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Court of Appeal decision on assessment of damages for non-acceptance under the Default Clause

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The Gafta Default Clause will be familiar to parties who trade on Gafta contract terms. It governs the measure of damages payable in default of fulfilment of the contract by either party. In *Sharp v Viterra*[1], the Court of Appeal has clarified this measure by finding that under sub-clause (c) the "*actual or estimated value of the goods, on the date of default*" is to be measured by reference to a notional substitute contract entered into on the date of default and on identical terms, except as to price.

What happened?

As discussed in the April 2022 edition of Gaftaworld, the parties entered into two contracts for the sale and purchase of lentils and peas from Vancouver to Mundra, India, on C&F Free Out terms. Payment was to be by cash against documents five days prior to the vessel's arrival at the discharge port but the buyer did not pay on time. The goods were discharged, customs cleared and stored in a warehouse pending payment, against a letter of indemnity from the buyer to the seller.

The parties also agreed an Addendum allowing the buyer to pay in instalments. However, it failed to do so. During this time, the Indian government imposed import tariffs on lentils. The buyer eventually released the goods to the seller who sold them to another buyer, C&F FO Mundra.

The seller claimed damages for non-acceptance under the Default Clause. The key question was whether, under sub-clause (c), the "*actual or estimated value of the goods, on the date of default*" was to be assessed by reference to (a) the market value of the goods at the discharge port, where they were located on the date of default (i.e. customs cleared in Mundra); or (b) the theoretical cost on the date of default of (i) buying the goods FOB at Vancouver, plus (ii) the market freight rate for transporting them to Mundra free out. This had a significant impact on quantum, as the value of the customs cleared goods in Mundra had increased substantially due to the imposition of tariffs.

The Gafta Board of Appeal found in favour of the seller and the buyer appealed to the High Court. The High Court dismissed the buyer's appeal and held that the authorities overall supported the seller's argument that the value of the goods should be based on a notional substitute contract on the same terms. The buyer appealed.

The Court of Appeal decision

The Court of Appeal found that, applying *Bunge v Nidera*[2], sub-clause (c) reflects the common law compensatory measure of loss, which requires that the injured party be put insofar as possible in the same position as if the contract had been performed. The measure of damages had to reflect the nature of the bargain the innocent party had lost. The words "*actual or estimated loss*" contemplate a measure of loss by reference to the market price of different but comparable goods. The loss of bargain must be measured by reference to a notional substitute contract entered into on the date of default on identical terms, except as to price.

The Court of Appeal went on to find that the effect of the letter of indemnity and the Addendum was that at the date of default, the contracts were no longer sales on C&F terms. Aside from the fact that risk had already passed to the buyer, the terms were otherwise an ex-warehouse sale of the specific goods.

In reaching this conclusion, the Court of Appeal held that it was possible to frame the question of law it was required to answer as being what was the proper measure of damages under sub-clause (c) *in the factual circumstances found by the Gafta Board*. This enabled it to consider the issue based on the contract as varied at the date of default, rather than on C&F FO terms.

Comment

The Court of Appeal's analysis of the compensatory principle of the measure of damages is undoubtedly correct. However, the seller can understandably feel aggrieved that the Court of Appeal reached its decision based on a line of reasoning that was not pleaded by the buyer and that required the grounds of appeal to be recast.

The decision is a useful reminder of the principles of the common law measure of damages and the importance of correctly analysing the nature and terms of the contract as at the date of default. When faced with a counterparty in default, careful consideration should be given whether to amend contracts to enable performance. It is also important to remember that there may be more than one default and the measure of damages may vary significantly depending on which date is used to assess the loss. Finally, bear in mind that it may be possible to recover additional expenses by reference to breaches of other terms of the contract, which would fall outside the scope of sub-clause (c).

[1] [2023] EWCA Civ 7 • [2] [2015] UKSC 43