Oct 2013. Vol. 3, No.2 ISSN 2307-227X
International Journal of Research In Social Sciences

www.ijsk.org/ijrss

THE EFFECTS OF INTENTIONAL BREACH OF CONTRACT WITH EMPHASIS ON INTERNATIONAL INSTRUMENTS

Ebrahim Shoarian , Roya Shirin Beig Pour[2]
Associate Professor, Law Department, Faculty of Law and Social Sciences, University of Tabriz, Iran
(e_shoarian@tabrizu.ac.ir)
Research Assistant in Private Law, University of Tabriz[2]

ABSTRACT

When breach of a contract takes place it is necessary to distinguish between different kinds of breach considering that their legal effects are not the same. Non-performance can take various forms such as fundamental and non-fundamental breach or anticipatory and actual breach. However, from the standpoint of will, the non-performance or breach can be divided into intentional and unintentional one. When the breach of the contract is willful, the Law cannot be apathetic to obligor who has behaved in bad-faith. To this end, some legal systems have been upgraded and changed the remedies in favor of obligee. Also, in some International Instruments like UPICC, PECL, and DCFR intentional breach has been encountered with special remedies. In this article we will examine the particular effects of intentional breach with emphasis on above mentioned documents.

KEY WORDS: *Contract, Intentional Breach, Effects, International Instruments*

INTRODUCTION

Contracts lie at the heart of commercial life and development in national and international relations have increased its importance. In spite of the fact that in most cases the parties live up to their contract which is appearance of their will, however there are cases where the contracting parties or one of them do not fulfill its obligations and as a result the non-performance occurs.

In all legal systems as well as international instruments the breach of the contract is not irresponsible and so they have set forth special rules to respond such a non-performance which in most cases show itself in the form of compensation in damages.

Remedies for intentional breach have various types and remedies vary depending on the type and severity of the violation. In this regard it should be noted that the fundamentality of breach may be relevant in assessing the severity of the violation.

Given the fact that intentional breach of the contract is reflection of the non-performing party's aggressive behavior their effects are different. In this connection, many legal systems as well as international instruments consider ill will as an important factor is establishing whether the non-performance is fundamental or not. Furthermore, in domestic law of some countries as well as some international instruments, the intentional breach of the contract has the effects that extend breaching party's liability to unforeseeable losses as well. Also, in case of intentional breach the aggrieved party

entitles to terminate the contract and also under some legal systems provisions on intentional breach of contract entitles the aggrieved party to demand punitive damages.

1. CONCEPT OF INTENTIONAL BREACH OF CONTRACT

Apart from the fact that in some international instruments the state of mind play a crucial part in assessing the fundamentality of the breach they provide no definition of intentional breach

It should be noted that giving a comprehensive definition for intentional or willful breach is a very difficult task considering that it has a close connection with the amounts of damages that can be awarded on the grounds of intentional breach. As it is evident from the subject of intentional breach it has close connection to do with the intent of the breaching party. In this regard, it has been suggested that willful act requires intent to injure, that is, both an intentional act and an intentional injury.[1] So, briefly we can define intentional breach as one in which the breaching party intent to do damages to non-breaching party or to take advantage of breach which requires both an intentional act and an intentional injury. In this connection, it has been argued that there is a difference between opportunistic breach and efficient breach.[2] Also, it should be said that breaching the contract in bad faith has the same effect as intentional breach.

2. EFFECTS OF INTENTIONAL BREACH OF CONTRACT

Intentional breach of contract has four important effects. Firstly, it has close connection to do with subject of fundamental breach, that is, it amounts to a decisive factor in assessing whether the non-performance constitutes fundamental breach or not. Secondly, it extends the non-performing party's liability to unforeseeable losses as well. Thirdly, intentional breach entitles the aggrieved party to terminate the contract. In fact in some international instruments the only possibility to terminate the contract is where the non-performance amounts to fundamental. Finally, the intentional breach of the contract entitles the aggrieved party to demand punitive damages which has been recognized in some legal systems.

2.1. Treatment of Intentional Breach as a Fundamental Breach

Breaching the contract intentionally is among other factors which may be used in determining whether the non-performance was fundamental or not. For instance, where the obligor expressly states that he will not perform its obligations one can speak of fundamental breach of the contract except where the obligor was entitled to avoid performing the contract.

In this connection a art.8:103(c) of PECL states a non-performance of an obligation is fundamental to the contract if the non-performance is intentional and gives the aggrieved party reason to believe that he cannot rely on the other party's future performance.[3]

In the same manner art7-3-1(2) (c) of UPICC set out if the non-performance is intentional or reckless it amounts to a fundamental breach.

Also DCFR art.3:502(2)(b) make it clear that the creditor may threat the non-performance as fundamental if it was intentional or reckless and gives the creditor reason to believe that the debtor's future performance cannot be relied on, even if non-

[1]Bryan Hoynak, *Filling in the Blank: Defining Breaches of Contract Excepted from Discharge as Willful and Malicious Injuries to Property Under 11 U.S.C. § 523(a)(6)*,67 WASH. & LEE L. REV. 693. 713(2010).

[2]Richard Craswell, When is a Willful Breach Willful? The Link between Definitions and Damages, 1509(Michigan Law Review 2009).

[3]LiueChengwei, *Remedies for Non-performance - Perspectives from CISG, UNIDROIT Principles and PECL* 118 (1st.ed.2003).

performance of obligation does not substantially deprive the creditor of what he could have expected to receive.[4]

It deserve to note that unlike UPICC which has regarded intentional or reckless non-performance and aggrieved party's reasonable belief in obligor's future inability in performing of the contract as a separate grounds for fundamental breach, the PECL and DCFR in art 8:103(c) and 3:502(2)(b) respectively do not consider these as a separate grounds for regarding the breach as fundamental and these factors with together constitute a fundamental non-performance. It may conduct as a fundamental if there is an indication of intentionality that gives the aggrieved party a reason to believe that he cannot rely on the other party's future performance.[5]

Unlike to DCFR art.3:502(2)(b) and to UPICC art.7-3-1(2)(c) are respect to a situation that non-performance is intentional or reckless, PECL art.8:103(c) has limited to intentional non-performance.[6] Nevertheless, some authors have put forward that according to PECL art.1:303(3), intentionality in this concept includes recklessness and relevant illustrations show this term intended to apply to a wide array of situations ranging from the obligor's mere knowledge of the respective non-performance to fraudulent conduct.[7]

As we mentioned above, one effect of intentional breach of the contract is that it turns the non-performance into fundamental one. As a result, in examining the subject of intentional breach of the contract in the context of CISG it seems appropriate to resort to art 25 of the CISG which has to do with the concept of fundamental breach. Unlike other international instruments which have made use of different factors for determining the fundamentality of the breach, context of art 25 of CISG is very concise. According to this article, breach of the contract is fundamental if it results in such detriment to the other party as substantially to deprive him of what he is entitled to expect under the contract. As it can be seen from the context of the article there is no trace of intentional or reckless breach in the context of the CISG. In fact, the CISG has no provision on intentional or reckless breach.[8] As a result, to focus on the issue that whether breach committed intentionally or recklessly is incompatible with the remedial system of the CISG that under it fault is not a condition of contractual liability and in the availability of either remedy is not important.

Therefore recourse to the approach in determining fundamental breach is not permissible.[9] Nonetheless, some authors points out that any intention of breach in breaching of the contract is also relevant under CISG art.49 (1) (a) and 25. The reason for this is not non-conformity itself, but the reason for this is the loss of trust in the other party with non-conforming delivery together.[10]

2.2. Extension of Liability to Unforeseeable Damages

It is widely accepted that the non-performing party is only liable for losses which he foresaw or ought to have foreseen at the time of the conclusion of the contract. This principle has a long history and dates back to Roman law. Much later it was

[4]Paul Varul, *Performance and Remedies for Non-performance: Comparative Analysis of the PECL and DCFR*, XIV Juridica International, 110 (2008).
[5]Lars Meyer, *Non-performance and Remedies under International Contract Law Principles and Indian Contract Law: A Comparative Survey of the UNIDROIT Principles of International Commercial Contracts, the Principles of European Contract Law, and Indian Statutory Contract Law* 166-67 (1st. ed. 2010).
[6]Ingeborg Schwenzer, Pascal Hachem and Christopher Kee, *Global Sales and Contract Law* 739 (1st. ed. 2012).
[7]Meyer, *supra* note 5, at 146.
[8]3 Christian von Bar, Eric Clive and Others, *Principles, Definitions and Model Rules of European Private Law, Draft Common Frame of Reference (DCFR)*, Art.3:502, Note 12 (1st. ed. 2009).
[9]Chengwei, *supra* note 3, at 118.
[10]Benjamin K. Leisinger, *Fundamental Breach Considering Non-Conformity of the Goods* 98 (1st. ed. 2007).

established in the code napoleon, consequently adopted by a number of legal systems. The rule has also been adopted by common law. The rule was established in a famous case *Hadley v. Baxendale*and further restated in *Victoria Laundry v. Newman Industries.*[11]

Foreseeability test is based on the foresight of non-performing party, or the foresight of the reasonable person in the position of non-performing party at the time of conclusion of contract. And the knowledge of the aggrieved party is not relevant. The concept of the phrase "could reasonably have foreseen" is what a normally prudent person could reasonably have foreseen as the consequences of non-performance in the ordinary course of things and in the particular circumstances of the contract, such as information provided by parties or their previous dealings. Therefore in a case that harm flows from the ordinary of things, it flows naturally from the non-performance, it is foreseeable.[12] It should, however, be noted that applicability of this rule may be annihilated where the non-performing party has breached the contract intentionally.

As a matter of fact, the extension of liability to unforeseeable losses runs contrary to the general principle which according to it the party in breach is liable only for loss which it foresaw or could reasonably have foreseen at the time of conclusion of the contract.

This general principle has also been reflected in many international instruments. Article 9:503 PECL states: "The non-performing party is liable only for loss which it foresaw or could reasonably have foreseen at the time of conclusion of the contract as a likely result of its non-performance, unless the non-performance was intentional or grossly negligent." The last part of the article lay down a special rule on intentional failure in performance or gross negligence. In the case losses that non-performing party is liable for, has not limited to foreseeability rule and the full damage has to be compensated even if it is not foreseeable.[13] In the similar way art.3:703 of DCFR set forth: "The debtor in an obligation which arises from a contract or other juridical act is liable only for loss which the debtor foresaw or could reasonably be expected to have foreseen at the time when the obligation was incurred as a likely result of the non-performance, unless the non-performance was intentional, reckless or grossly negligent."

Although in general the obligor is liable only for loss that the obligor foresaw or could reasonably be expected to have foreseen at the time of the contract, the last part of the article reflects a special rule in cases of intentional or reckless failure to performance or gross negligence. In this case the losses for that the obligor is liable are not limited by the foreseeability rule and the full damage has to be compensated, even if unforeseeable.[14]

In these cases it seems more reasonable to place the risk of a non-foreseeable loss on the obligor rather than on the innocent obligee. A person is reckless if the person knows of an obvious and serious risk of proceeding in a certain way but nonetheless voluntarily proceeds to act without caring whether or not the risk materializes; there is gross negligence if a person is guilty of a profound failure to take such care as is self-evidently required in the circumstances.[15]

Unlike UPICC and DCFR which make distinguish in recoverable damages where the breach is intentional and in cases where it is unintentional, as far as it is concerned to recoverability of damages the CISG and the UPICC make no distinction between these two types of breaches.

Under CISG art.74 liability for compensation to damages is limited to losses that the party could or should foresaw at the time of conclusion of the

[11]Chengwei, *supra* note 3, at 183.
[12]Stefan Vogenauer& Jan Kieinheisterkamp, *Commentary on TheUnidroit Principles of International Commercial Contracts (PICC) 886-87* (1st. ed. 2009).
[13]Ole Lando& Hugh Beals, *Principles of European Contract Law* 442 (1st. ed. 2000).
[14]Von Bar, Clive and Others, *supra* note 8, at Art. 3:703, Comment C.
[15]*Id. At comment A.*

contract in the light of circumstance that he then knew or ought knew.[16]

It seems that the role of intentional breach of the contract in the context of UPICC is that it functions as a factor for determining of the nature of the breach. That is to say, where it is established that the non-performing party has breached the contract intentionally and then the fundamental breach of the contract has occurred, the aggrieved party can terminate the contract. In other words, its function in the context of UPICC is that it paws the way for terminating the contract.

But as far as the role of intentional breach in the context of the CISG is concerned it should be noted that art 74 of the CISG is clear point in this regard. According to art 74 of the CISG Damages for breach of contract by one party consist of a sum equal to the loss, including loss of profit, suffered by the other party as a consequence of the breach. Such damages may not exceed the loss which the party in breach foresaw or ought to have foreseen at the time of the conclusion of the contract, in the light of the facts and matters of which he then knew or ought to have known, as a possible consequence of the breach of contract.

As it is self-explanatory from this article there is no limitation on recoverable damages in the case of intentional breach as the PECL and DCFR. This restriction also cannot be discovered by looking at to four corners of the CISG since the remedial system of the CISG is based on no fault rule. As a result it does not matter whether the breach of the contract is intentionally or not.

But it should be note that the role of ill will is not ineffective in the CISG Entirely since in some cases it diminishes the aggrieved party's responsibilities in resorting to its remedies. For example, in cases where the aggrieved party fix an additional period of time of reasonable length for performance by the seller of his obligations he cannot resort to inconsistent remedies with such a fixing of additional time. However, according to art 49(2)(b)(ii), if the seller has declared that he will not perform his obligations within such an additional period, the buyer can avoid the contract despite fixing an additional period for performance.

2.3.Termination of Contract Due to Intentional Breach

As we mentioned above the intentional breach of contract may play a role in assessing whether the non-performance amounts to fundamental or not. In this regard, art.9:301 of the PECL have set forth that a party may terminate the contract if the other party's non-performance amounts to fundamental breach of contract and under art.8:103(c) intentional non-performance treats as a fundamental breach. As a result, even if the intentional non-performance is insignificant, the breach of contract is fundamental and the aggrieved party can terminate the contract under art.9:301. However the good faith principle enshrined in art.1:201 may come into operation if the non-performance is so insignificant that it is unreasonable for aggrieved party to terminate the contract, he should not be entitled to do so.[17]

In addition, under art.3:502(1) of the DCFR a creditor may terminate the contract if debtor's non-performance of contractual obligations is fundamental and under art.3:502(2)(b) intentional non-performance is one of the factors which plays a crucial part in establishing fundamental breach.

Also, under UPICC art.7-3-1(1) a party can terminate the contract where the failure of other party to perform an obligation under the contract amounts to a fundamental non-performance and under art.7-3-1(2)(c) if the non-performance is intentional or

[16]André Janssen & Olaf Meyer, *CISG Methodology* 168 (1st. ed. 2009).

[17]Christian von Bar, MauritsBarendrecht and others, *The Private Law Systems in the EU: Discrimination on Grounds of Nationality and the Need for a European Civil Code* 10 (6th.ed. 2000).

reckless, the breach of contract is fundamental, aggrieved party can terminate the contract.

Official comment of UPICC states that it may be contrary to the good faith principles (art.1-7 UPICC) to terminate the contract if the non-performance, although intentional, is insignificant. However, it is submitted that there is no need to recourse to good faith principle to achieve this result. As factors listed in art.7-3-1(2) are not conclusive definitions or definite cases of a fundamental non-performance, but they are only provide material for the weighing of factors in each case, the same result can be reached by giving the intention factor less weigh than the other factors. Another argument for a restrictive interpretation of the intention factor is that the UPICC do not emphasize on the fault element.

CISG has no provision on intentional breach of contract and intentional breach does not treat as a fundamental breach.[18]

2.4. Possibility of Claim for Punitive Damages

As far as the concept of punitive damages is concerned Black's Law Dictionary states punitive damages are those which awarded in addition to actual damages when the defendant acted with recklessness, malice or deceit; specif., damages assessed by way of penalizing the wrongdoer or making an example to others."[19]

The possibility of demanding punitive damages has a deep root in the history of law. The concept of punitive damages had been recognized in codes of some ancient civilizations like The Babylonian Hammurabi Code in 2000 B.C the Hindu Code of Manu in 200 B.C. and the Bible.

This was also the case for ancient romans that enacted laws in 450 B.C. that mandated the imposition of multiple damages as a means of punishing egregious misconduct.[20]

Recently, art 1371 of reforming the French Law of Obligations also has recognized this concept. According to this article A person, who commits a manifestly deliberate fault, and notably a fault with a view to gain, can be condemned in addition to compensatory damages to pay punitive damages, part of which the court may in its discretion allocate to the Public Treasury. A court's decision to order payment of damages of this kind must be supported with specific reasons and their amount distinguished from any other damages awarded to the victim. Punitive damages may not be the object of insurance.[21]

This concept is regarded as an appropriate means of punishing and deterring aggressive acts. Awarding such damages had become a well-established part of the American legal system. In 1851, the U.S. Supreme Court wrote that "in actions of trespass and all actions on the case for torts, a jury may inflict what are called exemplary, punitive, or vindictive damages upon a defendant, having in view the enormity of his offence rather than the measure of compensation."[22]

Another definition of punitive damages is relevant in oxford dictionary of law that defines punitive damages as a " Damages given to punish the defendant rather than (or as well as) to compensate the claimant for harm done."[23]

The PECL and the UPICC took more liberal approach by emphasizing the compensatory function

[18]Vogenauer&Kieinheisterkamp, *supra* note 12, at *828*.
[19]Bryan A. Garner, *Black's Law Dictionary* 448 (9th.ed. 2009).
[20]Emily Gottlieb, *What You Need to Know About… Punitive Damages*, Center for Justice &Democracy, 4 (2011).
[21]John Cartwright & Stefan Vogenauer& Simon Whittaker (eds) ,*Reforming the French Law of Obligations, GB*, Hart pub, 857(2009).
[22]Gottlieb, *supra* note 20, at 4.
[23]Elizabeth A. Martin, *Oxford dictionary of law*191 (5th.ed. 2003).

of damages and does not provide for the payment of punitive damages.[24]

Similarly the DCFR does not provide for punitive damages in general and official comment of VI.–6:101 in this respect states that "the punishment of wrongdoers is a question for criminal law, not private law. Under these model rules, punitive damages are not available. They are not consistent with the principle of restitution in kind or with that of full restitution."

As far as the possibility of demanding punitive damages in the CISG is concerned advisory council consider it impossible in the context of the CISG.[25]Professor graves also view awarding of "punitive damages in excess of a party's actual loss is contrary to the basic principle of Article 74" which has confined recoverable damages to actual losses.[26] Nevertheless, some authors point out although such awards are not currently available under the CISG, but one can presuppose a role for punitive damages in certain exceptional cases. Schwenzer and Hachem suggest that punitive damages should be awarded in cases where the breach of contract was intentional and in bad faith in order to provide full compensation for the aggrieved party.[27]

2.5.The Non-breaching Party's Compensation Is Not Limited to Liquidated Damages

Where the contract has a clause which has determined the amount of damages in advance (in our assumption liquidated damages) one of the effects of intentional breach of contract is that the aggrieved party's compensation is not limited to pre-determined amount and the aggrieved party can recover the amount which exceed the liquidated damages. It should, of course, be noted that the court's award cannot exceed the actual damages. In this connection art 225 of EgyptianCivil Code has set out that where the obligor breaches the contract in bad faith which in fact is a kind of intentional breach of the contract the judge is able to increase the amount of liquidated damages up to actual damages. The same is true under art 267 of Lebanon Code of Obligations and Contracts.[28]

Furthermore, in Hexioncase[29]the court held that an intentional breach means they could be exposed to damages far beyond any liquidated damages in the contract.

CONCLUSION

In this article it has been showed that the intentional breach of the contract has been recognized in some legal systems as well as some international instruments. It has also established that in the event of intentional breach of the contract the aggrieved party will have wide range of remedies.He/she can recover damages regardless of the fact the sustained losses were unforeseeable for the obligor at the time of conclusion of the contract.Furthermore the aggrieved party is able to terminate the contract regardless of the fact that the breach is fundamental or not. In some legal systems, the aggrieved party may also demand punitive damages as well. Also in some regulations and decisions, the non-breaching party may claim for full-compensation despite of determining the amounts of damages under liquidated damage agreement in advance.

[24]ThomaszGanyst,*The influence of the United Nations Convention on Contracts for the International Sale of Goods on the Chinese Contract Law: damages for breach of contract*, 18.
25CISG Advisory Council Opinion No. 6, available at:http://www.cisg.law.pace.edu/cisg/CISG-AC-op6.html
26.Bruno Zeller, *When is a Fixed Sum not a Fixed Sum but a Penalty Clause?*, Journal of law and commerce, 184 (2012).
27D Saidov& R Cunnigton, *Current Themes in the Law ofContract Damages: Introductory Remarks, Contract Damages Domestic and International Perspectives*, Hart, 15 (2008).
281AbdolRazzag Ahmad Al-Sanhouri, *Alvasit*, Beirut, 877,(1974).
29Hexion Specialty Chem. Corp., et al. v. Huntsman Corp

REFERENCES

[1] Al-Sanhouri, AbdolRazzag Ahmad, *Alvasit*, Vol.1, Beirut, 1974.

[2] Cartwright, John&Vogenauer, Stefan& Whittaker, Simon (eds) ,*Reforming the French Law of Obligations, GB*, Hart pub, 2009.

[3] Chengwei, Liue, *Remedies for Non-performance - Perspectives from CISG, UNIDROIT Principles and PECL*, 2003.

[4] Craswell, Richard, *When is a Willful Breach Willful? The Link between Definitions and Damages*, Michigan Law Review, 2009.

[5] Ganyst, Thomasz, *The influence of the United Nations Convention on Contracts for the International Sale of Goods on the Chinese Contract Law: damages for breach of contract.*

[6] Garner, Bryan A., *Black's Law Dictionary*, 9th.ed, West, 2009.

[7] Gotanda, John Y., *Calculation of Damages under CISG Article 74*, CISG-AC Opinion, NO. 6, 2006.

[8] Gottlieb, Emily, *What You Need to Know about… Punitive Damages*, Center for Justice & Democracy, 2011.

[9] Hoynak, Bryan, *Filling in the Blank: Defining Breaches of Contract Excepted from Discharge as Willful and Malicious Injuries to Property Under 11 U.S.C. § 523(a)(6)*, 67 WASH. & LEE L. REV. 693, 2010.

[10] Janssen, André & Meyer, Olaf, *CISG Methodology*, 1st.ed, European Law Publishers, 2009.

[11] Lando, Ole &Beals, Hugh, *Principles of European Contract Law*, Hauge, Kluwer pub., 2000.

[12] Leisinger, Benjamin K., *Fundamental Breach Considering Non-Conformity of the Goods*, 1st.ed, European Law Publishers, 2007.

[13] Martin, Elizabeth A., *Oxford dictionary of law*, 5th.ed, Oxford University Press, 2003.

[14] Meyer Lars, *Non-performance and Remedies under International Contract Law Principles and Indian Contract Law: A Comparative Survey of the UNIDROIT Principles of International Commercial Contracts, the Principles of European Contract Law, and Indian Statutory Contract Law*, 1st.ed, Peter Labg, 2010.

[15] Saidov D &Cunnigton R, *Current Themes in the Law ofContract Damages: Introductory Remarks, Contract Damages Domestic and International Perspectives*, Hart, 2008.

[16] Schwenzer, Ingeborg&Hachem, Pascal and Kee, Christopher, *Global Sales and Contract Law*, 1st.ed, New York, Oxford University Press, 2012.

[17]*Unidroit Principles of International Commercial Contracts 2010*, Rome, International Institute for the Unification of Private Law (UNIDROIT).

[18] Varul, Paul, *Performance and Remedies for Non-performance: Comparative Analysis of the PECL and DCFR*, Juridica International, XIV, 2008.

[19] Vogenauer, Stefan &Kieinheisterkamp, Jan (eds), *Commentary on The Unidroit Principles of International Commercial Contracts (PICC)*, 1ed, New York, Oxford University Press, 2009.

[20] Von Bar, Christian &Barendrecht, Maurits and others, *The Private Law Systems in the EU: Discrimination on Grounds of Nationality and the Need for a European Civil Code*, 6th.ed, European Parliament, 2000.

[21] Von Bar, Christian & Clive, Eric and Others, *Principles, Definitions and Model Rules of European Private Law, Draft Common Frame of Reference (DCFR)*, Study Group on a European Civil Code and the Research Group on EC Private Law (Acquis Group), Sellier, Volume 3, 2009.

[22] Zeller, Bruno, *When is a Fixed Sum not a Fixed Sum but a Penalty Clause?*, Journal of law and commerece, 2012.