

## Contracts and Termination Right in Iran Law

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**Abstract:** Contract is among basic principles discussed in Labor and Commercial Laws. It is necessary to provide its definition, to survey its content and discuss one of the most controversial issues, namely contract termination. As a delicate matter in Labor and Commercial Laws, contract termination may lead to unfairness against one of the contracting parties; hence its terms are required to be investigated. It is worth mentioning that contract termination issue in Iran Law has knots which must be untied by jurists so that it may bring about more sense of security in labor and commerce environments of the society. So this paper, comparing laws of Iran and developing countries, aims at surveying solutions for legal problems pertaining to contract termination, underlining protection of contracting parties' interests.

[Saeed Eivazi. **Contracts and Termination Right in Iran Law**. *Academ Arena* 2018;10(9):74-79]. ISSN 1553-992X (print); ISSN 2158-771X (online). <http://www.sciencepub.net/academia>. 8. doi:[10.7537/marsaaj100918.08](https://doi.org/10.7537/marsaaj100918.08).

**Key words:** conclusion of contract, termination, specific performance, French Law, Common Law.

### Introduction

As commercial relationships and transactions are developed in modern societies, the matter of conflict in contracts has increasingly drawn jurists' attention, and it raises the question that how contracts and termination terms can be concluded to render the lowest damage to promisor and promisee. Contracts are consistently influenced by social, political and economic circumstances, and the contracting parties must undertake their obligations in turbulent times of social, political and economic changes with a sense of security.

This paper aims at defining contract and its types, and surveys contract termination following indentifying legal boundaries in a contract. The main question is that what is the position of law in the contract termination?

### Contract or Agreement Definition

A contract or agreement is deemed as a concurrence of two essential wills of constituting a legal obligation. In simple terms, whenever a concurrence or an agreement of two essential intentions is required for constitution of a legal effect such as sale, lease and so on, the contract will be realized. So such entities as possessory will, attorneyship, donation, and the other entities in which acceptance of the offer or is not an essential acceptance or a contractual acceptance, according to Prof. Langrudi, are excluded from contract definition and coverage.

Contracts are categorized into different groups in terms of various perspectives. For example contracts are divided into financial and non-financial contracts or possessory and promissory contracts in terms of subject.

Conclusion of all types of contracts requires at least two individuals (natural or legal). Whether the contracting parties are natural or legal persons, certain requirements must be fulfilled by them as well as by the representative of legal individual (usually managing director). Subject of the contract, effects of the contract, specific performance for each party (particularly for the obligations that are to the benefit of both parties), contract forecasting and dissolution are among the important items with regard to the contract conclusion.

Pursuant to article 183 of Iran Civil Code, "A contract does mean that two or more persons undertake an obligation towards other two or more persons who accept it." There has been some criticism on this definition including, it does not embrace possessory contracts as it constrains contracts to the parties' obligations. The criticism has been response by great jurists that although this article has been derived from French Law, Iran Civil Code legislators have changed it with respect to Islamic jurisprudence. Consequently, since in Islamic jurisprudence a promise is regarded as a contract, the article comprises all contracts. The other criticism raised is that it would be better if the word "individual" had been applied rather than "person" to comprise legal individuals as well.

### Types of Contract:

#### Irrevocable (Binding) Contract

Pursuant to article 185 of Iran Civil Code, "an irrevocable contract is one which cannot be broken by either party except under specified circumstances." The specified circumstances are the ones in which the option to terminate the contract has been foreseen in the regulations for either or both parties. However, when both parties intend to terminate the contract with

their consent, it is called cancellation; and from legal perspective two intentions that have created the contract, are capable of terminating that.

#### **Revocable Contract**

As per article 186 of Iran Civil Code, "a revocable contract can be cancelled by either party whenever he likes."

#### **Optional Contract**

Here the parties agree that the contract can be cancelled by either party, by both parties or by third party. Among contracts subjected in the above mentioned Law, interest-free loan transactions, installment sale, hire-purchase, contracts of partnership, bailment and reward are revocable.

#### **Unconditional Contract**

An unconditional contract is one which is not, in the intention of the makers, contingent upon any outside matter; otherwise it is a conditional contract. Deciding to conclude a contract and expressing it, is called forming of intension. For instance in a sale contract, upon parties agreement seller becomes the owner of his proposed price and buyer becomes the owner of the subject of the transaction, and transfer of ownership is the immediate effect of sale contract. In the other words, transfer of ownership is not subject to any condition.

#### **Suspended Contract**

As per article 189 of Iran Civil Code, a suspended contract is one which is, in the intention of the makers, contingent upon any outside matter. In such a contract, parties do not intend the contract to be immediately enforced, but rather it will be subject to satisfying a condition. For example, a condition that is laid down in a will by virtue of which the legatee will be the owner of the property when the legator dies.

#### **Mutual Interest Contract**

It is a contract by which either of the parties undertakes an obligation or a payment to the benefit of the other party in consideration of receiving a payment or an obligation promised.

#### **Gratuitous Contract**

It is a contract in which one party undertakes an obligation or a payment to the benefit of the other party without receiving anything in exchange, for example when some body donates his own property or possession to some body else for personal reasons.

#### **Possessory Contract**

It is a contract by virtue of which the ownership is transferred, for example in a sale contract, the ownership of the object of sale is transferred from the seller to the buyer and the ownership of price is transferred from the buyer to the seller.

#### **Promissory Contract**

It is a contract as a result of which a right, a debt or an obligation is created for one party against the other one, for example a transportation company

pledges to deliver the commodity to the owner in a certain destination, and in consideration, the owner undertakes the payment.

#### **Conditional Contract**

It is a contract into which one of the three types of conditions (condition about performance of an act, condition of description and condition of collateral events) are incorporated.

#### **Specified Contracts**

These are contracts whose titles and principles have in detail been stipulated in the Civil Code.

#### **Unspecified Contracts**

These are contracts which do not possess any particular title and principle, and is concluded as per article 10 of Civil Code and with regard to the parties intended requirements.

#### **The Governing Law**

In general, subject of the contract and terms and obligations specified by the contracting parties determine the governing law. Hence to write a contract, it is necessary to refer to other statutes besides Civil Law which is the main reference specifying conditions for contract validity and major descriptions. For instance an employment contract must be written with reference to Labor Law and Social Security Law or a transportation contract must be concluded pursuant to Commercial Law.

Components of a contract are as below:

1. Type of Contract
2. Contracting Parties
3. Subject of the Contract
4. Duration
5. Price of the Contract
6. Territory and Scope of Work
7. Contractual Obligations of the Parties
8. Termination
9. Price
10. Force Majeure

#### **Dissolution of the Contract, terms and forms:**

Dissolution means to terminate a contract and prevent it from continued existence and validity. Legal consequences pertaining to the dissolution are in different forms. Dissolution is a general concept; once the validity requirements of a contract are satisfied and then its legal effects are halted, the contract is deemed as a dissolved contract whether it is binding or revocable, possessory or promissory, mutual interest or gratuitous, and whether appertaining to natural or legal persons.

#### **Dissolution Forms:**

Dissolution of any contract may occur in different forms which are as following:

1. Termination
2. Revocation
3. Cancellation
4. Nullity

5. Lapse of Time
6. Waiver (of enjoyment of wife's company for the remaining period in a temporary marriage)
7. Death of either of the contracting parties (in revocable contracts such as attorneyship contract)
8. Frustration of purpose (impossibility of using the object of the contract when the contract is vitiated or when the object belongs to a third party)
9. Formal contracts
10. Contract vitiation

**Difference Between Nullity and Dissolution:**

Nullity is one of the forms of the contract dissolution. Some times a contract is divided into two separate contracts in terms of its subject. like *the option of sales unfulfilled in part* which arises once the transaction, in respect of a part of the thing sold, is void for any reason and in respect of the other part is valid; in that case the purchaser will have the right to cancel the transaction, or else to accept that part of the thing in respect of which the transaction was valid, while returning the consideration of that part in respect of which the transaction was void. Contract dissolution may be voluntary including the option to terminate in binding or irrevocable contracts such as death of either of the parties of a revocable contract (e.g., attorneyship contract).

**Termination Definition:**

The lexical meaning of termination is to violate, vitiate and break an agreement. It is also called voluntary dissolution which means in legal terms, rescinding a contract legally by either of contacting parties or by a third party.

The issue of contract termination appertains to binding contracts, as in revocable contracts either of the parties may terminate the contract whenever intend to do so. The question that is raised as regards the binding contracts is whether the claimant of contract termination enjoys the right of termination or he shall be bound over the contract.

With respect to the above-mentioned definition, one can say that termination is a unilateral intention to dissolve a contract and an obligation, which is a unilateral contract such as discharge of contract; i.e., one party may independently exert his right to terminate the contract without requiring the other party consent which is called the unilateral contract.

In fact, termination is the right to rescind a contract which has truly been concluded and is binding like contracts of sale, lease, barter, hire of persons, mortgage, loan and so forth. If the termination concept is applied in both revocable and binding contracts, cancellation and legal options including option of defect or option of loss and option of unfulfilled conditions and etc., are not applicable to revocable contracts. The right of termination may be incorporated into a binding contract by the parties'

intention and consent which is then called optional contract. A contract may be concluded by waiver of all options, as a consequence of which the termination right is created by virtue of law, and the requirement for terminating a binding contract is called legal option. The possessor of termination right is some one who may refer to judicial authorities and plead for termination of the binding contract or transaction; yet when the contract is void, any beneficiary may request the contract or transaction nullity from judicial authorities, as a void contract is in conflict with public order and public interests. To terminate any binding contract, the appropriate order shall be issued by a judicial authority (judge). The judicial authority, preceding any measure, shall attain termination terms in the contents of contract, maybe the owner of termination right including the option of delayed payment of the price or option of loss, perceives that he may terminate the contract relying upon the *option of delayed payment of the price* whereas the judicial authority may not attain it and may not vote for termination.

**Termination Grounds:**

Contract termination can be based on different grounds. It means that termination relies upon a right constituted by either contracting parties or legal order, and the related right belongs to one of the parties, both of them or a third party.

A- Parties consent: contracting parties may agree inside the contract or by a separate binding contract that one party, both of them or a third party may terminate the contract. For example a seller sells a car to a buyer subject to the condition that either the seller, or the purchaser, or both of them, or a third person, shall have the right of canceling the transaction within one month, which is called option of conditions as stipulated in articles 399 and 400 of Civil Code.

B- Direct legal order: in some cases in order to prevent unintended damages towards one of the parties, law directly grants the related party the right of termination. For instance, when some one signs a lease contract of a house and after a while finds out that it is not possible to reside there, he may cancel the lease by virtue of articles 478 and 479 of Civil Code.

**Termination Conditions:**

1. Intention: the terminator shall intend to rescind the contract.
2. Consent: the terminator shall consent to rescind the contract; otherwise if it is terminated under duress, it will have no legal effects.
3. Competence: the terminator shall possess legal competence in terms of wisdom and age.

**Termination Effects:**

Effects of termination are prospective by which the contract is rescinded as of the date of termination

and has no longer any effects, and these effects are not retrospective. Therefore the profit of the object of contract, essentially up to the termination date, shall belong to a party who has been the owner by virtue of the contract. However, as the profits and accretions which are an, can not be separated from the object of contract, the ownership of separable accretions and benefits, before termination, belongs to the person who has been the owner by virtue of the contract and after termination, belongs to the one who is the owner by means of termination.

Termination is among rights rather than orders; hence the parties may waiver it.

#### **Unenforceable Contract and its Termination Conditions:**

Providing a contract meets the indispensable requirements of contract validity, it will be regarded as a valid contract. Yet, if one or more indispensable requirements do not exist, the contract will be null and has no effect. Since the legislator tends to drive all contracts towards validity and prevent nullity as far as possible, he has specified unenforceable contract between valid and void contracts.

An unenforceable contract is pendent between valid and void contracts, thus it is neither valid nor void. In such a contract, all validity requirements of the contract have been fulfilled except to one that is relatively defective whose removal will make the contract valid.

Generally the unenforceable contracts require the confirmation of an individual by which the contract will become valid and otherwise it will be void. For example, the transaction of an individual under duress is unenforceable, provided that the forced individual confirms the contract, it will be valid and otherwise it will be void.

An unenforceable contract may not be terminated, as it is defective. Consequently it must be confirmed to become perfect and then termination may be requested, or such a contract may be rejected. The right of termination may be constituted either by the parties consent or by the legal order and court judgment. A termination right provided with the consent of the contracting parties, called the option of conditions, is constituted concurrently with the contract conclusion. However, there exist some legal options which are resulted precisely after the contract conclusion such as the option of delayed payment of the price and the option of unfulfilled conditions.

#### **The Conditions Render the Contract Null and Void:**

It is worth mentioning that a void condition, which underlies the contract nullity and termination, shall not be inserted in a contract; yet, stipulation of valid and legal conditions in contracts will pose no uncertainty. The other fact is that while specifying and

agreeing upon valid conditions, a certain period must be determined for them. The conditions make the contract null and void are as following:

1. Condition contrary to the requirement of contract: any conditions that are in conflict with the nature of contract, for example in a lease contract, when the tenant does not have the right of residence in and profiting from the rented premises. Or in a mortgage contract, if the mortgagee is not authorized to sell the mortgaged property when the mortgagor does not undertake the obligations. Strictly speaking, any condition in conflict with the major purpose of the contract like transfer of object and price in the sale contract which is the major purpose of such a contract.

2. Uncertain condition leading to uncertain considerations: any condition whose subject is uncertain, for example when it is stipulated in a sale contract that the buyer pays the price after returning from the trip to Mecca. Here as the returning date is uncertain so undoubtedly the date of paying the price will be uncertain as well, and this condition will make the contract null and void.

3. Once the condition stipulated in the contract is a condition of description and the related qualification does not exist, the option to terminate the contract is created for the beneficiary: whenever one of the contracting parties pledges the existence of a specific attribute in the object of the contract, then the object shall certainly be in accordance with the specified attribute. When an estate is sold based on a specific area, yet it becomes evident that it does not have the specified area, whether it is more or less, the option to terminate the contract is created. It is clear that if the real area is less than the specified one, the buyer has the option of termination and if it is more than the specified area, the seller owns the option. Even if the sale contract is concluded based on a specimen, the whole object delivered must be according to the provided specimen; otherwise, the purchaser may terminate the contract.

4. Condition that is void: inserting a void condition in a contract not only influence the contract validity it will also underlie nullity and termination of the contract. Void conditions are: a) impossible conditions, b) conditions without any benefit (proprietary worth) and c) illicit conditions.

#### **The Position of Termination Right in Iran and Other Countries Laws:**

It is popular in Iran law that once a promisor neglects to perform his obligations the other party may not primarily terminate the contract but he shall refer to the court and plead for specific performance, unless the obligation is not practicable even by another person paid by the promisor. This theory that has always dominated Iran Laws, and on some occasions brings about problems and unfairness,

neither has been derived from Islamic jurisprudence on the basis of which Iran Laws have been constituted, nor is consistent with developing countries laws and International Trade Law; even there exist no strong justification for this theory in the Civil Code.

It must be stated that recognizing the regency of the promisee termination right over the other ways of securing his rights, may cause him harm, distress and constriction. Yet it must be considered that recognizing an absolute right of termination for the promisee may occasionally breed injustice against the other party, particularly when the contract, though performed with delay, has not still lost its essential desirability or the undertaken obligations can be completed and its defects are removable, or even without removing the related defects, as they are minor, it may be compensated otherwise such as calculating the price margin; as a result, the promisor has briefly executed his obligations and the recognition of termination right for the promisee will cause him harm, distress and constriction. But Iranian jurists, with reference to some articles of the Civil Code and without differentiating the issues as per above, recognize regency of termination right to specific performance or implementing the contract by another person paid by the promisor.

In the legal systems of other countries, various stances have been adopted. For example, French Law stance as regards contracts represents that the contracts shall be accomplished as far as possible and the promisee may not easily terminate the contract. Yet it is not so closed ended and provided that the contract enforcement is not possible in terms of practical, moral or legal requirements, the contract may be terminated. Moral requirements refer to the contexts in which individuals freedom are supported and for example, if a promisor who fails to meet the obligation does not have bona fides, the other party may have the right to terminate the contract and in contrast, if the promisor failed to meet the obligation but has had bona fides, he might request the court permit for completing his obligations and preventing termination of the contract whose prerequisites he has provided. Consequently French courts, by virtue of articles 1184 and 1610 of French Civil Code, and through making balance between the rights of the contracting parties and preventing the promisor from abusing Irrevocability of the contract on the one hand and the promisee from misusing the termination right on the other hand, and in case the desirability of the contract still exists, endeavor to vote for performing the obligations, even by granting an additional respite to the bona fide promisor; however, if the two aforementioned conditions do not exist, they will not hesitate to recognize the promisee termination right.

In spite of the written law, common law adopts, seemingly in terms of its nature, an easier stance as regards the contract termination and prefers it to specific performance; thus in case of violating the obligation pertaining to the essential conditions of the contract, both parties have the right of termination and receiving compensation. In this legal system, contract terms are divided into conditions and warranties, as a result of which violating conditions renders the rights of termination and receiving compensation, but violating warranties renders merely the right of receiving compensation.

Instances of voting for specific performance in common law is limited and remains at the discretion of the court, and the court will not vote for the contract enforcement when the payment for damages is a sufficient remedy, or the court may have no control over the contract implementation, or the contract has personal aspects (for example, the client has fired the employer), or the promisor is minor, or a contract has been concluded for granting loan or when the purchased commodity is not unique.

As regards delay, there essentially exists an emphasis on the time significance in the business transactions, violating of which may bring about termination right for the promisee. However, if circumstances and conditions reveal that there is not such an emphasis, the court may reject contract termination.

Therefore, common law does not bind the promisor to enforce the contract but rather bind the promisee to reduce the damages and consequently drive him to conclude a new contract with another person for purchase or sale of the contract object; so if he delays and increases the loss, he can not bind the promisor to pay for all damages.

In fact, the law does not attribute the damages caused by the promisee delay in supplying his own needs from another source, to the promisor and merely regards the promisor as responsible for damages directly caused by his failure to meet the obligations.

### **Conclusions:**

The afore-mentioned discussions reveal clearly that contracts are among issues in which jurists may have innovations and each single step towards modifying the conditions of law interfere in contracts will lead to a profound effect on business conditions in the society.

Through a comparative study of contracts and their legal boundaries in different countries, we found out that the main differences lie in the contracts termination. It differs in developed countries with respect to their dominant policies. For instance, in the dynamic economy of the United States, given its

capitalism policies and economic giants development strategy, the issue of contract termination is treated more easily, and the swift and explicit profits of the capitalists are clearly preferred over the moral aspects and impact of bona fides in economic relations.

Iran Law, neither underscores the bona fide enforcement of the contract as far as possible like French Law, nor has facilitated this process by categorizing obligations and comprehensive probes as Common Law. By looking into the internal contracts of our country we will find out that enormous damages have been incurred by both promisor and promisee due to the legal shortcomings; in some cases there exist injustice against one of the parties and occasionally the absence of prompt and effective proceedings regarding these contracts as the subject of dispute, has underlain embezzlement and fraud.

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9/25/2018