2. THE JOINT VENTURE AGREEMENT

2.1 Negotiations

Articles

Farnsworth E.A. "Pre-contractual Liability and Preliminary Agreements: Fair Dealing and Failed Negotiations" (1987) 87 *Columbia Law Review* 217

According to Farnsworth, contractual negotiations in the United States are covered by existing contractual doctrines. Where negotiations succeed in producing a contract, then the negotiations may be covered by the doctrines of misrepresentation, duress, undue influence, or unconscionability, but where negotiations fail, the law traditionally offers little if any recourse to aggrieved parties. Farnsworth notes however, that US courts are now beginning to impose pre-contractual liability for *unjust enrichment* resulting from negotiations. Under this action, damage is measured according to rules of restitution, that consider the value of the benefit the defendant has received, which can include the value of property received or of any services rendered by the plaintiff. The plaintiff must prove the defendant had gained an actual benefit. US law is also beginning to recognise '*misrepresentations'* and '*specific promises'* made during negotiations. The measure of damages for these actions is based on the injured party's reliance interest, that is, the party in the wrong is liable for loss caused by reliance on the misrepresentation, promise, or undertaking. The measure of damages will depend on which ground the action is brought under, and what is considered to be lost due to reliance.

The US courts do not recognise a '*general obligation'* arising out of negotiations themselves, as the general duty of good faith implied by the *Uniform Commercial Code* and the duty of good faith and fair dealing contained in the *Restatement (Second) of Contracts*, do not extend such duties to pre-contractual negotiations. It is noted however, that in some civil law counties, including Argentina, Israel, Germany and France, a duty of good faith (or a duty not to act in bad faith) is imposed on contractual negotiations.

A '*duty of fair dealing'* does not extend to pre-contractual situations. However, where an agreement to agree has been concluded (and no later contract is formed) the unfairness in the *'duty of fair dealing'* will revolve around the means used to obstruct the agreement. The substance of what a court will consider to be unfair, is far from certain.

Sharwood M. "Joint Venture Agreements: Transition from Informality to Formality" [1988] *Australian Mining and Petroleum Law Association Yearbook* 1

A comprehensive and practical paper covering issues of particular relevance to mining and petroleum joint ventures in the time leading up to a final contract. Sharwood begins by examining Heads of Agreement ("HOA") and Letters of Intent ("LOI") pointing out that the difference in terminology between a LOI and HOA is legally insignificant. What is important is that the parties intentions are made clear as to whether and to what extent they intend to be bound by the document. If parties do not intend to be bound, Sharwood advocates using the precise words contained in *Masters v Cameron* rather than simply relying on "subject to contract".

Inadvertent agreements and oral agreements are considered. Sharwood discusses particular problems arising under mineral and petroleum statutes, in relation to the creation of interests in petroleum titles. He warns that the requirements for Ministerial approval or registration for a transaction involving mineral interests (the "*of no force*" provisions) can often be overlooked during initial stages of exploration negotiations, and can render agreements either unenforceable or even invalid. Sharwood then covers in detail, the legal and practical issues in connection with formal preliminary agreements such as bidding agreements and Area of Mutual Interest ("AMI") agreements, and the legal difficulties faced by intending corporate participants when entering contracts prior to incorporation.

The latter part of Sharwood's paper considers what fiduciary obligations may exist between parties prior to entering a contract and argues that the ultimate determinant of whether fiduciary duties are owed by persons negotiating a joint venture is the nature and degree of the relationship of confidence. Sharwood points out that parties should be aware of rights and duties arising not only through express provisions, but imposed under general law, which may be of particular concern where confidential information is disclosed in the course of negotiations.

Sharwood concludes with practical advice regarding pre-joint venture agreements and provides a list of essential matters which ought to be included in any preliminary agreements. Particular attention is drawn to setting out clearly the extent to which the agreement is intended to be binding according to *Masters v Cameron*, and where an "entire agreement" clause is being utilised, that the clause either refers expressly to antecedent agreements and terminates them, or expressly incorporate them in to the current agreement, to avoid inconsistencies.

Cases:
Masters v Cameron (1954) 91 CLR 353
LAC Minerals Ltd v. International Corona Resources Ltd (1989) 61 DLR (4th) 14

Ahrens M.C. "Negotiating the Joint Venture" in Part 1 of *Joint Ventures*, Papers delivered at a workshop held April 1990, Business Law Education Centre, April 1990

The first part of Ahrens' article provides a concise overview of the factors to consider in selecting a joint venture partner, and a list of legal principles (with supporting case authority) relevant to determining whether a preliminary agreement will be considered by a court, to be binding and enforceable. Ahrens discusses the fiduciary duties owed between prospective venturers during negotiations and warns that safeguards should be put in place early in the negotiations, if sensitive information is to be received or transmitted.

Cases:
LAC Minerals Ltd v. International Corona Resources Ltd (1989) 61 DLR (4th) 14
Noranda Australia Ltd v Lachlan Resources NL (1988) 14 NSWLR 1

Bagot C.N.H. "Comment on Joint Venture Agreements: Transition from Informality to Formality" [1988] ***Australian Mining and Petroleum Law Association Yearbook*** **32**

In commenting on Michael Sharwood's paper, Bagot discusses the application of *Walton Stores (Interstate) Ltd v Maher* in which the High Court enforced a voluntary promise to enter a deal on terms contained in a document which had been exchanged, despite no binding agreement having come into existence. He points out that where a Letter Of Intent or Heads Of Agreement is intended to be binding, problems may arise in enforcing the agreement if important terms are omitted. The problems of joint venture agreements being rendered unenforceable or void under the peculiarities of statutory regimes for mining and petroleum tenements is highlighted. Brief comment is offered as to remedies in the event a proposed joint venture does not eventually proceed.

Cases:
Walton Stores (Interstate) Ltd v Maher (1988) 164 CLR 387

Ahrens M.C. "Negotiating the Joint Venture" Paper presented at BLEC Seminar in May 1998, ***Annual Joint Ventures Seminar*****, Business Law Education Centre, Sydney, 2000**

Ahrens provides a general overview of types of heads of agreement (HOA) and discusses whether HOAs are binding. After examining the case of *Coal Cliff Collieries Pty Ltd v Sijehama Pty Ltd* in which the court enunciated the factors relevant to determining whether a HOA is binding, Ahrens argues that since that case, Australian courts appear more likely to find a HOA binding, particularly where parties act as if a binding agreement exists. A court will look at the entire factual matrix to find the objective intention of the parties, having regard to the magnitude, subject matter and complexity of the transaction. Provided the HOA covers all material terms, the court will strive to give effect to the intention of the parties. Ahrens observes that drafting documents to fit the appropriate *Masters v Cameron* categories can be awkward, and he sets out practical steps that can be taken to create a binding HOA. Ahrens briefly discusses other non-contractual remedies based on unjust enrichment, breach of fiduciary duty or equitable estoppel, that may be available where the HOA is not binding.

The second part of Ahrens' paper lists and briefly describes the essential factors that should be included in a joint venture agreement, and the types of deadlock breaking mechanism available, including majority vote, sole risk, independent "swing man", senior executive meetings, event options, compulsory buy/sell provisions, auction systems, arbitration and mediation.

Cases:
Travel World Services Pty Ltd v Rose Brisbrook Pty Ltd Unreported, 22 September 1995, Supreme Court of Victoria
Toyota Motor Corporation Australia Ltd v Ken Morgan Motors Pty Ltd [1994] 2 VR 108, Supreme Court of Victoria
Coal Cliff Collieries Pty Ltd v Sijehama Pty Ltd (1991) 24 NSWLR 1

Gardner A. "Aspects of Joint Ventures—Fiduciary obligations of parties negotiating for a joint venture" Paper presented at *Second Annual Australian Mining and Petroleum Law Association (WA Branch) State Conference*, Scarborough, Perth, 22 October 1988.

Gardner draws together the various propositions of the principal legal authors and case law, to provide a very useful and clear paper regarding fiduciary obligations in the context of negotiating mining or petroleum joint ventures. He argues that the existence or not, of fiduciary obligations will depend on the underlying character of the particular relationship, rather than on the existence of an identifiable legal category of relationship, and that this test of underlying character will be the same for both an established joint venture or where parties are negotiating a joint venture. His paper discusses (i) why fiduciary obligations and remedies for their breach are important to joint venture parties; (ii) how fiduciary obligations can arise in respect of joint venturers and parties negotiating a joint venture; (iii) what types of fiduciary obligations negotiating parties should consider (conflict of duty and interest, and duty of confidence) and the scope and legal principles applicable; (iv) measures that can be taken by parties negotiating for a joint venture and industry associations to clarify industry practice; and (v) problems with the *Mining Act* 1978 (WA) in terms of the procedures and remedies available where there has been a breach of fiduciary obligations.

Legislation:
Mining Act 1978 (WA)

Cases:
LAC Minerals Ltd v International Corona Resources Ltd (1988) 44 DLR (4th) 592

Books

Fisher S. "Negotiating Joint Ventures" in W.D. Duncan (ed), *Joint Venture Law in Australia*, The Federation Press, Sydney, 1994, Chapter 4

Fisher briefly sets out the role and use of Letters of Intent ("LOI") and Heads of Agreement ("HOA") as preliminary agreements to a final contract. This is followed by an extensive discussion of the principles of equitable estoppel, and its application to negotiation of joint ventures. These principles will be relevant in situations where one party has encouraged a second party to believe a contract will come into existence and the second party suffers some loss as a result of relying on that promise.

Fisher then discusses the application of principles of good faith under Australian law, and concludes that there is no generally recognised duty for parties to negotiate in good faith. However, it may be possible that parties voluntarily assume a duty to act in good faith, by virtue of having entered into a contractual relationship. An "agreement to agree" may give rise to such a relationship, however, Australian courts have not generally recognised these agreements. Similarly, a contractual clause containing an agreement to negotiate in good faith has not found unanimous favour with Australian courts. Fisher examines the case of *Coal Cliff Collieries Pty Ltd v Sijehama Pty Ltd* in which a clause promising "to proceed in good faith" had been included in a HOA. Australian courts have declined to enforce such a clause as contractually binding, however this may depend on the construction of the particular agreement.

Fisher also covers the use of contractual terms which restrict a party's capacity to exercise rights only "on reasonable grounds" or to use its "best endeavours" to achieve particular results. After considering the case of *Noranda Australia Ltd v Lachlan Resources NL,* Fisher considers that a court will look objectively at all the circumstances in determining whether a party has acted "reasonably" or with "best endeavours" under the contract. In concluding, Fisher advises that in circumstances where there will be disclosure of sensitive information in the course of negotiations, a confidentially agreement should be used, to protect against unauthorised disclosure through both a contractual remedy and though breach of confidence.

Cases:
Masters v Cameron (1954) 91 CLR 353
Commonwealth v Verwayen (1990) 179 CLR 394
Walton Stores (Interstate) Ltd v Maher (1988) 164 CLR 387
Noranda Australia Ltd v Lachlan Resources NL (1988) 14 NSWLR 1
Coal Cliff Collieries Pty Ltd v Sijehama Pty Ltd (1991) 24 NSWLR 1

Bradley D. "Disputes Arising From Failure to Complete Initial Joint Ventures Negotiations" in *The Rights and Duties of Joint Venturers in Tough Times*, Papers delivered at a 2-day Master Class, Business Law Education Centre, Melbourne, November 1990, Part 1

Bradley examines in comprehensive detail, whether and to what extent prospective parties to an unincorporated joint venture are bound by the terms of their negotiations, and in what circumstances equitable obligations may be imposed on the pre-contractual dealings between the parties *inter se*. He discusses whether parties may be bound in law or equity, in the typical pre-contractual situations: (i) where parties not intending to be bound are nevertheless bound by their conduct or representations; (ii) where parties intending to be bound may not be bound due to statute (or otherwise): and (iii) where parties have failed to turn their minds as to whether they intend to be bound, and will be subject to the test in *Masters v Cameron*. An overview of the remedies available for breach of pre-incorporation contracts is considered.

In the second part of the paper, Bradley discusses the statutory and equitable remedies available to an aggrieved party, whether or not a binding enforceable agreement is formed. The tests as to the existence of a fiduciary duty are considered in detail through the judgments in *Hospital Products Ltd v. United States Surgical Corporation* (*Hospital Products*) and *United Dominions Corp Ltd v. Brian Pty Ltd.* the latter showing fiduciary obligations may arise in a pre-contractual situation. The case of *Noranda Australia Ltd v Lachlan Resources NL* is discussed as important for the emphasis place on express contractual terms to limit fiduciary obligations in a non-partnership joint venture. Bradley argues that where the "interest" test proposed by Gibbs J. in *Hospital Products* is applied, a fiduciary obligation can arise in pre-contractual situations.

The final part of Bradley's paper gives an overview of the situation in which confidential information is disclosed during negotiations, giving rise to a duty of confidentiality. Other remedies available to prospective joint venturers, including unconscionability, good faith and misrepresentation, are considered. Bradley makes the following conclusions:

(i) joint venturers who do not wish to be bound by pre-contractual agreements, should make this intention clear in documentation;

(ii) fiduciary obligations may be restricted by express contractual stipulation regarding extent of fiduciary obligation;
(iii) confidentiality agreements should be made before any information is imparted; and
(iv) preliminary agreements should address the nature of all matters yet to be formalised.

Cases:
United Dominions Corp Ltd v. Brian Pty Ltd (1985) 157 CLR 1
Hospital Products Ltd v. United States Surgical Corporation (1984) 156 CLR 41
Noranda Australia Ltd v Lachlan Resources NL (1988) 14 NSWLR 1

McLauchlan D.W. "The Legal Status of Heads of Agreements: Recent Developments" [2002 *Australian Mining and Petroleum Law Association Yearbook* 518

McLauchlan discusses recent developments concerning the enforceability of heads of agreement. The paper focuses on the two main issues that are likely to arise when a party repudiates a heads of agreement and the other party seek s remedy for breach of contract: first, was the agreement intended to be legally binding and, secondly, is the agreement sufficiently compete and certain to be enforceable? The author argues that the doctrines of the classical law of contract that sometimes prevented enforcement of preliminary agreement no longer exert the influences that they one did and that the courts are now better placed to reach commercially sensible solutions that reflect the reasonable expectations of the parties. He points, in particular, to the recent recognition by the Australian courts of the principles that there may be a valid contract where parties reach agreement on a limited number of terms which they regard as essential and they defer other matters for future agreement between them.

In the second part of the paper, McLauchlan discusses the decision in *Fletcher Challenge Energy Ltd v Electricity Corporation of New Zealand Ltd*. The statements of legal principles by the Court of Appeal in the course if its judgment are consistent with, and in some respects overtly more liberal than the approach reflected in recent Australian cases, but the author questions the correctness of the actual decision that the heads of agreement in question was not intended to be legally binding. The paper concludes by suggesting some lesson to be leaned from the recent case law.

Cases:
Fletcher Challenge Energy Ltd v Electricity Corporation of New Zealand Ltd [2002] 2 NZLR 433

Cases:
***Fletcher Challenge Energy Ltd v. Electricity Corporation of New Zealand Ltd* [2001] 2 NZLR 219, High Court, Wellington. (Wild J.)**

Facts:
In the course of negotiations for purchase and supply of gas, a heads of agreement (HOA) was entered into. All essential terms were to be binding including quantities, flow rates, start date, duration, prices and force majeure clauses. The HOA provided for approval by the board of directors of ECNA as a condition precedent, for confidentiality, and for the parties to use all reasonable endeavours to complete a full agreement. When full agreement was not reached, FCE sought a declaration that ECNA had not used its best endeavours. ECNZ argued the HOA was incomplete and therefore unenforceable.

HELD: (finding that ECNZ was in breach of its obligation in the HOA to use all reasonable endeavours to reach a full agreement in the required time)

1. When a contractual document shows an intention to be bound, a Court will seek to give effect to that intention notwithstanding uncertainty or incomplete terms. Parties could intend to be immediately bound by an informal document even if a more formal agreement was contemplated. Useful factors in determining parties' intentions were: (a) the importance and complexity of the transaction; (b) the degree of formality, informality and terminology of the agreement; (c) detail settled in the agreement; (d) the parties' previous dealings and conduct at and after the agreement; (e) acts in reliance on or part performance of the agreement; and (f) whether the agreement was part of a series of inter-related agreements.

2. The parties intended the HOA to be immediately binding because: (a) such an important, complex and valuable transaction could be stated shortly with important matters left for later agreement; (b) the formal structure and language of the HOA (words such as "agree", "obligation", "liability" and "elect", the confidentiality clause, execution by senior managers and reference to a later "full" (not "binding") agreement) indicated an intention to be bound; (c) the chief executives required a binding HOA; and (e) the parties' subsequent conduct showed they believed the HOA was binding (for example, in bidding for the shares, disclosure of the HOA to third parties and negotiations for a full agreement).

3. An agreement to state contractual terms in a later formal contract was complete, and therefore binding, if the parties agreed to be immediately bound to perform the terms of the contract but also agreed to restate them in a fuller or more precise but not different form; or if the parties agreed on all terms but with one or more terms conditional on execution of a formal document. The Court could supply reasonable terms if the parties failed to agree on essential terms. However, there was no binding contract if the parties agreed not to be bound until a formal contract was executed.

4. The parties' agreement was not incomplete by stating that certain terms were "not agreed" or "to be agreed" because the Court could supply reasonable terms if necessary, or such terms were not essential, or not necessary to make the contract workable.

5. An ambiguous contract did not fail for uncertainty if there was one sensible or definite meaning of essential terms.

6. A term requiring best or all reasonable endeavours was enforceable if what had to be done was sufficiently certain. The obligation in the HOA to use all reasonable endeavours was sufficiently certain to be enforceable.

For commentary on this case see:

Willis J. (2000) 19 *Australian Mining and Petroleum Law Journal* 266 (NZ High Court)

Willis J. (2001) 20 *Australian Mining and Petroleum Law Journal 312* (NZ Court of Appeal)