

**Supreme Court Ruling 74/2018, Division for Civil Affairs, Section I  
of 14 February 2018**

On 14 February 2018, Ruling 74/2018 ruled on a claim against a penalty clause agreed in a rent contract involving the distinct use of a dwelling. The lease contract established a 10-year lease with a monthly rent of €45,075 plus the applicable VAT and regular lease reviews to come about in keeping with the Spanish National General Consumer Price Index (IPC). The lease contract contained a penalty clause that was later the subject of litigation between the parties. The aforementioned clause read: "If the Lessee rescinds the Contract in advance without due cause, the Lessee shall be obliged to pay the Lessor as a penalty a sum equal to 25% of the rents pending maturity prior to 1 June 2010 and 40% of those pending maturity as of that date to the termination of the contract; the foregoing without prejudice to the Lessor's right to claim unpaid due rent and compensation for any damages that may be caused by any such early rescission."

After several non-payments of rent, the Lessor filed for eviction. On 18 September 2012, the Magistrate's Court and Court of First Instance, Court No 3 of Cuenca, upheld the claim, declaring the contract to be rescinded, ordering the Lessee to be evicted from the premises and sentencing them to pay the Lessor €226,119.24 and any rents that should accrue until they abandoned the premises, which took place on the following 8 October 2012.

After the eviction, the Lessor immediately let the premises to a new Lessee. Nevertheless, on 15 October 2012, the Lessor once again filed a lawsuit against the first Lessee, claiming the amount corresponding to the penalty clause that had been agreed in the lease contract (€717,809.70).

The Lessee opposed the Lessor's claim, alleging that the lease contract had been improperly rescinded, that the purpose of the penalty clause was to help the Lessor avoid damages and that no damage could have been caused, as the premises were immediately leased after the Lessee was evicted.

The Court of First Instance ruled against the claim filed by the Lessor, considering that the compensation was limited to the time the premises remained empty and that, in this case, as it had not been left empty, the compensation was unwarranted.

After this judgment, the Lessor appealed before the Provincial Court. This action was challenged by the Lessee, who sought a ruling on the abusive character of the penalty clause on the grounds that it was disproportionate and difficult to fulfil owing to the Lessee's lack of assets. In its judgment, the Provincial Court confirmed the sentence of the Court of First Instance, but dismissed the challenge against the penalty clause made by the Lessee by finding that when a penalty clause is agreed, it cannot be abusive, given that its purpose is to ensure fulfilment of the obligation and settle damages, furthermore stating that it is the fulfilment of the penalty clause that becomes abusive when aspiring to collect despite the fact that the premises had not been empty.

In its reasoning, the Provincial Court stated:

1. The penalty clause is abusive given that the compensation was limited to the time the premises remained empty, otherwise there would be unjust enrichment.
2. The declaration of abusiveness render the clause null.
3. The function of the penalty clause, in accordance with Section 1152 of the Spanish Civil Code, is to replace the damage compensation and that, in this case, it was agreed to help the Lessor avoid damage and that, as the pending rent was paid, the Lessor did not suffer any damage.

After this pronouncement, the Lessor filed an appeal to the Supreme Court. The latter first assessed the issue in terms of current regulations and existing case law. In its first analysis, the Supreme Court stated:

- a) Apart from the general contract conditions between businesses and consumers, our legal system allows for penalty clauses as a restraining, sanctioning and punishing instrument and even allows for them not replace it, but to be added to damage compensation.
- b) The possibility of stipulating penalty clauses for punitive purposes is subject to the general limits of private independence established in Section 1255 of the Spanish Civil Code, as there is no specific control on abusiveness for contracts between businesses.
- c) The possibility of courts moderating the amount of a penalty clause is only practicable when the obligation has been partially fulfilled. In cases where there is a full breach of the penalty clause or this provides for circumstances of partial breach, this cannot be moderated by the courts.
- d) This Supreme Court is aware that a considerable section of scientific doctrine favours the modification of our set of laws and the introduction of the possibility of courts modifying punitive penalties, as well as patently disproportionate settlement clauses.
- e) There are several Supreme Court rulings in which it refrained from moderating the agreed compensation; however, its Ruling 300/2014 on 29 May warranted the moderation of a penalty clause on the grounds that i) the penalty clause had a damage compensation function, thus there was no room for imposing it automatically and fully when there was evidence that it was in excess of the damages that had really been caused; ii) if the lessee had received the totality of the penalty clause in addition to the rents from a new lessee, there would be a clear case of unjust enrichment; and iii) the pacta sunt servanda principle cannot be applied given the injustice and disproportionate character of the result.

After this contextual exposition, the Supreme Court found for the appeal and, thus, sentenced the Lessee to pay the penalty clause in full.

The Supreme Court grounded its ruling by arguing as follows: firstly, the penalty clause established by the parties to the contract was valid given that it was a contract entered into between two businesses and the Lessor was not in a situation that would allow it to exercise any abuse of power. Secondly, the Supreme Court reasoned that the fact that the sum claimed in the penalty clause was not equal to full payment of all the pending years' rent, but rather a percentage of the same, was in keeping with the deterrent purpose of the instrument and did not impede the early rescission of the contract. Furthermore, the Supreme Court pointed out that the quantity set in the penalty clause was not the equivalent of compensation for damages for loss of profit, but rather a penalty that did not exclude a claim being made for damages that were caused by the breach, thus its purpose was, therefore, not that of settling in advance any damages that might be caused by the breach and which were enforceable once the breach took place without prejudice to the accrediting of damages.

Accordingly, on foot of this Supreme Court Ruling, it can be concluded that the lessee is obliged to fully pay the lessor the agreed amount in the penalty clause, as it is not possible for courts or tribunals to moderate any such amount, even when no damage has been caused by the lessor as a result of the immediate lease of the premises.