Global Arbitration Review

The Middle Eastern and African Arbitration Review

2023

Economic damages: a reconsideration of retrospective valuation

The Middle Eastern and African Arbitration Review

2023

The Middle Eastern and African Arbitration Review 2023 contains insight and thought leadership from 15 preeminent practitioners from the region. It provides an invaluable retrospective on what has been happening in some of Europe's more interesting seats.

This edition also contains think pieces on human rights in arbitration, the mechanism's growing use in technology disputes, damages in investment disputes and the use of statistical samples.

Generated: March 7, 2024

GAR Global Arbitration Review

Explore on GAR

Economic damages: a reconsideration of retrospective valuation

Jennifer Paterson, **Mohammad Rwashdeh**, **Kami Zargar** and **James Church-Morley**

FTI Consulting

K&L Gates LLP

Summary

In summary

The date at which damages are assessed or an asset is valued may have a significant impact on the quantum of damages or the value of the asset. This impact could be increasingly material during the times of economic uncertainty. This article provides an overview of the legal principles (under both common law and civil law) that underpin the determination of the appropriate date of assessment for damages. It then considers the practical implications of this determination on the quantification of damages.

Discussion points

- Date of damages assessment under common law and civil law, and impact of the date of assessment and use of hindsight on the assessment of damages
- Application of the date of assessment in measuring a claimant's financial position in the 'counterfactual' and 'actual' scenarios
- Significance of the date of assessment in times of economic uncertainty

Referenced in this article

- *MDW Holdings Limited v James Robert Norvill and Others* [2022] EWCA Civ 883
- *Golden Strait Corporation v Nippon Yusen Kubishika Kaisha* [2007] UKHL 12
- *Classic Maritime Inc v Limbungan Makmur SDN BHD & Anor* [2019] EWCA Civ 1102
- Dubai Court of Cassation Case No. 246/2022 Civil, Case No. 457/2017 Civil, Case No. 412/2018 Civil, Case No. 111/2017 Civil

The date at which damages are assessed or an asset is valued will often inform the appropriate valuation methodologies to adopt and the information that can be considered. The date of assessment may have a material impact on the assessed value. It is therefore important for legal counsel and experts to accurately determine the appropriate date of assessment to ensure that the appropriate analysis can be performed. This article provides an overview of the legal and valuation principles that underpin the determination of the appropriate date of assessment for damages.

We first consider the appropriate date of assessment and compare approaches under civil and common law. Second, we explore the implications of the date of assessment for assessing damages. Finally, we illustrate how a change in the date of assessment can impact damages by way of a simplified hypothetical scenario.

A damages assessment is determined by the information that can be referred to and relied upon. In turn, the information that can be relied upon is determined by the date of assessment. In times of economic uncertainty or volatility, small changes to the date of assessment may have material impacts on the assessment of damages.

Common law position

Under English common law, it is important to determine whether the basis for the damages assessment is a claim for breach of contract or in tort. In a breach of contract claim, the compensatory principle involves asking what position the innocent party would have been in had the contract been properly performed and seeking, as far as money can do it, to place the innocent party in the same situation, with respect to damages, as if the contract had been performed. In contrast, the general aim of an award of damages in tort is to put the injured party in the same position as they would have been in if the tort had not occurred.

The general rule under English law in tort and for breach of contract is that damages are to be assessed as at the date of the breach, that being the date on which the claimant's loss crystallised. Accordingly, events subsequent to the breach are generally not considered when assessing damages.

For example, the general measure of damages under a claim for deceit under English law (a tort arising from a false statement of fact made by one person, knowingly or recklessly, with the intent that it shall be acted on by another, who suffers damages as a result), is the price paid less the benefits received as a result of the transaction (ie, the value of the property acquired on the date of acquisition). Subsequent events are not relevant to the damages assessment because whatever happened after the acquisition date does not affect the value of the property on the date of acquisition.

Similarly, English cases concerning breaches of contractual warranties given in respect of a sale of shares – where the measure of damages is generally the difference between the 'as warranted' value of the shares purchased and their true value – demonstrate that there is a general preclusion of any adjustment on account of later events. Indeed, the Court of Appeal in ***Joiner v George*** [2003] BCC 298 confirmed that the statement made by the judge in the lower court that 'hindsight ought to be excluded' was 'a statement of the general legal principles of share valuation so well established as to require no amplification'.

The issue of whether it was appropriate, in claims arising out of breaches of warranties given in respect of the purchase of shares, to take into account events subsequent to the execution of the share purchase agreement (SPA) was recently considered again by the Court of Appeal in ***MDW Holdings Limited v James Robert Norvill and Others*** [2022] EWCA Civ 883. In that case, the buyer successfully brought a claim against the sellers of shares in a waste management company for damages for deceit and breach of contractual warranties on the basis that the company had been operating in breach of applicable laws. The High Court awarded damages on a contractual basis in an amount that reflected the difference between the value of the business on the basis that the warranties were true versus the actual value of the business given that the warranties were false. When valuing the business on the basis that the warranties were false, the court considered that it was appropriate to make a reduction in the multiplier used to value the business to reflect the reputational damage (or damage to the company's goodwill) that breaches of the warranties were liable to cause to the company, notwithstanding that there had been no regulator intervention, and therefore, the risk of impairment to the goodwill of the business never materialised.

On appeal, the Court of Appeal considered whether it was appropriate when assessing damages to take into account that there was no actual impairment to the goodwill of the business. The Court of Appeal held that, in general, a defendant cannot limit its liability for breach of warranty on a share sale by showing that a contingency, which as at the date of the sale, could have reduced the value of the shares did not in fact materialise. If a particular risk does, or does not, occur, the value of the shares may increase or decrease, but that will not retrospectively change the value of the shares at the time they were sold.

The Court of Appeal stated that it would be rare for it to be appropriate in a breach of warranty case to refer to subsequent events to consider whether a contingency occurred, and it would likely involve situations where the purchaser would otherwise gain an unjustified windfall. An increase in the value of the relevant shares since the date of the SPA is not sufficient to demonstrate a windfall, particularly if the increase is the result of steps taken by the purchaser after the transaction.

However, there are certain instances in which a court (or arbitral tribunal) applying English law may depart from this general rule and take into account events subsequent to the breach when assessing damages. One example is where damages fall to be assessed in respect of an anticipatory breach of contract (ie, a breach of contract whereby one party repudiates the contract before performance is due, by indicating its intention not to perform its obligations), which was accepted, where it is appropriate to consider what would have happened if the breach had not occurred and, in that context, events subsequent to the breach may be relevant.

This concept is illustrated by ***Golden Strait Corporation v Nippon Yusen Kubishika Kaisha*** [2007] UKHL 12, which concerned damages for a breach of a seven-year charter party dated 10 July 1998. In December 2001, the charterers repudiated the charter by redelivering the vessel to the owners, and the owners accepted the repudiation a few days later. At this point, the charter had nearly four years to run. Subsequently, in March 2003, a war broke out, which fell within a contractual provision that gave both parties the right to cancel if war or hostilities were to break out between certain countries. The House of Lords held (by majority) that the outbreak of war should be considered and the owners were not entitled to damages after March 2003; otherwise, the level of compensation would exceed the actual loss.

Lord Scott of Foscote noted that, in cases where the contract was not for a one-off sale, but for the supply of goods or services over a specified period, the application of the general rule – that damages should be assessed at the date of breach – may not be appropriate. He demonstrated this point with the example of the case of a three-year supply contract for the supply of goods and a repudiatory breach of contract at the end of the first year that was accepted. If, before damages were assessed, an event occurred that would have been a frustrating event terminating the contract (eg, legislation prohibiting the sale of the goods), the contractual benefit that the victim of the breach had been deprived of would not have extended beyond the frustrating event, and therefore, there was no principled basis for awarding damages after that date. In his opinion, the same would be true of any anticipatory breach, the acceptance of which had terminated an executory contract.

He explained:

> The contractual benefit for the loss of which the victim of the breach can seek compensation cannot escape the uncertainties of the future. If, at the time the assessment of damages takes place, there were nothing to suggest that

> the expected benefit of the executory contract would not, if the contract had remained on foot, have duly accrued, then the quantum of damages would be unaffected by uncertainties that would be no more than conceptual. If there were a real possibility that an event would happen terminating the contract, or in some way reducing the contractual benefit to which the damages claimant would, if the contract had remained on foot, have become entitled, then the quantum of damages might need, in order to reflect the extent of the chance that that possibility might materialize, to be reduced proportionately. . . . But if a terminating event had happened, speculation would not be needed, an estimate of the extent of the chance of such a happening would no longer be necessary and, in relation to the period during which the contract would have remained executory had it not been for the terminating event, it would be apparent that the earlier anticipatory breach of contract had deprived the victim of the breach of nothing.

This exception, which has been held to apply in respect of an anticipatory breach of contract, has limited application and does not extend to claims arising out of actual breach of contract. For example, ***Classic Maritime Inc v Limbungan Makmur SDN BHD & Anor*** [2019] EWCA Civ 1102 concerned a long-term contract of affreightment providing for shipments of iron ore pellets and the charterer's failure to provide seven shipments. The issue in dispute concerned the assessment of damages relating to what should have been the third-to-seventh shipments. The High Court found that the failure of the Fundao dam in Brazil had made it impossible for the charterer to perform the contract in respect of the third-to-seventh shipments, but also that the charterer would have defaulted on those shipments even if the dam had not burst.

It was common ground that the charterer's obligation to supply cargoes was an absolute obligation subject only to a contractual exceptions clause, which protected it from liability in certain circumstances (similar to a force majeure clause). It was accepted that the burst dam was a qualifying event, but the High Court found that the loss did not result from the burst dam, and therefore the contractual defence was not available to the charterer.

The judge held that, notwithstanding that the charterer was unable to excuse its failure by reference to a contractual exclusion of liability clause, the claimant was not entitled to substantial damages for the charterer's failure to supply and ship the five cargoes. The reasoning for this decision was that, even if the charterer had been able and willing to ship the five cargoes, no cargoes would, in fact, have been shipped because of the dam burst, which would have excused the charterer from its failure to make the required shipments; therefore, a substantial award of damages would breach the compensatory principle.

The Court of Appeal disagreed and held that the dam bursting did not absolve the charterer from liability for substantial damages. In reaching this conclusion, the Court of Appeal distinguished between cases concerning the assessment of damages for an anticipatory breach and cases of actual breach. In cases of anticipatory breach, such as in the ***Golden Strait Corporation*** case, the court was required to value the innocent party's right to future performance. The compensatory principle operated to reduce or extinguish the innocent party's damages because the value of the performance to which that party was entitled was adversely affected by events that occurred after the acceptance of the repudiation.

In contrast, the ***Classic Maritime Inc*** case was not concerned with an anticipatory breach but with actual breaches as a result of the charterer's failure to supply cargoes for each of the shipments in issue. The value of the performance to which the shipowner was entitled (the supply of cargoes) was the freights that the shipowner would have earned if the cargoes had been supplied less the cost of earning them. Therefore, the assessment of damages was the difference between the freights that the shipowner would have earned less the cost of earning them and the actual position in which the shipowner found itself as a result of the breach.

In summary, in common law, the general rule is that damages are to be assessed at the date of the breach and events subsequent to the breach are not considered. However, there are a few limited circumstances in which subsequent events may be considered, for example, in the case of anticipatory breach.

Civil law position

Under civil law, the underlying principle for awarding damages in contract and tort is broadly the same. In both types of claims, the law provides that an injured party is entitled to receive direct damages commensurate to the actual loss sustained, taking into consideration all of the surrounding circumstances.[1] Accordingly, while not expressed in these terms, civil law effectively seeks to place the injured party, insofar as is possible, in the position it would have been in had it not been for the act that gave rise to the damage.

The main difference between the award of damages for actions in contract and tort is that liability for a contractual breach is limited to direct damages that were reasonably foreseeable upon entry into the contract, whereas in tort, an injured party may recover direct damages for all loss suffered, without needing to prove such loss was reasonably foreseeable.

When assessing damages, civil law draws a distinction between variable loss and invariable loss. In the event of an invariable loss, such as compensation for a written-off car, the damage is calculated by assessing the market value of the car at the date of the damage.[2] Another example is a claim for damages against the seller of property or a product in the event of deceit, defect or breach of contractual warranties, which rendered the property or product significantly less valuable than would otherwise have been the case. In these cases, the loss in value – which may be calculated as the difference between the price paid and the true value of the property or product – is assessed on the date of the transaction, without taking into account subsequent events.

In contrast, where there is variable loss (such as a continuing loss of profit or the fluctuating price of replacement parts), the general rule is that loss is calculated at the point that damages are assessed and awarded, taking into account all of the circumstances. Accordingly, irrespective of whether the claim is in contract or tort, damages should be assessed at the time of the judgment, and the circumstances between the date of the event giving rise to the claim and the judgment date must be considered.[3]

The renowned Egyptian scholar Professor Abdel Razzaq Al Sanhouri gives the example of where a person is hit by a car due to the driver's fault and sustained a fracture in his or her hand.[4] After he or she claimed compensation, the fracture developed and became more serious, and when the judgment was issued, the severity had increased and had turned into a permanent disability. Al Sanhouri states that the judge must take into account the change in the severity of the injury suffered when assessing damages (whether the injury has improved or worsened). Al Sanhouri further states that other types of changes between the date of injury and the judgment date must also be considered, such as fluctuation in currency, market prices, etc. However, by contrast, in the event that the injured party has remedied the damage (for example, fixed a damaged car), their only recourse is to the amount actually paid regardless of any changes that may occur before the judgment date (such as the change in the price of spare parts or labour costs).

In Dubai Court of Cassation Case No. 412/2018 Civil, the Court of Cassation was required to consider an award of damages made to a hotel apartment owner for loss caused by a fire, which was started due to an electrical short circuit caused by the hotel's negligence and that resulted in closure of the hotel for repair work for a period of two years. At first instance, the assessment of damages was calculated by a court-appointed expert who assumed the same level of rent would have been received by the apartment owner throughout the period that the hotel was closed for repair. The matter was ultimately appealed by the defendants to the Court of Cassation, who held that the assessment of damages must be fair and commensurate to the damage suffered and, therefore, should have been reduced to reflect the fall in rental values that had occurred between the incident and the judgment date.

Accordingly, in civil law, the general rule is that, in the case of variable damages, assessment is made at the date of the award. However, where the damage is invariable, it is assessed on the date that the damage was suffered. In other words, damages should be assessed when the loss crystallised, either at the time the damage was incurred or at the time of the award.

Implications of the date of assessment for assessing damages

Typically, valuation and damages experts are instructed to assess damages in claims for lost profits or in the diminution of the value of an asset (such as shares, a business or entitlement to future profits under a contractual right) arising from a breach of contract, warranty, obligation or treaty.

To do so, the expert compares the claimant's financial position in two scenarios:

- a counterfactual scenario under which the alleged breach complained of never occurred, and the claimant and respondent performed their contractual obligations. This is often referred to as the 'but for scenario' or 'counterfactual scenario'; and
- the claimant's actual financial position, taking into consideration the financial impact of the alleged breaches. This is often referred to as the 'actual scenario'.

There are a number of approaches available to calculate the claimant's financial position in these scenarios. The expert is typically required to make assumptions about either the claimant's future growth prospects, or those of the asset that belongs to it, and the risk associated with those prospects under each of these approaches.[5] These assumptions are benchmarked against information that would have been available at the date of assessment. The date at which damages are assessed is therefore important, as an expert must reflect expectations at that date. Information that came to light after this date is considered 'hindsight' information and should typically be disregarded.

As noted above, under common law, damages are typically assessed at the date of breach. In contrast, under civil law, damages are often assessed when they are awarded, taking into consideration all the circumstances of the matter. Accordingly, experts are typically instructed to assess damages at the date of breach or the date of award, or both if there is a dispute about this issue.

In the assessment of damages, the expert should only consider information known or foreseeable at the date of assessment. This is because the expert, especially when performing the valuation of an asset, is often asked to consider what value a hypothetical purchaser or seller would accept in a transaction. The expert can therefore only consider information that would have been available to the hypothetical parties.

Hindsight information, or information that became known after this date, should typically be disregarded. This means that when a date of breach is adopted as the date of assessment they can only consider information known or foreseeable at that point in time. In contrast, where the date of award is adopted, there is no limit on what information can be considered, either historical or prospective.

Where there is a long period of time between the date of breach and the date of award, this can result in material differences in the information that can be relied upon, as well as future expectations. These differences can have wide-ranging effects.

The above principles also apply to the assessment of damages arising from breach of warranties in the context of a share sale. Such assessments are made as at the date of the breach, which is usually the date of the SPA. These assessments typically ignore events after the date of the SPA and the information available thereof.

As noted above, in the ***MDW Holdings Ltd*** case, the Court of Appeal held that hindsight information would only be taken into consideration when assessing the value of shares on the basis that the warranties were false in exceptional cases, where ignoring post-SPA events would result in a party receiving a windfall.

While the price paid for shares is often used as a proxy to determine the value of the shares had the warranties been true, different factors, such as market conditions at the date of the SPA, can lead to a difference between the purchase price paid and the value. The experts need to carefully identify the correct position had the warranties been true, guided by the relevant legal instructions, the underlying deal and market circumstances at the date of the SPA.

As explained above, under civil law, the assessment of damages arising from warranty claims is broadly similar to common law, except that, under civil law, the value had the warranties been true is typically inferred from the price paid.

In the following subsections, we discuss the impact of the date of assessment on projections of the claimant's financial position in the counterfactual and actual scenarios. We also consider how the date adopted may impact discounting and the application of interest. Finally, we present a case study to explain how the date of assessment plays an important role in assessing damages.

The claimant's financial position in the counterfactual scenario

The counterfactual scenario reflects the financial position that the claimant would have been in absent the alleged breach. In this scenario, the expert is required to make explicit assumptions about growth and risk in a scenario that does not, and will not, exist. The expert may also be required to project the claimant's financial position a long way into the future, which causes additional uncertainty.

Where the expert adopts the date of breach as the date of assessment, the expert should only consider information known or foreseeable as at the date of assessment without using hindsight. This principle is consistent with the judgment in the ***Classic Maritime*** Inc case.

However, this results in practical challenges for the expert that do not exist when adopting the date of award as the date of assessment. For example, if a substantial amount of time has passed since the date of breach, it may be hard to determine what information was known or foreseeable as at the date of breach. The passage of time may also highlight differences between expectations at the date of breach and information that became known after this date.

In such damages assessments, an expert may, for example, refer to contemporaneous forecasts of cash flows to estimate the claimant's financial position. However, the expert should ensure that these forecasts only reflect expectations as at the date of breach and have not been updated afterwards to reflect actual performance, which involves hindsight information.

This position is further complicated where external factors may impact the underlying business after the date of breach. In recent years, such events include the outbreak of the covid-19 pandemic and the ongoing Russia–Ukraine conflict. Recent rapid growth in inflation and interest rates also impact expectations. These events may result in material changes to future expectations.

In contrast, where the expert adopts the date of award as the date of assessment, the expert may consider all information known at that point including such events that only came into existence after the date of breach. The impact of these events on future expectations beyond the date of assessment, and therefore the date of award, should also be considered.

When projecting the claimant's financial position in the counterfactual scenario, experts need to ensure that the information to which they refer is in keeping with the relevant legal principles described above. Where hindsight is not allowed, it is important that the counterfactual scenario reflects only information that is known or foreseeable as at the date of assessment. However, as explained above, there are limited circumstances where, under common law, hindsight may be considered in the assessment of damages.

The claimant's financial position in the actual scenario

The actual scenario reflects the financial position of the claimant, taking into consideration the impact of the alleged breach. In this scenario, the expert may still need to consider future expectations for the claimant's financial position after the breach. However, where the breach results in a complete cessation of activity, the claimant's financial position in the actual scenario may be nil, as no further cash will be earned, or may even be negative, to reflect that the claimant may need to incur costs following the breach.

When assessing damages at the date of breach, experts are likely to have access to information concerning the real-world financial position of the claimant following the date of breach. Due to this, experts often adopt the claimant's real-world financial position as a proxy to determine its financial position in the actual scenario.

When doing so, experts need to consider whether such an approach creates an inconsistency between the information used in the counterfactual scenario and in the actual scenario. In instances where there have been material changes in the economic and business environment following the date of the alleged breach (such as a date of breach followed by the covid-19 pandemic), the financial position in one scenario may reflect factors that are not captured in the other. This may result in the assessment of damages capturing the impact of these factors, which are not attributable to the alleged breach.

Experts should also consider whether the claimant's real-world financial position includes attempts to mitigate loss (such as rationalising headcount that is surplus to requirement or selling assets that have become redundant). If it does not, some form of adjustment may be required.

In the past few years, global economic events have resulted in rapid changes in the economic environment. As disputes with a date of assessment in this period crystallise, it will be important for experts to explain how they project the claimant's financial position in the actual scenario and the extent to which this is done by reference to the claimant's real-world financial position following the date of breach.

Discounting and the application of interest

One approach used to assess damages is a discounted cash flow (DCF) model. In a DCF model, the expert projects future cash flows for an asset or contract and then converts them into a single lump sum amount at the relevant date of assessment by applying a discount rate.

The discount rate reflects two factors. The first is the time value of money, or that a dollar today is worth more than a dollar in one year as it can be invested and earn a return in the interim. The second is that there is no guarantee that a party will actually receive the amount of money that they project. They may receive more or less than the projected amount (or none at all) and they may receive it earlier or later than they project. This uncertainty is reflected in the discount rate.

When using the date of breach as the date of assessment, projected cash flows in the counterfactual and actual scenarios are discounted to arrive at a single lump sum amount at the date of breach. Pre-judgment interest is then applied to this lump sum amount to state the damages in present terms at the date of the award.

When the date of award is adopted as the date of assessment, interest is applied to all cash flows that were impacted as a result of the breach, or would have been impacted, prior to this date of award to state them in present terms. All future cash flows are discounted to a lump sum amount at this date.

The cost of equity, or the return that investors require to provide equity capital for an investment, or to a company, is one of the key components of the discount rate. One common model used to estimate the cost of equity is the capital asset pricing model (CAPM).[6] This has three inputs:

- a risk-free rate, which reflects the return an investor could earn on a risk-free security, such as a government treasury instrument;
- the equity risk premium, which reflects the return required by investors to invest in equities as opposed to risk-free instruments; and
- beta, which reflects the risk of a particular sector or industry relative to the market as a whole.[7]

The input for the CAPM changes on a daily basis to reflect various economic and market factors, including, inter alia, movements in the yields on risk-free instruments, expectations as to the returns on equities and movements in the prices of listed shares. Changes in inflation and interest rates also impact the calculation of the discount rate. Similarly, interest rates used to calculate prejudgment interest may be based on prevailing lending rates. These also change over time to reflect market conditions.

Due to this, moving the date of assessment can result in changes to the discount rate or the interest rate, and consequently changes to an expert's assessment of damages. To illustrate this, we provide a simple example where the date of breach is in January 2020 and the date of assessment is in January 2023.

At the date of breach in a hypothetical dispute, the risk-free rate is 1 per cent, the equity risk premium is 6 per cent and the appropriate beta to apply for the claimant is 1. This results in a cost of equity of 7 per cent.[8] However, at the date of assessment these inputs have changed to reflect prevailing market conditions. The risk-free rate is now 3 per cent, the equity risk premium remains at 6 per cent and the appropriate beta to apply remains at 1. The cost of equity is now 9 per cent.[9] This reflects a nearly 30 per cent increase in the cost of equity. All being equal, this results in a lower assessment of damages at the date of assessment, as a higher discount rate results in a lower lump sum amount.

The date of assessment impacts both the chosen discount rate and the interest rate used in an assessment of damages. Changes to these inputs can have material consequences. Experts should be aware of such differences and be able to explain how changing the date of assessment may impact their chosen discount rate and interest rate.

Hypothetical example of how the date of assessment impacts the information that can be considered by an expert

For illustrative purposes, the following example provides a highly simplified description of how changing the date of assessment may impact an assessment of damages in a given hypothetical scenario. This example focuses only on one aspect of the damages calculation, namely, the revenue that the claimant has been deprived of as a result of the alleged breach. This example does not consider other variables or underlying factors such as costs, other cash outflows or categories of loss that may arise and would normally be considered in the assessment of damages.

In this hypothetical scenario, Company A and Company B entered into a contract in which Company B agreed to provide a certain volume of gas to Company A each year at a price consistent with market rates. This contract was agreed in 2013, with a term of 20 years. In breach of its contractual obligations, Company B never provided any gas to Company A. Company A commenced legal proceedings against Company B, seeking compensation for this breach. The date of the award has been set for 2023.

As explained above, the expert will compare Company A's financial position in the counterfactual scenario and the actual scenario. As no gas has been supplied or will be supplied, the expert can assume that in the actual scenario, Company A earned no revenue. The relevant question for the expert is therefore how to assess Company A's financial position in the counterfactual scenario. The date of assessment will impact the approach that an expert adopts, and the information they may consider.

Using the date of breach as the date of assessment, the expert should typically disregard hindsight information. The expert therefore needs to project gas prices for a 20-year period from 2013 and calculate the discount rate associated with the expected revenue from the sale of gas, in 2013. In this hypothetical example, in 2013, the projected price of gas in 2023 was around US$3 per million British thermal units.

In contrast, where the date of award is used as the date of assessment, the expert may be entitled to consider facts that became known after the date of the breach. This means that revenue for the period 2013 to 2023 could be informed by actual gas prices in this period. The expert could adopt actual prices, as opposed to the projected price in 2013 (ie, US$3 per million British thermal units). In this hypothetical example, the projected gas price at the date of award was around US$6 per million British thermal units, as compared to the projected price of US$3 per million British thermal units in 2013, which results in higher revenue in this period.

Furthermore, the expert may project future gas prices from 2023 onwards by reference to contemporaneous projections and events that would inform the price of gas. In this hypothetical example, the expert could refer to the projected gas price of around US$6 per million British thermal units in its assessment of projected revenue for the period 2023 to 2033. This would result in higher revenue projections, as compared to if projections at the date of breach (of US$3 per million British thermal units) were adopted.

In practice, an assessment of damages involves a detailed assessment of the claimant's financial position in both the counterfactual and actual scenarios. This assessment is informed by detailed financial analysis and available data, and refers to the relevant applicable legal principles.

However, as this simplified hypothetical example shows, the information available to the expert, which informs their analysis, may differ depending on the date of assessment. The difference in information may also have material consequences.

Conclusion

As this article shows, the date of assessment is a relevant consideration in assessing damages, and determines the information that the expert can consider. Under both common law and civil law, there are well-developed frameworks for determining the date of assessment.

In common law, the general rule is that damages are to be assessed at the date of breach. However, there are limited circumstances where hindsight information may be considered, for example, in the case of anticipatory breach.

In civil law, the general rule is that, in the case of variable damages, assessment is made at the date of the award. However, where the damage is invariable, the general rule is that damages are assessed on the date that the damage was suffered.

From a damages assessment perspective, hindsight information should typically be disregarded. This means that, when a date of breach is adopted as the assessment date, information that became known after this date should be disregarded. However, where the date of award is adopted, experts may be entitled to adopt all information known at the date of assessment to inform their calculations. This difference in approach changes the information that can be relied upon and the conclusions that experts will arrive at.

* *This information is provided for informational purposes only and nothing in this article should be construed as legal advice. The examples provided throughout are simplified to illustrate the points under discussion and therefore they do not represent the actual practice.*

Footnotes

[1] See articles 292 and 389 of the UAE Civil Code; article 170 of the Egyptian Civil Code; *Al-Waseet in Explaining the Civil Law (al-Wasīṭ fī Sharḥ al-Qānūn al-Madanī al-Jadīd)*, Vol. 1/1 (Beirut: Al-Halabi Legal Publications, 2011), paragraph 648, p. 1098; and Dubai Court of Cassation Judgment No. 246/2022 Civil.

[2] Dubai Court of Cassation Judgment No. 457/2017 Civil.

[3] Dubai Court of Cassation Judgment No. 111/2017 Civil.

[4] *Al-Waseet in Explaining the Civil Law (al-Wasīṭ fī Sharḥ al-Qānūn al-Madanī al-Jadīd)*, Vol. 1/1 (Beirut: Al-Halabi Legal Publications, 2011), paragraph 649, p. 1102.

[5] Experts make assumptions about future growth and risk either explicitly through inputs into a discounted cash flow (DCF) model when preparing cash flow forecasts or by their choice of financial ratio, or multiple ratios, when preparing a multiples analysis.

[6] The capital asset pricing model calculates the cost of equity as: the risk free rate plus the equity risk premium multiplied by the beta.

[7] Beta can generally be thought of as a measure of how much the share price of a company moves as compared to the market as a whole. For example, if a company has a beta of 1.5, it means that when the market moves by 1.0 per cent (either up or down), the share price will move in the same direction by 1.5 per cent. A beta of greater than 1 suggests that a company is more volatile than the market as a whole, and a beta of less than 1 suggests that it is less volatile.

[8] Calculated as 1 per cent + 6 per cent x 1.

[9] Calculated as 3 per cent + 6 per cent x 1.

IN SUMMARY

The date at which damages are assessed or an asset is valued may have a significant impact on the quantum of damages or the value of the asset. This impact could be increasingly material during the times of economic uncertainty. This article provides an overview of the legal principles (under both common law and civil law) that underpin the determination of the appropriate date of assessment for damages. It then considers the practical implications of this determination on the quantification of damages.

DISCUSSION POINTS

- Date of damages assessment under common law and civil law, and impact of the date of assessment and use of hindsight on the assessment of damages
- Application of the date of assessment in measuring a claimant's financial position in the 'counterfactual' and 'actual' scenarios
- Significance of the date of assessment in times of economic uncertainty

---

REFERENCED IN THIS ARTICLE

- *MDW Holdings Limited v James Robert Norvill and Others* [2022] EWCA Civ 883
- *Golden Strait Corporation v Nippon Yusen Kubishika Kaisha* [2007] UKHL 12
- *Classic Maritime Inc v Limbungan Makmur SDN BHD & Anor* [2019] EWCA Civ 1102
- Dubai Court of Cassation Case No. 246/2022 Civil, Case No. 457/2017 Civil, Case No. 412/2018 Civil, Case No. 111/2017 Civil

---

The date at which damages are assessed or an asset is valued will often inform the appropriate valuation methodologies to adopt and the information that can be considered. The date of assessment may have a material impact on the assessed value. It is therefore important for legal counsel and experts to accurately determine the appropriate date of assessment to ensure that the appropriate analysis can be performed. This article provides an overview of the legal and valuation principles that underpin the determination of the appropriate date of assessment for damages.

We first consider the appropriate date of assessment and compare approaches under civil and common law. Second, we explore the implications of the date of assessment for assessing damages. Finally, we illustrate how a change in the date of assessment can impact damages by way of a simplified hypothetical scenario.

A damages assessment is determined by the information that can be referred to and relied upon. In turn, the information that can be relied upon is determined by the date of assessment. In times of economic uncertainty or volatility, small changes to the date of assessment may have material impacts on the assessment of damages.

COMMON LAW POSITION

Under English common law, it is important to determine whether the basis for the damages assessment is a claim for breach of contract or in tort. In a breach of contract claim, the compensatory principle involves asking what position the innocent party would have been in had the contract been properly performed and seeking, as far as money can do it, to place the innocent party in the same situation, with respect to damages, as if the contract had been performed. In contrast, the general aim of an award of damages in tort is to put the injured party in the same position as they would have been in if the tort had not occurred.

The general rule under English law in tort and for breach of contract is that damages are to be assessed as at the date of the breach, that being the date on which the claimant's loss crystallised. Accordingly, events subsequent to the breach are generally not considered when assessing damages.

For example, the general measure of damages under a claim for deceit under English law (a tort arising from a false statement of fact made by one person, knowingly or recklessly, with the intent that it shall be acted on by another, who suffers damages as a result), is the price paid less the benefits received as a result of the transaction (ie, the value of the property acquired on the date of acquisition). Subsequent events are not relevant to the damages assessment because whatever happened after the acquisition date does not affect the value of the property on the date of acquisition.

Similarly, English cases concerning breaches of contractual warranties given in respect of a sale of shares – where the measure of damages is generally the difference between the 'as warranted' value of the shares purchased and their true value – demonstrate that there is a general preclusion of any adjustment on account of later events. Indeed, the Court of Appeal in ***Joiner v George*** [2003] BCC 298 confirmed that the statement made by the judge in the lower court that 'hindsight ought to be excluded' was 'a statement of the general legal principles of share valuation so well established as to require no amplification'.

The issue of whether it was appropriate, in claims arising out of breaches of warranties given in respect of the purchase of shares, to take into account events subsequent to the execution of the share purchase agreement (SPA) was recently considered again by the Court of Appeal in ***MDW Holdings Limited v James Robert Norvill and Others*** [2022] EWCA Civ 883. In that case, the buyer successfully brought a claim against the sellers of shares in a waste management company for damages for deceit and breach of contractual warranties on the basis that the company had been operating in breach of applicable laws. The High Court awarded damages on a contractual basis in an amount that reflected the difference between the value of the business on the basis that the warranties were true versus the actual value of the business given that the warranties were false. When valuing the business on the basis that the warranties were false, the court considered that it was appropriate to make a reduction in the multiplier used to value the business to reflect the reputational damage (or damage to the company's goodwill) that breaches of the warranties were liable to cause to the company, notwithstanding that there had been no regulator intervention, and therefore, the risk of impairment to the goodwill of the business never materialised.

On appeal, the Court of Appeal considered whether it was appropriate when assessing damages to take into account that there was no actual impairment to the goodwill of the business. The Court of Appeal held that, in general, a defendant cannot limit its liability for breach of warranty on a share sale by showing that a contingency, which as at the date of the sale, could have reduced the value of the shares did not in fact materialise. If a particular risk does, or does not, occur, the value of the shares may increase or decrease, but that will not retrospectively change the value of the shares at the time they were sold.

The Court of Appeal stated that it would be rare for it to be appropriate in a breach of warranty case to refer to subsequent events to consider whether a contingency occurred, and it would likely involve situations where the purchaser would otherwise gain an unjustified windfall. An increase in the value of the relevant shares since the date of the SPA is not sufficient to demonstrate a windfall, particularly if the increase is the result of steps taken by the purchaser after the transaction.

However, there are certain instances in which a court (or arbitral tribunal) applying English law may depart from this general rule and take into account events subsequent to the breach when assessing damages. One example is where damages fall to be assessed in respect of an anticipatory breach of contract (ie, a breach of contract whereby one party repudiates the contract before performance is due, by indicating its intention not to perform its obligations), which was accepted, where it is appropriate to consider what would have happened if the breach had not occurred and, in that context, events subsequent to the breach may be relevant.

This concept is illustrated by ***Golden Strait Corporation v Nippon Yusen Kubishika Kaisha*** [2007] UKHL 12, which concerned damages for a breach of a seven-year charter party dated 10 July 1998. In December 2001, the charterers repudiated the charter by redelivering the vessel to the owners, and the owners accepted the repudiation a few days later. At this point, the charter had nearly four years to run. Subsequently, in March 2003, a war broke out, which fell within a contractual provision that gave both parties the right to cancel if war or hostilities were to break out between certain countries. The House of Lords held (by majority) that the outbreak of war should be considered and the owners were not entitled to damages after March 2003; otherwise, the level of compensation would exceed the actual loss.

Lord Scott of Foscote noted that, in cases where the contract was not for a one-off sale, but for the supply of goods or services over a specified period, the application of the general rule – that damages should be assessed at the date of breach – may not be appropriate. He demonstrated this point with the example of the case of a three-year supply contract for the supply of goods and a repudiatory breach of contract at the end of the first year that was accepted. If, before damages were assessed, an event occurred that would have been a frustrating event terminating the contract (eg, legislation prohibiting the sale of the goods), the contractual benefit that the victim of the breach had been deprived of would not have extended beyond the frustrating event, and therefore, there was no principled basis for awarding damages after that date. In his opinion, the same would be true of any anticipatory breach, the acceptance of which had terminated an executory contract.

He explained:

> The contractual benefit for the loss of which the victim of the breach can seek compensation cannot escape the uncertainties of the future. If, at the time the assessment of damages takes place, there were nothing to suggest that the expected benefit of the executory contract would not, if the contract had remained on foot, have duly accrued, then the quantum of damages would be unaffected by uncertainties that would be no more than conceptual. If there were a real possibility that an event would happen terminating the contract, or in some way reducing the contractual benefit to which the damages claimant would, if the contract had remained on foot, have become entitled, then the quantum of damages might need, in order to reflect the extent of the chance

> that that possibility might materialize, to be reduced proportionately. . . . But if a terminating event had happened, speculation would not be needed, an estimate of the extent of the chance of such a happening would no longer be necessary and, in relation to the period during which the contract would have remained executory had it not been for the terminating event, it would be apparent that the earlier anticipatory breach of contract had deprived the victim of the breach of nothing.

This exception, which has been held to apply in respect of an anticipatory breach of contract, has limited application and does not extend to claims arising out of actual breach of contract. For example, ***Classic Maritime Inc v Limbungan Makmur SDN BHD & Anor*** [2019] EWCA Civ 1102 concerned a long-term contract of affreightment providing for shipments of iron ore pellets and the charterer's failure to provide seven shipments. The issue in dispute concerned the assessment of damages relating to what should have been the third-to-seventh shipments. The High Court found that the failure of the Fundao dam in Brazil had made it impossible for the charterer to perform the contract in respect of the third-to-seventh shipments, but also that the charterer would have defaulted on those shipments even if the dam had not burst.

It was common ground that the charterer's obligation to supply cargoes was an absolute obligation subject only to a contractual exceptions clause, which protected it from liability in certain circumstances (similar to a force majeure clause). It was accepted that the burst dam was a qualifying event, but the High Court found that the loss did not result from the burst dam, and therefore the contractual defence was not available to the charterer.

The judge held that, notwithstanding that the charterer was unable to excuse its failure by reference to a contractual exclusion of liability clause, the claimant was not entitled to substantial damages for the charterer's failure to supply and ship the five cargoes. The reasoning for this decision was that, even if the charterer had been able and willing to ship the five cargoes, no cargoes would, in fact, have been shipped because of the dam burst, which would have excused the charterer from its failure to make the required shipments; therefore, a substantial award of damages would breach the compensatory principle.

The Court of Appeal disagreed and held that the dam bursting did not absolve the charterer from liability for substantial damages. In reaching this conclusion, the Court of Appeal distinguished between cases concerning the assessment of damages for an anticipatory breach and cases of actual breach. In cases of anticipatory breach, such as in the ***Golden Strait Corporation*** case, the court was required to value the innocent party's right to future performance. The compensatory principle operated to reduce or extinguish the innocent party's damages because the value of the performance to which that party was entitled was adversely affected by events that occurred after the acceptance of the repudiation.

In contrast, the ***Classic Maritime Inc*** case was not concerned with an anticipatory breach but with actual breaches as a result of the charterer's failure to supply cargoes for each of the shipments in issue. The value of the performance to which the shipowner was entitled (the supply of cargoes) was the freights that the shipowner would have earned if the cargoes had been supplied less the cost of earning them. Therefore, the assessment of damages was the difference between the freights that the shipowner would have earned less the cost of earning them and the actual position in which the shipowner found itself as a result of the breach.

In summary, in common law, the general rule is that damages are to be assessed at the date of the breach and events subsequent to the breach are not considered. However, there are a few limited circumstances in which subsequent events may be considered, for example, in the case of anticipatory breach.

CIVIL LAW POSITION

Under civil law, the underlying principle for awarding damages in contract and tort is broadly the same. In both types of claims, the law provides that an injured party is entitled to receive direct damages commensurate to the actual loss sustained, taking into consideration all of the surrounding circumstances.[1] Accordingly, while not expressed in these terms, civil law effectively seeks to place the injured party, insofar as is possible, in the position it would have been in had it not been for the act that gave rise to the damage.

The main difference between the award of damages for actions in contract and tort is that liability for a contractual breach is limited to direct damages that were reasonably foreseeable upon entry into the contract, whereas in tort, an injured party may recover direct damages for all loss suffered, without needing to prove such loss was reasonably foreseeable.

When assessing damages, civil law draws a distinction between variable loss and invariable loss. In the event of an invariable loss, such as compensation for a written-off car, the damage is calculated by assessing the market value of the car at the date of the damage.[2] Another example is a claim for damages against the seller of property or a product in the event of deceit, defect or breach of contractual warranties, which rendered the property or product significantly less valuable than would otherwise have been the case. In these cases, the loss in value – which may be calculated as the difference between the price paid and the true value of the property or product – is assessed on the date of the transaction, without taking into account subsequent events.

In contrast, where there is variable loss (such as a continuing loss of profit or the fluctuating price of replacement parts), the general rule is that loss is calculated at the point that damages are assessed and awarded, taking into account all of the circumstances. Accordingly, irrespective of whether the claim is in contract or tort, damages should be assessed at the time of the judgment, and the circumstances between the date of the event giving rise to the claim and the judgment date must be considered.[3]

The renowned Egyptian scholar Professor Abdel Razzaq Al Sanhouri gives the example of where a person is hit by a car due to the driver's fault and sustained a fracture in his or her hand.[4] After he or she claimed compensation, the fracture developed and became more serious, and when the judgment was issued, the severity had increased and had turned into a permanent disability. Al Sanhouri states that the judge must take into account the change in the severity of the injury suffered when assessing damages (whether the injury has improved or worsened). Al Sanhouri further states that other types of changes between the date of injury and the judgment date must also be considered, such as fluctuation in currency, market prices, etc. However, by contrast, in the event that the injured party has remedied the damage (for example, fixed a damaged car), their only recourse is to the amount actually paid regardless of any changes that may occur before the judgment date (such as the change in the price of spare parts or labour costs).

In Dubai Court of Cassation Case No. 412/2018 Civil, the Court of Cassation was required to consider an award of damages made to a hotel apartment owner for loss caused by a fire, which was started due to an electrical short circuit caused by the hotel's negligence and that resulted in closure of the hotel for repair work for a period of two years. At first instance, the assessment of damages was calculated by a court-appointed expert who assumed the same level of rent would have been received by the apartment owner throughout the period that the hotel was closed for repair. The matter was ultimately appealed by the defendants to the Court of Cassation, who held that the assessment of damages must be fair and commensurate to the damage suffered and, therefore, should have been reduced to reflect the fall in rental values that had occurred between the incident and the judgment date.

Accordingly, in civil law, the general rule is that, in the case of variable damages, assessment is made at the date of the award. However, where the damage is invariable, it is assessed on the date that the damage was suffered. In other words, damages should be assessed when the loss crystallised, either at the time the damage was incurred or at the time of the award.

IMPLICATIONS OF THE DATE OF ASSESSMENT FOR ASSESSING DAMAGES

Typically, valuation and damages experts are instructed to assess damages in claims for lost profits or in the diminution of the value of an asset (such as shares, a business or entitlement to future profits under a contractual right) arising from a breach of contract, warranty, obligation or treaty.

To do so, the expert compares the claimant's financial position in two scenarios:

- a counterfactual scenario under which the alleged breach complained of never occurred, and the claimant and respondent performed their contractual obligations. This is often referred to as the 'but for scenario' or 'counterfactual scenario'; and
- the claimant's actual financial position, taking into consideration the financial impact of the alleged breaches. This is often referred to as the 'actual scenario'.

There are a number of approaches available to calculate the claimant's financial position in these scenarios. The expert is typically required to make assumptions about either the claimant's future growth prospects, or those of the asset that belongs to it, and the risk associated with those prospects under each of these approaches.[5] These assumptions are benchmarked against information that would have been available at the date of assessment. The date at which damages are assessed is therefore important, as an expert must reflect expectations at that date. Information that came to light after this date is considered 'hindsight' information and should typically be disregarded.

As noted above, under common law, damages are typically assessed at the date of breach. In contrast, under civil law, damages are often assessed when they are awarded, taking into consideration all the circumstances of the matter. Accordingly, experts are typically instructed to assess damages at the date of breach or the date of award, or both if there is a dispute about this issue.

In the assessment of damages, the expert should only consider information known or foreseeable at the date of assessment. This is because the expert, especially when performing the valuation of an asset, is often asked to consider what value a hypothetical purchaser or seller would accept in a transaction. The expert can therefore only consider information that would have been available to the hypothetical parties.

Hindsight information, or information that became known after this date, should typically be disregarded. This means that when a date of breach is adopted as the date of assessment they can only consider information known or foreseeable at that point in time. In contrast, where the date of award is adopted, there is no limit on what information can be considered, either historical or prospective.

Where there is a long period of time between the date of breach and the date of award, this can result in material differences in the information that can be relied upon, as well as future expectations. These differences can have wide-ranging effects.

The above principles also apply to the assessment of damages arising from breach of warranties in the context of a share sale. Such assessments are made as at the date of the breach, which is usually the date of the SPA. These assessments typically ignore events after the date of the SPA and the information available thereof.

As noted above, in the ***MDW Holdings Ltd*** case, the Court of Appeal held that hindsight information would only be taken into consideration when assessing the value of shares on the basis that the warranties were false in exceptional cases, where ignoring post-SPA events would result in a party receiving a windfall.

While the price paid for shares is often used as a proxy to determine the value of the shares had the warranties been true, different factors, such as market conditions at the date of the SPA, can lead to a difference between the purchase price paid and the value. The experts need to carefully identify the correct position had the warranties been true, guided by the relevant legal instructions, the underlying deal and market circumstances at the date of the SPA.

As explained above, under civil law, the assessment of damages arising from warranty claims is broadly similar to common law, except that, under civil law, the value had the warranties been true is typically inferred from the price paid.

In the following subsections, we discuss the impact of the date of assessment on projections of the claimant's financial position in the counterfactual and actual scenarios. We also consider how the date adopted may impact discounting and the application of interest. Finally, we present a case study to explain how the date of assessment plays an important role in assessing damages.

THE CLAIMANT'S FINANCIAL POSITION IN THE COUNTERFACTUAL SCENARIO

The counterfactual scenario reflects the financial position that the claimant would have been in absent the alleged breach. In this scenario, the expert is required to make explicit assumptions about growth and risk in a scenario that does not, and will not, exist. The expert may also be required to project the claimant's financial position a long way into the future, which causes additional uncertainty.

Where the expert adopts the date of breach as the date of assessment, the expert should only consider information known or foreseeable as at the date of assessment without using hindsight. This principle is consistent with the judgment in the ***Classic Maritime*** Inc case.

However, this results in practical challenges for the expert that do not exist when adopting the date of award as the date of assessment. For example, if a substantial amount of time has passed since the date of breach, it may be hard to determine what information was known or foreseeable as at the date of breach. The passage of time may also highlight differences between expectations at the date of breach and information that became known after this date.

In such damages assessments, an expert may, for example, refer to contemporaneous forecasts of cash flows to estimate the claimant's financial position. However, the expert should ensure that these forecasts only reflect expectations as at the date of breach and have not been updated afterwards to reflect actual performance, which involves hindsight information.

This position is further complicated where external factors may impact the underlying business after the date of breach. In recent years, such events include the outbreak of the covid-19 pandemic and the ongoing Russia–Ukraine conflict. Recent rapid growth in inflation and interest rates also impact expectations. These events may result in material changes to future expectations.

In contrast, where the expert adopts the date of award as the date of assessment, the expert may consider all information known at that point including such events that only came into existence after the date of breach. The impact of these events on future expectations beyond the date of assessment, and therefore the date of award, should also be considered.

When projecting the claimant's financial position in the counterfactual scenario, experts need to ensure that the information to which they refer is in keeping with the relevant legal principles described above. Where hindsight is not allowed, it is important that the counterfactual scenario reflects only information that is known or foreseeable as at the date of assessment. However, as explained above, there are limited circumstances where, under common law, hindsight may be considered in the assessment of damages.

THE CLAIMANT'S FINANCIAL POSITION IN THE ACTUAL SCENARIO

The actual scenario reflects the financial position of the claimant, taking into consideration the impact of the alleged breach. In this scenario, the expert may still need to consider future expectations for the claimant's financial position after the breach. However, where the breach results in a complete cessation of activity, the claimant's financial position in the actual scenario may be nil, as no further cash will be earned, or may even be negative, to reflect that the claimant may need to incur costs following the breach.

When assessing damages at the date of breach, experts are likely to have access to information concerning the real-world financial position of the claimant following the date of breach. Due to this, experts often adopt the claimant's real-world financial position as a proxy to determine its financial position in the actual scenario.

When doing so, experts need to consider whether such an approach creates an inconsistency between the information used in the counterfactual scenario and in the actual scenario. In instances where there have been material changes in the economic and business environment following the date of the alleged breach (such as a date of breach followed by the covid-19 pandemic), the financial position in one scenario may reflect factors that are not captured in the other. This may result in the assessment of damages capturing the impact of these factors, which are not attributable to the alleged breach.

Experts should also consider whether the claimant's real-world financial position includes attempts to mitigate loss (such as rationalising headcount that is surplus to requirement or selling assets that have become redundant). If it does not, some form of adjustment may be required.

In the past few years, global economic events have resulted in rapid changes in the economic environment. As disputes with a date of assessment in this period crystallise, it will be important for experts to explain how they project the claimant's financial position in the actual scenario and the extent to which this is done by reference to the claimant's real-world financial position following the date of breach.

DISCOUNTING AND THE APPLICATION OF INTEREST

One approach used to assess damages is a discounted cash flow (DCF) model. In a DCF model, the expert projects future cash flows for an asset or contract and then converts them into a single lump sum amount at the relevant date of assessment by applying a discount rate.

The discount rate reflects two factors. The first is the time value of money, or that a dollar today is worth more than a dollar in one year as it can be invested and earn a return in the interim. The second is that there is no guarantee that a party will actually receive the amount of money that they project. They may receive more or less than the projected amount (or none at all) and they may receive it earlier or later than they project. This uncertainty is reflected in the discount rate.

When using the date of breach as the date of assessment, projected cash flows in the counterfactual and actual scenarios are discounted to arrive at a single lump sum amount at the date of breach. Pre-judgment interest is then applied to this lump sum amount to state the damages in present terms at the date of the award.

When the date of award is adopted as the date of assessment, interest is applied to all cash flows that were impacted as a result of the breach, or would have been impacted, prior to this date of award to state them in present terms. All future cash flows are discounted to a lump sum amount at this date.

The cost of equity, or the return that investors require to provide equity capital for an investment, or to a company, is one of the key components of the discount rate. One common model used to estimate the cost of equity is the capital asset pricing model (CAPM).[6] This has three inputs:

- a risk-free rate, which reflects the return an investor could earn on a risk-free security, such as a government treasury instrument;
- the equity risk premium, which reflects the return required by investors to invest in equities as opposed to risk-free instruments; and
- beta, which reflects the risk of a particular sector or industry relative to the market as a whole.[7]

The input for the CAPM changes on a daily basis to reflect various economic and market factors, including, inter alia, movements in the yields on risk-free instruments, expectations as to the returns on equities and movements in the prices of listed shares. Changes in inflation and interest rates also impact the calculation of the discount rate. Similarly, interest rates used to calculate prejudgment interest may be based on prevailing lending rates. These also change over time to reflect market conditions.

Due to this, moving the date of assessment can result in changes to the discount rate or the interest rate, and consequently changes to an expert's assessment of damages. To illustrate this, we provide a simple example where the date of breach is in January 2020 and the date of assessment is in January 2023.

At the date of breach in a hypothetical dispute, the risk-free rate is 1 per cent, the equity risk premium is 6 per cent and the appropriate beta to apply for the claimant is 1. This results in a cost of equity of 7 per cent.[8] However, at the date of assessment these inputs have changed to reflect prevailing market conditions. The risk-free rate is now 3 per cent, the equity risk premium remains at 6 per cent and the appropriate beta to apply remains at 1. The cost of equity is now 9 per cent.[9] This reflects a nearly 30 per cent increase in the cost of equity. All being equal, this results in a lower assessment of damages at the date of assessment, as a higher discount rate results in a lower lump sum amount.

The date of assessment impacts both the chosen discount rate and the interest rate used in an assessment of damages. Changes to these inputs can have material consequences. Experts should be aware of such differences and be able to explain how changing the date of assessment may impact their chosen discount rate and interest rate.

HYPOTHETICAL EXAMPLE OF HOW THE DATE OF ASSESSMENT IMPACTS THE INFORMATION THAT CAN BE CONSIDERED BY AN EXPERT

For illustrative purposes, the following example provides a highly simplified description of how changing the date of assessment may impact an assessment of damages in a given hypothetical scenario. This example focuses only on one aspect of the damages calculation, namely, the revenue that the claimant has been deprived of as a result of the alleged breach. This example does not consider other variables or underlying factors such as costs, other cash outflows or categories of loss that may arise and would normally be considered in the assessment of damages.

In this hypothetical scenario, Company A and Company B entered into a contract in which Company B agreed to provide a certain volume of gas to Company A each year at a price consistent with market rates. This contract was agreed in 2013, with a term of 20 years. In breach of its contractual obligations, Company B never provided any gas to Company A. Company A commenced legal proceedings against Company B, seeking compensation for this breach. The date of the award has been set for 2023.

As explained above, the expert will compare Company A’s financial position in the counterfactual scenario and the actual scenario. As no gas has been supplied or will be supplied, the expert can assume that in the actual scenario, Company A earned no revenue. The relevant question for the expert is therefore how to assess Company A’s financial position in the counterfactual scenario. The date of assessment will impact the approach that an expert adopts, and the information they may consider.

Using the date of breach as the date of assessment, the expert should typically disregard hindsight information. The expert therefore needs to project gas prices for a 20-year period from 2013 and calculate the discount rate associated with the expected revenue from the sale of gas, in 2013. In this hypothetical example, in 2013, the projected price of gas in 2023 was around US$3 per million British thermal units.

In contrast, where the date of award is used as the date of assessment, the expert may be entitled to consider facts that became known after the date of the breach. This means that revenue for the period 2013 to 2023 could be informed by actual gas prices in this period. The expert could adopt actual prices, as opposed to the projected price in 2013 (ie, US$3 per million British thermal units). In this hypothetical example, the projected gas price at the date of award was around US$6 per million British thermal units, as compared to the projected price of US$3 per million British thermal units in 2013, which results in higher revenue in this period.

Furthermore, the expert may project future gas prices from 2023 onwards by reference to contemporaneous projections and events that would inform the price of gas. In this hypothetical example, the expert could refer to the projected gas price of around US$6 per million British thermal units in its assessment of projected revenue for the period 2023 to 2033. This would result in higher revenue projections, as compared to if projections at the date of breach (of US$3 per million British thermal units) were adopted.

In practice, an assessment of damages involves a detailed assessment of the claimant's financial position in both the counterfactual and actual scenarios. This assessment is informed by detailed financial analysis and available data, and refers to the relevant applicable legal principles.

However, as this simplified hypothetical example shows, the information available to the expert, which informs their analysis, may differ depending on the date of assessment. The difference in information may also have material consequences.

CONCLUSION

As this article shows, the date of assessment is a relevant consideration in assessing damages, and determines the information that the expert can consider. Under both common law and civil law, there are well-developed frameworks for determining the date of assessment.

In common law, the general rule is that damages are to be assessed at the date of breach. However, there are limited circumstances where hindsight information may be considered, for example, in the case of anticipatory breach.

In civil law, the general rule is that, in the case of variable damages, assessment is made at the date of the award. However, where the damage is invariable, the general rule is that damages are assessed on the date that the damage was suffered.

From a damages assessment perspective, hindsight information should typically be disregarded. This means that, when a date of breach is adopted as the assessment date, information that became known after this date should be disregarded. However, where the date of award is adopted, experts may be entitled to adopt all information known at the date of assessment to inform their calculations. This difference in approach changes the information that can be relied upon and the conclusions that experts will arrive at.

* *This information is provided for informational purposes only and nothing in this article should be construed as legal advice. The examples provided throughout are simplified to illustrate the points under discussion and therefore they do not represent the actual practice.*

Endnotes

1 See articles 292 and 389 of the UAE Civil Code; article 170 of the Egyptian Civil Code;- *Al-Waseet in Explaining the Civil Law (al-Wasīṭ fī Sharḥ al-Qānūn al-Madanī al-Jadīd)*, Vol. 1/1 (Beirut: Al-Halabi Legal Publications, 2011), paragraph 648, p. 1098; and Dubai Court of Cassation Judgment No. 246/2022 Civil. ^ Back to section

2 Dubai Court of Cassation Judgment No. 457/2017 Civil. ^ Back to section

3 Dubai Court of Cassation Judgment No. 111/2017 Civil. ^ Back to section

4 *Al-Waseet in Explaining the Civil Law (al-Wasī fī Shar al-Qānūn al-Madanī al-Jadīd)*, Vol. 1/1 (Beirut: Al-Halabi Legal Publications, 2011), paragraph 649, p. 1102. ^ Back to section

5 Experts make assumptions about future growth and risk either explicitly through inputs into a discounted cash flow (DCF) model when preparing cash flow forecasts or by their choice of financial ratio, or multiple ratios, when preparing a multiples analysis. ^ Back to section

6 The capital asset pricing model calculates the cost of equity as: the risk free rate plus the equity risk premium multiplied by the beta. ^ Back to section

7 Beta can generally be thought of as a measure of how much the share price of a company moves as compared to the market as a whole. For example, if a company has a beta of 1.5, it means that when the market moves by 1.0 per cent (either up or down), the share price will move in the same direction by 1.5 per cent. A beta of greater than 1 suggests that a company is more volatile than the market as a whole, and a beta of less than 1 suggests that it is less volatile. ^ Back to section

8 Calculated as 1 per cent + 6 per cent x 1. ^ Back to section

9 Calculated as 3 per cent + 6 per cent x 1. ^ Back to section

FTI CONSULTING

200 Aldersgate,Aldersgate Street,London EC1A 4HD,United Kingdom

Tel: +44 20 3727 1000

https://www.fticonsulting.com/

K&L GATES

599 Lexington Avenue,New York, NY 10022,United States

Tel: +1 212 536 4065

http://www.klgates.com

Read more from this firm on GAR