**W**illful” can be a problematic word for the commercial litigator. According to Webster’s, it simply means “deliberate” (or obstinate, in the case of a disobedient child). In the legal world, it sometimes means something more—“malicious,” “wanton,” “egregious,” “wrongful,” “injurious,” or a whole host of similar synonyms that mean “with bad intent.” Despite this built-in ambiguity, the term “willful” has found its way into a host of significant commercial contracts, including sophisticated merger agreements and other major corporate contracts. In our practice, for example, we have seen numerous contracts that use the word “willful”—usually nestled in provisions that attempt to place limits on liability in the event of a breach of the contract.

In a typical provision using this word, one or both parties will attempt to insulate or cap damages available to the other side to only those damages resulting from a “willful” breach. When such a contract is breached and the dispute lands before a court, the question of what “willful” means can be an outcome-determining issue.

This question will essentially boil down to the two options above. The first is to use the broad, dictionary definition of “willful,” which means deliberate, as in by choice, intentional, not by accident. If the defendant breached the contract on purpose, the damage-limiting language will not save him from his conscious decision.

The other option regards “willful” as going beyond mere conscious choice, even beyond choice motivated by pure self-interest. This option regards “willful” as requiring the intent to injure the other party, or some other reckless disregard for the well-being of the other side. Courts have often equated “willful” in this context with conduct rising to the level of an independent tort.

This second option springs from a purist’s vision of contract law, which finds questions of intent to be inconsistent with traditional contractual analysis. Contract law, unlike tort law or criminal law, generally does not care about the reasons why a party may choose to transgress, i.e., breach a contract. In fact, the law traditionally protects the choice of a party to make a rational economic decision, so long as the party is willing to compensate the other side through contract damages. According to Holmes, “[t]he duty to keep a contract at common law means a prediction that you must pay damages if you do not keep it—and nothing else.”

The concept of “efficient breach” sees a societal benefit in allowing a party to breach a less desirable contract in order to pursue a more economically beneficial course so long as the non-breaching party is awarded its full expectation interest in the contract. It is for this same reason that contract law, with very limited exceptions, does not countenance punitive damages for breach of contract. In determining the meaning of “willful” in commercial contracts, this school of thought finds it anathema to fundamental contract principles to punish a party who makes the economically rational “deliberate” decision to breach a contract by depriving that party of the bargained-for limitation on damages.

### The ‘MetLife’ Case

Although there is a dearth of published cases that define “willful” in a contract, the New York Court of Appeals has tackled the issue head on in Metropolitan Life Insurance Co. v. Noble Lounodes Int’l, Inc., 84 N.Y.2d 430 (1994). There, a jury found that the defendant, a software licensor, breached its contract to develop and install certain insurance claims software. The contract in that case contained a broad limitation of liability clause, limiting plaintiff’s recovery of consequential damages—by far the largest category available to plaintiff in that case—to only those damages arising out of defendant’s “willful acts or gross negligence.” Nonetheless, after trial, the jury awarded plaintiff a large sum of consequential damages, finding that defendant’s breach had been “willful.” Importantly, the jury also found that the reason for the breach was purely economic self-interest, specifically to escape an “unprofitable business undertaking in order to promote the sale of its computer software division to a competitor company.” Id. at 439.

On appeal, the Appellate Division, First Department, reversed the award of consequential damages, finding that defendant’s breach did not rise to the level of “willful.” In doing so, the Appellate Division adopted the second definition of “willful” outright: “Willful is a term of tort, not contract.” Metropolitan Life Ins. Co. v. Noble Lounodes Int’l, Inc., 192 A.D.2d 83, 90 (1st Dept. 1993). The court found that, as a matter of law, “willful” means a level of intent that rises to the level of an independent tort, which plaintiff had failed to prove.

On appeal, plaintiff argued that the Appellate Division erred in “refusing to attribute the common, ordinary meaning of willful acts as merely deliberate or intentional conduct.” 84 N.Y.2d at 434-35. Instead of accepting the principle of contract construction proposed by the plaintiff (plain and ordinary meaning) and instead of adopting the definition adopted by the Appellate Division, the Court of Appeals opted for another, perhaps more basic, contract axiom: intent of the parties.

The issue here is not how we and other courts have construed “willful” in other contexts, such as in interpreting statutes using that term or in formulating or applying legal principles in tort or contract law. Rather, the issue is what the parties intended by “willful acts” as an exception to their contractual provision limiting defendant’s liability…Id. at 435. Although the Court of Appeals acknowledged that “whether the breaching party deliberately rather than inadvertently failed to perform contractual obligations should not affect the measure of damages,” it refused to apply a blanket definition for “willful.”

Instead, the Court employed standard tools of contractual analysis to determine the intent of the parties. First, it looked to the manner in which the risks of non-performance were distributed throughout the contract. For instance, under one provision of the contract, if defendant had failed to perform in accordance with certain specifications, plaintiff’s sole remedy was to terminate the agreement and receive a full refund. Id. at 436. In another provision, which dealt with one particular service that the Court noted constituted approximately two-thirds of the purchase price, plaintiff’s remedy was limited to (i) terminating the contract, completing the work itself and recovering any cost difference from defendant; or (ii) receiving a full refund of payments already paid to defendant. Id. at 437.

The Court noted that these provisions made clear that the intent of the parties was to place the risks on the shoulders of the plaintiff. In
other words, given the context of the entire agreement, it would make no sense to interpret "willful" to expose the defendant manufacturer to massive consequential damages for intentional non-performance.

Second, but along these same lines, the Court looked at the entire contract and noted that plaintiff could not have been held liable for significant consequential damages if the roles had been reversed and it had been the breaching party. Accordingly, the Court found that it would make no sense to interpret the limitation on liability clause to "eliminate any semblance of reciprocity between plaintiff and defendant as to their exposure to liability for breaching party. Accordingly, the Court found that it would make no sense to interpret the limitation on liability clause to "eliminate any semblance of reciprocity between plaintiff and defendant as to their exposure to liability for breaching party.

Finally, the Court looked at the provision in which the word "willful" appeared and observed that it contained phrases peculiar to tort law, not contract law.

Under the interpretation tool of ejusdem generis applicable to contracts as well as statutes, the phrase "willful acts" should be interpreted here as referring to conduct similar in nature to the "intentional misrepresentation" and "gross negligence" with which it was joined as exceptions to defendant's general immunity from liability for consequential damages. Id. at 438.

In light of the above, the Court of Appeals held that the term "willful acts"—in that contract—was intended by the parties to include only "truly culpable, harmful conduct" and would not include a mere intentional or deliberate breach. Id. at 438. Critically, the Court limited its interpretation of the term "willful" to the meaning contained within the four corners of that particular contract and expressly overturned the holding of the Appellate Division to the extent it purported to define the term with respect to all contracts as a matter of law. Id. at 435.

After ‘MetLife’

Both before and after the MetLife decision, there are almost no other published cases on this issue. Although there is little reason to believe a court would depart from the reasoning of New York's highest court, there is scant guidance as to how lower courts will go about determining whether parties intended to use one or the other definition of "willful" in a commercial contract. The lack of guidance on this issue is further complicated by the fact that two federal district court cases dealing with motions. The most notable examples are two federal district court cases dealing with motions. The most notable examples are two federal district court cases dealing with motions.

Conclusion

The broader lesson, of course, is that parties should recognize the inherent ambiguity of the term "willful" and draft their commercial agreements to avoid leaving this issue in the hands of judges, parties can—and should—make the definition clear on the face of the contract. They should be advised either to use a different word (e.g., "malicious" or "deliberate") or simply to define "willful" (e.g., "acts taken with malice and in bad faith, which rises to the malicious/tortious level.

Breach as Independent Tort

Although cases dealing with contractual definitions of "willful" are scarce, there are a number of cases involving Vtech. For example, in Vtech Holdings, Ltd. v. Lucent Technologies, Inc., 172 F.Supp.2d 435 (S.D.N.Y. 2001), plaintiff Vtech claimed that it was entitled to hundreds of millions of dollars in consequential damages arising out of Lucent’s breach of warranty under a merger contract. On a motion to dismiss, Lucent argued that the claim should be dismissed because plaintiff was not entitled to "consequential damages for intentional wrongdoing.

Kalsch-Jarche, Inc. v. City of New York, 58 N.Y.2d 377 (1983). The second area where this issue arises is where a party seeks punitive damages for breach of contract. In Delaware, for example, while punitive damages are not generally available for breach of contract, they can be awarded if the conduct is willful or malicious. For a party's breach of contract to be considered willful or wanton, such conduct must be 'malicious' and without probable cause, for the purpose of injuring [the other party] by depriving him of the benefits of the contract."

The American Original Corp. v. Legend, Inc., 689 F.Supp. 372, 388-89 (S.D.N.Y. 1988). While these cases and their progeny may not convince a judge that "willful" means "tortious" as a matter of law—at least not in a New York court—they give guidance regarding the types of conduct that courts have held to meet (or not meet) the higher level of culpability. The MetLife decision in the Appellate Division provides a useful overview of that concept: [T]he necessary theory of the complaint is that breach of contract may be so intended and planned; so purposely fitted to time, and circumstances and conditions; so interwoven into a scheme of oppression and fraud as to make the breach of contract an innocent cause which otherwise would not operate, as to cease to be a mere breach of contract, and become, in its association with the attendant circumstances, a tortious and wrongful act or omission.


2. This line of cases, of course, raises the question of why parties would even need to carve out a willful/malicious breach exception from a damages limitation provision when courts have already done so by operation of law.

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