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RECOVERY OF DAMAGE CAUSED BY LATE PERFORMANCE OF OBLIGATIONS RESULTING FROM INTERNATIONAL COMMERCIAL CONTRACTS

Abstract. This article analyses the different approaches in comparative law, arbitral practice and in doctrine regarding the institution of interest on late performance (default interest) allocated to compensate for the damage arising from the late performance of contractual obligations, known by most legal systems and instruments of uniform law. Despite the trend of harmonization of regulations in this area, national legislations enshrine different solutions regarding some aspects of this institution. Consequently, the national and international tribunals give various decisions, depending on the legal regulations and the international commercial customs that they consider applicable in the case, the jurisprudence in this field being different.

Keywords: damage, compensation, default interest, contractual obligation, late performance, interest for delay, liquidated damages, penalty.

Concept of interest on late payment

The obligation to pay compensation due for the delay in the execution of a contractual obligation related to a sum of money, interest on late payment (called also default interest), exists in most legislations of continental Europe and in the instruments of uniform contract law. Interest on late payment is monetary compensation that represent the equivalent of the damage caused to the creditor by delaying the performance of the pecuniary obligation contractually assumed by the debtor and is expressed in a lump sum, corresponding to interest on the amount of debt accumulated between maturity and actual payment.

In continental European countries, a fairly uniform concept has been formed regarding the interest on late payment. In the French Civil Code, Art.1231-6 (ex...
1153-1) provides that ”damages due on the ground of delay in satisfaction of a monetary obligation consist of interest at the rate set by legislation, starting from the time of notice to perform. These damages are due without the creditor having to establish any loss”.

Under the German Civil Code (hereinafter – BGB), ”if the obligor, following a warning notice from the obligee that is made after performance is due, fails to perform, he is in default as a result of the warning notice” (sec.286). ”A person who is liable in damages must restore the position that would exist if the circumstance obliging him to pay damages had not occurred” (sec.249). ”The damage to be compensated for, also comprises the lost profits. Those profits are considered lost that in the normal course of events or in the special circumstances, particularly due to the measures and precautions taken, could probably be expected” (sec.252).

In the Vienna Convention of 11 April 1980 on Contracts for the International Sale of Goods [1] (hereinafter - CISG), according to Article 78, if a party fails to pay the price or any other sum that is in arrears, the other party is entitled to interest on it, without prejudice to any claim for damages recoverable under Article 74, which provides that 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. Under the CISG, default interest allocation shall not be subject to a prior warning notice; the moment from which the interest starts to flow, in case of non-payment of the price, is the date of payment indicated in the contract.

Article 7.4.9 of the "Principles of International Commercial Contracts" developed by UNIDROIT (hereinafter - UNIDROIT Principles) [2] and Article III-3: 708 of the "Draft Common Frame of Reference of European Private Law" [3], developed in European academic institutions, published in 2008 (hereinafter - DCFR) provide that, if payment of a sum of money is delayed, whether or not the non-performance is excused, the creditor is entitled to interest on that sum from the time when payment is due to the time of payment. The interest is due regardless of whether or not the debtor benefits from an exemption in accordance with Art.7.1.7 of the UNIDROIT Principles or with Art.III.-3: 104 of DCFR. The creditor is entitled to this interest regardless of whether or not he has taken measures to mitigate the loss.
In harmony with the laws of other European states and with the instruments of uniform law, the Civil Code of the Republic of Moldova provides that, *if an amount of money is not paid at maturity, the creditor is entitled to interest on arrears for that amount from the date immediately following the due date until the date on which the payment was made* (art. 942 para. (1)).

In the practice of international trade, arbitral tribunals consistently award interest for late payment of sums of money due [4]. In international arbitrations, the allocation of default interest as an integral part of damages is generally a long-standing practice [5]. Thus, for example, in the award of an arbitral tribunal under the International Chamber of Commerce (hereinafter - the ICC award) no. 15913 of 2015, it was ruled: 

"80. (...) both by the convergence of legal systems as a whole, and by the Unidroit Principles applicable to international commercial contracts - in particular in the provisions of its article 7.4.9 (1) - which can serve as a ratio scripta, than by practice and international arbitration awards”, a general principle of law and international trade practice has been established, according to which “it is accepted in international law that the parties who are successful on the merits have the right to receive interest on the principal granted” [6] (see also: ICC Award No. 7331/ 1995[7]; ICC Award No. 9333/1998[8].

**Rate of interest**

Many national legal systems contain legal provisions regarding the interest rate. In France, for example, the interest is charged according to the statutory rate, which is set, according to Art. L.313-2 of the Monetary and Financial Code, by order of the Minister of Economy and, when the creditor is not a natural person who does not act for professional needs, is calculated every six months, based on the basic rate (*taux directeur* - fr.) of the European Central Bank for the main refinancing operations and the rates applied by credit institutions and financial companies.

In Germany, the legal interest rate consists of the following elements: a) the basic rate of interest is (3.62%), announced by the Deutsche Bundesbank; it changes on 1 January and 1 July each year by the percentage points by which the reference rate has risen or fallen since the last change in the basic rate of interest. The reference rate is the rate of interest for the most recent main refinancing operation of the
European Central Bank before the first calendar day of the relevant six-month period (sec.247 BGB); b) five percentage points above the basic rate of interest, in the case of legal transactions to which a consumer is not a party; and c) eight percentage points above the basic rate of interest, in the case of legal transactions to which a consumer is not a party (sec.288 BGB)

A European directive comes to harmonize regulations on the amount of statutory interest for late payment in the EU. Article 2 of Directive 2011/7 / EU of the European Parliament and of the Council of 16 February 2011 provides that the rate of the ‘statutory interest for late payment’ is equal to the sum of the reference rate and at least eight percentage points. Also, it is stated that reference rate means either of the following: (a) for a Member State whose currency is the euro, any of the following: (i) the interest rate applied by the European Central Bank on its most recent main refinancing operations; or (ii) the marginal interest rate resulting from the variable-rate tender procedures for the most recent main refinancing operations of the European Central Bank; and (b) for a Member State whose currency is not the euro, the equivalent rate set by the national central bank [9].

According to the modernized Civil Code of the Republic of Moldova, the default interest rate is equal to the rate provided by the provisions of Art.874 plus five (5) percentage points per year, if the debtor is a consumer, or nine (9) percentage points per year, in the other cases (art. 942 par. (2)). According to art.874, if the obligation bears interest, an interest equal to the basic rate of the National Bank of Moldova as follows is paid: a) for the first semester of the year, is the rate in force on January 1 of that year; b) for the second semester of the year, is the rate in force on July 1 of that year. At the same time, special legal provisions may provide for another rate. The new regulations differentiate between default interest rates depending on whether or not the delay is justified. According to Art.942 paragraph (5), if the amount of money is not paid at maturity with justification, the interest rate is the one provided in art.874. It may happen that the pecuniary obligation bears interest before maturity, such as, for example, obligations under loan, bank credit or bank deposit contracts. In such situations, in order to determine the default interest rate, the creditor may replace the rate provided by the provisions of Art. 874 with
the interest rate provided by the contract. For example, if the interest on a bank loan contract is 12% per annum, the creditor, in the event of a delay in repaying the loan amount, may charge a default interest of 17% per annum, if the debtor is a consumer, or 21%.% - in other cases.

Instruments of uniform law contain different solutions regarding the rate of the default interest. Contrary to all other conventions and statutes, CISG does not fix a rate of interest because it proved impossible to agree upon a standard: the discount rate was thought to be inappropriate for measuring credit costs; nor could agreement be reached on whether the credit costs in the seller's or the buyer's country were to be selected [3, p.964]. In the absence of such regulations in CISG, the issue is to be settled at the discretion of judges and arbitrators, who apply the general principles on which CISG is based or, in the absence of such principles, in conformity with the law applicable by virtue of the rules of private international law (Art. 7 para. 2) [10].

In the UNIDROIT Principles (Art.7.4.9 para.2) and in DCFR (Art.III.-3: 708), in case of delay, the interest rate is at the average commercial bank short-term lending rate to prime borrowers prevailing for the currency of payment at the place where payment is due. In the opinion of the authors of DCFR the lending rate for the currency of payment (III.–2:109 (Currency of payment)) at the due place of payment (III.–2:101 (Place of performance)) has been selected because this is the best yardstick for assessing the creditor’s loss. Unless otherwise agreed, interest is to be paid in the same currency and at the same place as the principal sum [3, p.963].

We will mention that the solutions proposed by the UNIDROIT Principles and other standardized restatements of commercial customs have often been used as references by arbitral tribunals in the settlement of disputes, including when the lex causae was the CISG. Thus, in the ICC Award no. 8128 of 1995 [11] it was stated that, due to the fact that the rate of interest is not envisaged in article 78 of the Convention, it is possible, within the framework of article 78 of the Convention, to apply an international interest rate such as LIBOR which applies to interbank transactions on the London market, according to Article 7.4.9 (2) of UNIDROIT Principles, which provides that the interest rate corresponds to the average interest rate charged for short-term loans by first class banks. The arbitrator considered it
justified to apply to the dispute the identical rules contained in the UNIDROIT Principles and the Principles of European Contract Law as general principles within the meaning of Article 7 (2) of the Convention.

It has been held in jurisprudence that, in the absence of contractual provisions relating to default interest, it is for the arbitrators to determine in a discretionary manner the susceptible rate, being limited only by international public policy, taking into account all relevant circumstances of the case [12]. It was also stated that this determination is not governed by strict and precise rules. The general tendency that emerges from the doctrine and from the international arbitration practice is to leave to the arbitrator a great freedom in fixing this rate.

**Interest on late payment vs. stipulated damages**

Normally, the statutory interest on late payment rate is not mandatory and the parties to the contract may provide for agreed interest rates (insofar as they do not contradict the limits established by law for some categories of transactions). In such cases it is the conventional interest. These interests are stipulated in the contractual clauses (*clause pénale* – fr., *liquidated damages* – engl.), widely used in international commercial contracts. National laws vary considerably with respect to the validity of the type of clauses in question, ranging from their acceptance in the civil law countries, with or without the possibility of judicial review of particularly onerous clauses, to the outright rejection in common law systems of clauses intended specifically to operate as a deterrent against non-performance, i.e. penalty clauses [2, p.339]. In such situations, it is important to establish the correlation between the interest regulated by the provisions referred to above and the stipulated damages (agreed payments for late performance).

In comparative law, the solutions in this regard are different. In France, for example, Article 1231-5 C. civ. provides: *where a contract stipulates that the person who fails to perform shall pay a certain sum of money by way of damages, the other party may be awarded neither a higher nor a lower sum. Nevertheless, a court may, even of its own initiative, moderate or increase the penalty so agreed if it is manifestly excessive or derisory.* Consequently, it can be accepted that, in the event that the amount of the penalties is derisory in relation to
the actual damage suffered by the creditor, the judge will allocate a default interest that will supplement the amount of conventional penalties.

In Germany, sec.288 para.3 BGB provides that the obligee may demand higher interest on a different legal basis. Consequently, in the presence of a stipulated damages clause, there is nothing to prevent the creditor from charging the conventional interest, when it is higher than the legal one.

In Republic of Moldova, the general rule is that the creditor can request, at his choice, either the statutory interest for delay or the penalty for delay according to the stipulated damages clause, called penal clause (Art. 942 para (4) of the Civil Code). This rule, inserted in the modernized Civil Code, seems to have put an end to the controversies that existed in practice and in the doctrine regarding the correlation between the delay interest and the penalties for delaying the performance stipulated in the penal clause. Although the doctrinaires stated that the interest on late payment should not be cumulated with the penalties provided for in the penal clause, as this constitutes an excessive penalty for the debtor, the courts most often applied such cumulation. Currently, by virtue of the regulations in force, the creditor may cumulate the interest on delay, calculated according to the legal provisions, with the penalty calculated according to the penal clause, only when the respective contractual clause (called punitive penal clause) expressly provides this (Art. 949 para (2) of the Civil Code).

**Damages in addition to interest**

Default interest is intended to fully compensate for the damage suffered due to late payment of a sum of money. However, the delay in payment may lead to a greater damage than that covered by the amount of default interest at the legal rate. Therefore, the legal systems of continental Europe and the instruments of uniform law grant the creditor the right to additional damages, insofar as the default interest at the statutory rate does not compensate for all the actual damage suffered.

In France, Art.1231-6 of the Civil Code (ex 1153-1) provides that where a debtor who is late in performing has by his bad faith caused his creditor a loss independent of this delay, the latter may obtain damages distinct from interest arising from the delay. Also, in Germany the BGB states that the assertion of further
damage is not excluded (sec.288 para 4). Article 942 para (4) of the Civil Code of the Republic of Moldova, in accordance with the regulations of other continental European states, provides that the creditor may claim compensation for the damage caused in the part not covered by the interest on late performance. The instruments of uniform law (Art.78 of the CISG, Art.7.4.9 paragraph 3 of the UNIDROIT Principles and Art.III.-3: 708 of the DCFR) as well expressly provide for the unconditional right of the creditor to additional damages at default interest.

In international commercial arbitration, allocating additional compensation, when default interest at the statutory rate does not cover the entire damage suffered by the creditor, is a common practice. For example, in one case, the arbitral tribunal ruled: "it follows from Article 78 CISG that the right to interest exists without prejudice to the right to damages according to Article 74 CISG, so that the reimbursement of interest whose rate would be higher than the legal rate. The plaintiff proved that he worked with bank loans for which she pays interest at the rate of 12% per annum. As a result, the arbitral tribunal applied for the late payment interest the rate of 12% per annum instead of the statutory rate of 5% per annum, as provided by Austrian law (Article 352 of the Commercial Code), applicable in the present case [13]."

Conclusions

Most legal systems and instruments for the standardization of contract law enshrine the institution of default interest, which is allocated to compensate for the damage resulting from the late performance of contractual obligations. However, despite the trend of approximation of regulations in this area, the laws of different countries contain uneven solutions to some aspects of this area. In particular, matters are regulated differently such as: the duration of the default interest, the delay as a condition for benefiting from the right to the interest in question, the amount of this interest, the correlation between the legal default interests and the penalties provided in stipulated damages clauses. Respectively, the arbitral tribunals give deferred solutions, depending on the legal regulations and the international commercial customs that they consider applicable in this case, the jurisprudence in this field being uneven. The general tendency that emerges from the practice of international arbitration is to leave
to the arbitrators a great freedom in solving these problems, being limited only by the international public order and by the general principles of law.

It has been held in international commercial arbitration that the allocation of default interest must take into account the fact that, due to the delay in the performance of the contractual obligation by the debtor, the creditor is deprived for a certain period of time of the amounts to which he was entitled to receive. The amount of interest in question is related to the rate at which the creditor will normally have to borrow money that he has not received from his debtor. The amount of interest must be reasonable and must be determined taking into account all relevant circumstances, in particular contractual provisions, including contractual clauses on the allocation of late payment interests; the nature of the facts which caused the damage; the interest rates prevailing in the relevant markets for the currency in question; the inflation of that currency and the time elapsed between the time of non-performance of the pecuniary obligation, the time of the award of the interest in question by the court or arbitral tribunal and the time of the actual payment of the amount due. At the same time, in accordance with the principle of full reparation for damage caused by non-performance of contractual obligations, the legal systems of continental Europe and uniform law instruments grant the creditor the right to additional damages when the default interest does not cover all the damage suffered by the creditor.

References: