of Article 3 expressly states that the lease ends on 31 March 2013, the second sentence expresses that after the expiration of the contract, D has the right to renew the lease for three years. The rental for renewal, being an essential part of the rental relationship, is also expressly agreed. Therefore, this clause constitutes a term of right enjoyed by D in relation to the lease renewal. The provision stating: “the request for renewal shall be raised within a month prior to the expiry of tenancy” constitutes a time limit restricting D’s exercising of the right. Given that D exercised the right to renew within the stipulated period, C is bound to accept the renewal. C’s claim that the renewal shall be mutually negotiated is inconsistent with the wording of the Article. We represented D in the suit and presented the above argument to the court. The case was eventually settled under the court’s jurisdiction and D continued to rent the disputed plant.

Draft Carefully

It is important to understand whether a contractual term is a term of right or obligation for a party, which concerns whether claim of rights under the article will be upheld by the court. We suggest the following when drafting contractual terms:

- **Understand the methods of contractual interpretation which are to be employed according to the law.** This concerns Article 125 of the *PRC Contract Law*, which shows that there are methods of literal, overall, teleological, customary and integrity interpretation that may be used to construe a term.
- **Pay attention to the accuracy and clarity of language expression and wording. Literal interpretation is the starting point in contract interpretation.** Use wording that states a party’s right or duty more explicitly, for example, “has the right/may (but has no obligation)” or “shall/ is obliged to (but has no right)”. Avoid wording which is ambiguous, vague or contradictory.

Where disputes arise as to contractual interpretation, courts generally take the above method into account in determining the parties’ true intention in practice.

Determining Rights and Obligations

Contact Details

If you would like to know more information about the subjects covered in this publication, please feel free to contact the following people or your usual Llinks contact.

Shanghai	Beijing
David Yu Tel: (86 21) 3135 8686 David.Yu@llinkslaw.com	Charles Qin Tel: (86 10) 8519 2266 Charles.Qin@llinkslaw.com
Charles Qin Tel: (86 21) 3135 8668 Charles.Qin@llinkslaw.com	
Ming Zhang Tel: (86 21) 3135 8777 Ming.Zhang@llinkslaw.com	
Peiming Yang Tel: (86 21) 3135 8787 Peiming.Yang@llinkslaw.com	

This article was first published in *China Law & Practice*, January/February 2014, Volume 28, Number 1.