Norwegian Sale Agreement - Damages vs. Deposit?

Where a buyer under a Memorandum of Agreement ("MOA") to purchase a ship fails to pay the deposit due and is in repudiatory breach, is the seller's claim limited to compensation for the actual loss flowing from the lost sale or, if greater, the deposit? This was the issue that was recently before the English High Court in Griffin Shipping LLC and Filodri Shipping Ltd [2013] EWHC 693 (Comm).

Facts

Griffin Shipping ("the Sellers") agreed to sell the MV Griffin to Filodri Shipping ("the Buyers") for US$22 million. The parties entered into a MOA which was on the Norwegian Saleform 1993 ("NSF 1993"), commonly used in ship sale and purchase agreements, and which was signed on 1st May 2010. A deposit of 10% (US$2,146,000) was payable within three banking days of signing the MOA. However, the Buyers did not pay the deposit. As a consequence, the Sellers cancelled the MOA in reliance on the Buyers’ repudiatory conduct in failing to pay the deposit and claimed the deposit. Their loss was based on the difference between the contract and market price of the vessel which was US$275,000 - a sum considerably lower than the deposit.

The claim was referred to Arbitration. The Sellers argued that the right to payment of the deposit had accrued before the MOA was terminated, and therefore they were entitled to claim the deposit, either as a debt or as damages for breach of contract. Buyers, on the other hand, maintained that the Sellers were only entitled to claim "compensation for losses" and not the deposit. The Tribunal preferred the Buyer’s case.

The Tribunal appealed the Tribunal’s decision to the High Court. The High Court concluded that the Tribunal erred in law and found in favour of the Sellers on the preliminary issue before them. It should be noted that the Buyers have appealed the High Court’s decision to the Court of Appeal, which is currently pending.

The Tribunal's decision

The MOA contained the following clauses which were relevant to the issues in dispute:

2. Deposit

As security for the correct fulfillment of this Agreement the Buyer shall pay a deposit of 10% (ten per cent) of the Purchase Price within 3 (three) banking days after this Agreement is signed by both parties and exchange by fax/email. This deposit shall be placed in the Sellers’ nominated account with the Royal Bank of Scotland PLC, Piraeus and held by them in a joint interest bearing account for the Sellers and the Buyers, to be released in accordance with joint written instructions of the Sellers and the Buyers ....

3. Payment

The said Purchase Price ... shall be paid ... on delivery of the vessel ....

13. Buyers’ default

Should the deposit not be paid in accordance with Clause 2, the Sellers have the right to cancel this Agreement, and they shall be entitled to claim compensation for their losses and for all expenses incurred together with interest.

Should the Purchase Price not be paid in accordance with Clause 3, the Sellers have the right to cancel the Agreement, in which case the deposit together with interest earned shall be released to the Sellers. If the deposit does not cover their loss, the Sellers shall be entitled to claim further compensation for their losses and all expenses incurred together with interest.

The Tribunal had concluded that:

- In the event of a breach of clause 2, i.e. a failure to pay the deposit, the only right under clause 13 was to claim "compensation", not the deposit; and

- The parties could have expressed an intention mirroring the second paragraph of clause 13 – that refers to a failure to pay the purchase price – by including wording to the effect that if cancelled for a breach of clause 2, the Sellers were entitled to claim the deposit and/or any additional compensation for losses in excess of the deposit, but they had not.

The Tribunal's decision was in stark contrast to an earlier London arbitration decision (2011) in which a claim for the deposit under the NSF 1993 where the deposit had not been paid succeeded either because the deposit had fallen due before the contract was terminated or as damages for breach of the obligation to pay the deposit. The Tribunal felt that "compensation" in the first paragraph of clause 13 was wide enough to include the value of the deposit. Similarly, in "The Blankenstein" (1985), the deposit was not paid by the Buyers and the Court of Appeal allowed a claim for damages for the amount of the deposit. In this case, Robert Goff LJ, dissenting, considered that the Sellers were only entitled to damages for the difference between the contract and market price of the ship, while in "Zalco Marine Services v Humboldt Shipping" (1988), the Court of Appeal held that the Sellers' only remedy was for "compensation" under the first paragraph of clause 13.

The High Court decision

The Judge held that the language of the MOA enabled the Sellers to recover the deposit because clause 2 described the deposit as security for "the correct fulfillment" of the MOA, and that the rights provided by clause 13 were in addition to the right to claim the deposit as a debt.

Moreover, the judge highlighted the distinction between a requirement to pay a deposit and a partial payment of an agreed price. If a deposit is paid, it is to be forfeited if the contract comes to an end because it is paid as "an earnest of performance". It is forfeited if the Buyer fails to perform, even where the deposit exceeds the loss of bargain damages, and there is no commercial or business sense in permitting a buyer to improve their position simply by not paying the deposit.

Accordingly, because accrued rights are not lost by the subsequent termination of a contract, since the obligation to pay the deposit had fallen due before the contract had been terminated, the Court allowed the Sellers’ appeal, and they were entitled to recover the amount of the deposit as a
Where the contract has been terminated, the Court of Appeal may have allowed a claim for the amount of the deposit as a debt, or by way of damages.

Comment
It is understood the decision is being appealed.

Meanwhile, and given the conflicting decisions, until there is greater certainty it is advisable that the parties to any vessel sale and purchase contract give careful consideration to the status of the deposit. Furthermore, while “The Griffin” concerns the NSF 1993 (and the 1988 form in “The Blankenstein”), the amended NSF 2012 does not expressly address this issue.

In contrast, the Singapore Sale Form (“SSF”) seeks to address the situation.

“[Sellers] … shall be entitled to claim compensation for their losses and expenses (but with no automatic right to compensation in the amount of the deposit).”

Note: Click here to read our article which discusses the Court of Appeal decision in this matter.

© 2020