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Arbitration Decision
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February 15, 2017

CASE NUMBER 2737

PLAINTIFF: **POET NUTRITION, INC.**
SIOUX FALLS, SD

DEFENDANT: **AFEC COMMODITIES (SERVICES AND SOLUTIONS), INC.**
PHOENIX, AZ

STATEMENT OF THE CASE

This dispute is about nonperformance on six contracts to purchase Dakota Gold™ Distillers Dried Grains with Solubles (DDGS). On March 3, 2014, AFEC Commodities, Inc. (AFEC) executed a total of nine contracts with POET Nutrition, Inc. (POET) to purchase 59,000 metric tons of DDGS at $278 per ton delivered to Midwest Bulk Transport in Joliet, IL. The nine contracts corresponded to separate monthly shipment periods in 2014 (for the months of March, April, May, June, July, August, October, November and December).

During the course of discussions between the parties surrounding this trade, AFEC disclosed and POET was made aware that the DDGS were destined for export to China. POET made known it wanted the DDGS identified by the brand name "Dakota Gold" and not commoditized or commingled with another brand. The parties discussed issues arising out of detection in shipments of U.S. corn and distillers grains of MIR162 (a biotechnology-enhanced trait not yet approved by the Chinese government) and AFEC's plans to handle the import process. Prior to execution of the trade, POET made known its interests in having AFEC sell the DDGS for shipment to China.

The parties performed on the first two contracts without dispute. In April 2014, the parties agreed to washout certain tonnages on four of the remaining contracts. On April 21, amendments to those four contracts were exchanged between the parties and confirmed in writing, which resulted in the washout of 5,000 tons under each of the May, June, July and August contracts. The washout for the May contract resulted in credit due to AFEC of $5 per ton. The washout for the June contract resulted in credit due to AFEC of $2 per ton. The washouts for the July and August contracts were "at no charge." The May contract had a remaining balance of 2,000 tons, which POET shipped and AFEC accepted.

As of June 2014, the following six contracts remained open and are the subject of this case:

Contract Number	Tons	Shipment Period
70048265-001	4,000	June 2014
70048266-001	5,000	July 2014
70048267-001	5,000	August 2014
70048269-001	5,000	October 2014
70048271-001	5,000	November 2014
70048272-001	5,000	December 2014

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On June 9, 2014, POET made inquiries to AFEC arising out of reports that China had stopped issuing import permits for DDGS from the U.S. POET also inquired when AFEC would begin taking delivery under the June contract. In response, AFEC acknowledged the issues with exports to China and advised it was looking for solutions. AFEC then stated "but for the time being we have to play this safe and stop taking delivery." POET responded that it had to keep the product moving because of production and storage issues.

On June 16, AFEC notified POET that it was claiming *force majeure* on the June contract. AFEC also at that time stated: *"confirm you prefer doing this on a month to month basis. I prefer to maintain the contracts in force at the contractual price but roll back until the China DDGS markets open up while paying a compensation for such arrangement."*

On June 25, during a telephone conversation between the parties, which POET confirmed by e-mail to AFEC, AFEC made clear it was claiming *force majeure* on all six open contracts and it had no intentions of accepting delivery under the June contract. POET responded by letter to AFEC on June 26, stating that according to POET the contracts remained open and POET was summarily rejecting AFEC's claim of *force majeure*. POET also noted that the contracts terms contained no GMO-related guarantees. POET further stated that unless AFEC proposed an agreeable solution by July 3, POET would refer the matter to NGFA Arbitration.

On July 1, POET again notified AFEC by e-mail that POET would apply NGFA Feed Trade Rule 19(B)(3) by cancelling the defaulted portion of the shipments at the fair market value on the close of business on July 3. POET ultimately closed the June contract on July 3, and calculated its damages using a third-party market price for distillers delivered by truck in Illinois, plus various fees and transload charges. POET subsequently filed its first arbitration complaint against AFEC with NGFA for $362,156.92 in damages arising from default of the June default.

On July 21, POET cancelled the July contract and calculated its damages using the same methodology for establishing fair market value that it had applied for the June contract. On August 18, POET cancelled the August contract and assessed damages using the same method again. Also on August 18, POET similarly closed and assessed damages for the October, November and December contracts after determining that AFEC had no intention to accept shipments under those contracts.

On August 29, AFEC filed a lawsuit in Houston, TX, asking the court to declare that AFEC's failure to perform on the contracts was excused based upon *force majeure*. The court dismissed the case and ordered the parties to NGFA Arbitration. On September 5, POET filed a second and third arbitration complaint with NGFA against AFEC for default of the July contract in the amount of $404,500; and default of the August, October, November and December contracts in the amount of $2,058,900.

POET is claiming damages against AFEC for non-performance of the six contracts of DDGS for June through December of 2014. According to POET, the quantities under these contracts totaled 29,000 metric tons and POET's losses amounted to $2,825,551.

AFEC's defense throughout this dispute has been that the import restrictions imposed by the Chinese government were responsible for AFEC's inability to perform under the contracts. AFEC argues that these actions by the Chinese government entitle AFEC to assert *force majeure* as a defense to excuse it from performing on the contracts. AFEC also asserts the related legal defenses of "commercial frustration" and "commercial impracticability" pursuant to South Dakota state law. The arbitrators noted that the contracts stipulated that South Dakota law would govern the contract as well as the NGFA Trade Rules and NGFA Arbitration. AFEC further argues that it was restricted by POET to only supplying the DDGS to China under the contracts. AFEC also claimed in its defense that POET failed to properly apply NGFA Feed Trade Rule 19(B)(3) when it provided notice to AFEC that it was determining the contracts to be in default.

AFEC further asserted a counter-claim against POET for monies that AFEC claimed were wrongfully withheld by POET. These claimed damages consisted of $349,012.09 that AFEC stated it was required to pay in advance for execution of the contracts in 2014; and $100,381.23 attributed to "shrink" related to shipments in 2013.

THE DECISION

The arbitrators closely reviewed and deliberated concerning the extensive arguments and materials provided by the parties in this case. Also, an oral hearing was conducted in this case at the request of AFEC pursuant to Rule 8 of the NGFA Arbitration Rules. During the hearing the parties thoroughly presented their positions to the arbitrators with oral argument and witness testimony.

The arbitrators concluded that the four corners of the contracts, as laid out by NGFA Feed Trade Rule 1, clearly defined the relevant points of this trade between the parties. Any other conditions, guarantees or other understandings or considerations that either party had an interest in incorporating as a component of the trade (such as the availability of the Chinese market) should have been written into the contracts. Otherwise, they risked not be enforceable in many situations.

The arbitrators considered AFEC's claim that it was required by POET to ship the DDGS under the contracts only to China or face some penalty from POET. POET had made known its interests before the trade in having AFEC sell the DDGS for shipment to China. However, the arbitrators determined that AFEC failed to prove that this presented a valid defense in this case or even that in the end POET was imposing any such requirements or penalties related to the resale of the DDGS.

With respect to the parties' arguments concerning *force majeure*, the arbitrators noted that the contracts contained a "Force Majeure" clause that stated "POET will not be liable for any failure or delay" in its shipment or performance under the contract due to "law, act of government, prohibition to export," etc. The contracts did not correspondingly provide a basis for *force majeure* as a defense against non-performance by AFEC. The arbitrators further considered other defenses under South Dakota law that AFEC claimed would similarly excuse it from executing on these contracts – "commercial frustration" and "commercial impracticability." Based upon a close review of the extensive legal argument presented by both parties on these defenses, the arbitrators concluded that AFEC failed to meet its burden to have these defenses apply in these circumstances. The shipment required under the express terms of the contracts was to take place in the city of Joliet, IL. There was no indication in the contracts that AFEC's performance under the contracts was dependent upon policies of the Chinese government. The arbitrators determined that AFEC had accepted the risk of this action by the Chinese government in this trade. Indeed, it appeared that the parties were aware – or should have been aware – of at least the potential risks arising out of import restrictions imposed by the Chinese government. AFEC was accountable for management and control of those risks under the contracts. The policy imposed by the

Chinese government did not negate the express purpose of these contracts or otherwise excuse AFEC's performance under the contracts.

AFEC also argues that NGFA Feed Trade Rule 5 [Electronic Communication] applies in this case in support of its defense for non-performance on these contracts. AFEC's argument is that all the e-mails between the parties serve as a basis for the trade, whether those e-mails were exchanged before or after the contract was made. The arbitrators noted that Rule 5 does provide for contracting parties to agree to terms or changes to contracts by electronic means "in lieu of paper-based documents" in some situations. The arbitrators concluded, however, that e-mails between the parties did not serve to replace or amend the expressly stated and agreed upon terms of the written and executed contracts in this case. AFEC further claims that certain agreements in a previous trade would carry over to the 2014 contracts in this dispute. For such changes to apply, however, the arbitrators concluded that they should have been written into the contracts with the express consent of both parties.

The arbitrators noted that AFEC did not present any argument or evidence related to the amount of damages to which POET would be potentially entitled if an award were issued in its favor. The arbitrators had only POET's calculations of damages to consider. However, through testimony and examination at the oral hearing the arbitrators were able to more closely evaluate the damages that applied in this case. Damages were calculated by POET in this case using a third party market reporting service, McDonald Pelz Global Commodities LLC. POET's assessment of damages was based upon a Channahon/Elwood, Illinois (truck delivered) mid-point between bid and offer prices on the date of default, plus additional charges ($16 per ton transload fee; 11-cents per ton phytosanitary charge; 78-cents per ton chassis fee). POET's total claimed damages were based upon the following calculations:

Date of default determined by POET	Contract	Cost/Tonnage	Damages
7/03/2014	June contract	$72.08/MT x 4,000	$ 288,320
	(additional trucking, transload and interest charges)		$ 73,831.92
7/21/2014	July contract	$80.90/MT x 5,000	$ 404,500
8/18/2014	August contract	$109.56/MT x 5,000	$ 547,800
8/18/2014	October contract	$100.74/MT x 5,000	$ 503,700
8//18/2014	November contract	$100.74/MT x 5,000	$ 503,700
8/18/2014	December contract	$100.74/MT x 5,000	$ 503,700
			$2,825,551.92

The arbitrators rejected POET's claims related to the June contract for additional interest, transload and trucking fees because these charges were not sufficiently explained or proven.

The arbitrators also agreed with AFEC that POET did not correctly apply NGFA Feed Trade Rule 19(B)(3) when POET was provided with the notice of default pertaining to all the contracts on June 25, 2014. The evidence showed that as of June 25, AFEC had changed its position on all contracts in place and had no intentions of executing on the balance of any contracts. This position was different from AFEC's position on June 16. The arbitrators determined that market prices continued to decrease from the time POET was provided with the notice of default until it ultimately fixed its damages. AFEC was entitled to have damages fixed as of the day POET provided notice that it intended to cancel the contracts as the result of AFEC's default. POET had the obligation to fix the damages as of June 25.

POET elected to proceed under NGFA Feed Trade Rule 19(B)(3) and had an obligation to act on all tonnage and contracts as of this day of notification. POET did not have the option to wait until July and August to fix damages on the contracts for July, August, October, November, and December.

AFEC did not provide market prices in reference to June 25, 2014 as the applicable cancellation date. The most relevant pricing information available to the arbitrators was provided by POET for July 3, 2014. Based on this information, the arbitrators adjusted the damages due to POET.

The arbitrators further noted that as is the custom of the trade, contracts are written with specific reference to a base point. If changes to the destination are subsequently necessary, then adjustments are made to this base point. There may also be additional rail, truck or transfer costs. In this case, the contracts provided for transloading from trucks to containers. To accomplish this, POET entered into a contract with a third-party provider. The arbitrators closely examined the impact of this component of POET's claimed damages during the witnesses' testimony presented at the oral hearing conducted in this matter. The evidence indicated that POET's agreement with the third-party transloader required that minimum tonnages move through the transfer site. An $8 per ton charge applied if POET failed to meet that minimum. After the export market collapsed, it became apparent that any DDGS shipped would move domestically and that paying the $8 per ton penalty charge would be more economical than forcing the loading of containers. POET included a $16 per ton transloading fee in its calculations of damages. The arbitrators, therefore, reduced the damages due from AFEC in the amount of $8 per ton for the defaulted portions of the July, August, October, November and December contracts (or 25,000 metric tons).

With regard to the claims in AFEC's counterclaim, the arbitrators noted that POET in its arguments acknowledged that its damages should be reduced by the amount prepaid by AFEC of $349,012.09. The arbitrators further concluded that AFEC's claim for the *shrink*-related charges of $100,381.25 was also valid.

Therefore, the arbitrators determined that AFEC pay monetary damages to POET as set forth below.

Date of default calculated by the arbitrators	Contract	Cost/Tonnage	Damages
7/3/2014	June contract	$72.08/MT x 4000	$ 288,320
7/3/2014	July contract	$72.08/MT x 5000	$ 360,400
7/3/2014	August contract	$74.84/MT x 5000	$ 374,200
7/3/2014	October contract	$76.49/MT x 5000	$ 382,450
7/3/2014	November contract	$76.49/MT x 5000	$ 382,450
7/3/2014	December contract	$76.49/MT x 5000	$ 382,450
			$2,170,270

Transload Adjustment	<$200,000.00>
Pre-paid Dollars	<$349,012.09>
Shrink Charges from Previous Contract	<$100,381.25>
Damages due from AFEC to POET	$1,520,876.80

Further, the arbitrators determined that neither party was as diligent as it could have been in mitigating damages or working toward alternatives and possible solutions after the issues arose with the Chinese market. Thus, the arbitrators declined to award any interest to POET or lawyers' fees in this case to either party.

THE AWARD

The arbitrators awarded $1,520,876.80 in damages to POET from AFEC.

Decided: December 2, 2016

SUBMITTED WITH THE UNANIMOUS CONSENT OF THE ARBITRATORS, WHOSE NAMES APPEAR BELOW:

Mike Meyers, *Chair*
Director of Wheat By-Products
APEX LLC
Hamburg, NY

Edmund Hall
President
Harris-Crane Inc.
Charlotte, NC

John Augspurger
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