



A Comparative Study of the Nature of Late Payment Damages In Iranian and English Law

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Abstract

In legal obligations involving monetary payments, delay in performance causes significant consequences. On one hand, the real value of money depreciates over time, and on the other, the obligee is deprived of the benefits that could have been earned from timely access to the funds. These two faces of loss due to inflation and deprivation of use are both referred to as “Late Payment Damages” in Iranian law. However, in a more technical and accurate sense, only the second type-loss due to the creditor’s deprivation from using money-is considered genuine late payment damages.

The backdrop to this legal evolution in Iran is instructive. The repeal of earlier provisions-such as Article 719 of the 1939 Civil Procedure Code-based on the assumption that late payment damages are usury, created significant legal and economic uncertainty. The absence of enforceable delay penalties led to widespread defaults, particularly among bank debtors, effectively stripping monetary obligations of real enforceability. The introduction of Article 522 in 1999, therefore, was a necessary corrective, aimed at restoring order to financial transactions by permitting compensation equivalent to the inflation rate.

Nevertheless, ambiguity persisted: Was the purpose of Article 522 merely to preserve the real value of the debt, or was it also meant to provide compensation for actual harm due to the loss of money’s utility? The answer significantly impacts the debtor-creditor relationship. The decision as a unified judicial procedure of the Supreme Court No.805 has provided partial clarity by allowing parties to set late payment damages above inflation rates through contractual clauses, assuming no violation of overriding legal norms.

This raises a critical question: To what extent can parties exercise freedom in stipulating late payment damages? Is this autonomy absolute, or are there principles and boundaries that limit it?

In response, it should be said that although Article 522 of the Civil Procedure Code (enacted in 1999) recognizes the possibility of compensating for losses caused by depreciation of money only up to the rate of inflation officially announced and the

decision as a unify judicial procedure No. 805 has created a turning point by affirming that parties may mutually agree to higher amounts of late payment damages, even beyond the inflation rate, but it is conditional to: Such agreements must not contravene mandatory legal rules. As a result, compensation for actual delay damages—whether objective damages in general, personal damages proven with debtor’s fault, or unforeseeable damages with established malicious intent—has become feasible through mutual contractual agreement.

In comparison, the English legal system has evolved considerably in handling monetary obligations. Historically, English law strictly adhered to the rule against awarding more than the principal debt; However, this has gradually changed. While the system now allows late payment damages in financial obligations, it imposes strict scrutiny on pre-agreed penalty clauses and maintains a pragmatic approach—allowing pre-agreed damages so long as they represent a genuine pre-estimate of loss and are not designed to punish the breaching party. So, if a predetermined sum for late payment damages in a contract is excessive and appears to penalize rather than compensate, it may be deemed an unenforceable penalty clause. As a result, English courts distinguish between liquidated damages—permissible pre-estimates of loss—and penalties, which are viewed as coercive or punitive.

Also, Iranian recent jurisprudence seems to align with this cautious liberalism. It means that while the recent verdict authorizes higher-than-inflation late payment damages by agreement, it expressly emphasizes that such agreements must not violate public order or mandatory provisions. Furthermore, by invoking the Islamic legal principle of non-harm, Iranian jurisprudence invalidates excessively high penalty clauses that resemble usury, thus aligning with the notion of moral and legal fairness in contractual relations. In effect, the autonomy of contracting parties to define delay damages is bounded: the agreed sum must qualify as “compensation for loss”, not “usury”.

The Supreme Court’s condition that agreed sums must not contradict public law or equate to usury, mirrors the English concern with penalty clauses. In both systems, the core inquiry centers around the function of the clause: Is it compensatory or punitive?

From a theoretical standpoint, late payment damages can be analyzed in two frameworks:

1. **As Contractual Liability:** This is the conventional view where late payment damages serve as a contractual tool to compensate for inflation. It is formulaic and aligns with general principles of fairness and predictability.
2. **As Tort Liability:** Here, late payment damages are understood in the broader sense of compensating actual harm from non-performance. This model is more responsive to creditors’ needs but requires proof of harm, fault, or intent.

This article concluded that the Iranian legal discourse now recognizes both aspects, albeit with varying legal preconditions. Contractual liability under Article 522 does not require fault, while tort-based claims may demand evidence of wrongdoing or loss. The recent Supreme Court verdict bridges this gap by endorsing contractual flexibility, thus



accommodating both frameworks under certain safeguards.

In conclusion, while both the Iranian and English legal systems now permit late payment damages in financial obligations, they impose limitations. The Iranian system, influenced by Islamic legal principles, allows compensation through agreement but prohibits usury. The English common law model is shaped by equity and contract law, disallowing punitive damages disguised as liquidated damages. Both legal orders aim to balance creditor protection with debtor fairness.

Keywords: Late Payment Damages, Monetary Obligation, Usury, Imposed Condition.



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