regarded as a proper and lawful purpose and thus take the provision outside of the doctrine. Waite distinguishes between contractual rights and property rights, and between those rights and mere contractual obligations, discussing the extent to which each of these may be validity assigned.

Books

Manning W.F. "Some Practical Aspects of Resources Joint Ventures" in W.D. Duncan (ed), *Joint Venture Law in Australia*, The Federation Press, Sydney, 1994, Chapter 10

Manning's paper provides a very clear and concise practical overview of issues involved in assignment of a joint venture interest. The paper discusses the advantages and disadvantages of pre-emptive rights and the operation of pre-emptive provisions, including the rule against perpetuities and prohibition on restraints against alienation. Manning then discusses other restrictions on assignment such as: consent of other parties; agreement as to minimum levels of interest; and the prohibition on partition or judicial sale. Manning also considers how change of ownership may be effected by a joint venture parent company, through sale of a wholly-owned subsidiary holding the joint venture interest, in order to avoid restrictions on assignment of the interest. It is suggested that in these circumstances, a guarantee from the parent company can be made a condition for such an assignment to proceed. If change of control or ownership provisions are included in the joint venture agreement, a specific exception should be made for a listed company as the change of ownership is beyond the control of the existing shareholders or directors of the company, where shares are being traded on the market.

Legislation:
Trade Practices Act 1974 (Cth)
Section 45B(1) provides
A covenant, ... is unenforceable in so far as it confers rights or benefits or imposes duties or obligations on a corporation ... if the covenant has, or is likely to have, the effect of substantially lessening competition in which the corporation, ... supplies or acquires, or is likely to supply or acquire, goods or services or would, but for the covenant, supply or acquire, or be likely to supply or acquire, goods or services.

2.3 Farm-outs and Farm-ins

Articles

Mykyta T. "Farm-in Arrangements in the Mining Industry: The GST Implications" (2000) 19 *Australian Mining and Petroleum Law Journal* 247

Mykyta gives a clear and concise explanation of the problems arising in the application of the "*GST Act*" to farm-in/farm-out arrangements. Through a hypothetical case study, the author demonstrates how both the exploration activities of the farming-in entity, and the giving of an

interest in return by the farming-out entity, may constitute "supply" for "consideration" subject to goods and services tax ("GST"). However in the circumstances of a farm-in agreement, the supply of exploration services (consideration for tenement interest) is periodic and progressive, while the rights to the tenement (consideration for services) are conditional, creating potential cash flow problems because the GST liability and claiming of imputation tax credits are unlikely to arise in the same tax period. Mykyta offers several solutions, including treating the transaction as a supply of a going concern, so that the transfer of the interest in the tenement would be GST-free; utilising the GST Joint Venture provisions, such that supplies and acquisition are treated as akin to transactions made within an entity (although the author raises concern that on the facts of *Pursell v Newberry*, a farm-in may not fit the description of 'joint venture' for tax purposes, and even if it did, may not alleviate the compliance burdens imposed in a farm-in arrangement); or to invoke the discretion of the Commissioner of Taxation to override the general attribution rule and determine a different tax period to that in which the GST liability or the entitlement to an imputation tax credit is ordinarily attributable.

Cases:
Pursell v Newberry (1968) 118 CLR 381

Acts:
A New Tax System (Goods and Services Tax) Act 1999 ("GST Act")

Williams H.P "Matters to be taken into consideration in the Negotiations of Farm-outs and Operating Agreements" (1978) 1(2) *Australian Mining and Petroleum Law Journal* 509

Williams describes the operation and procedures relevant to farm-out arrangements in the Australian context, and investigates problems for farm-in/farm-out arrangements under Australian law. In discussing the legal contracts, Williams first looks at the issues arising under the Commonwealth and State legislation, including petroleum legislation, trade practices legislation, foreign takeover legislation and foreign exchange control legislation. Williams then considers the effect of the "of no force" provisions on the indefeasibility of petroleum titles and concludes that those provisions act merely as a conditional imperfection, and do not derogate from the legal or equitable rights which otherwise attach to unregistered instruments. Williams offers practical suggestions on mechanisms by which a royalty holder can secure an overriding royalty to effect recourse against an assignee. Where transfers of royalty agreements cannot be registered, the title of a transferee may be protected by novation, so long as the original royalty agreement permits this.

In the second part of the paper, Williams steps through the provisions of a typical farmout-operating agreement, and considers the salient commercial and legal issues relating to particular aspects, including recitals as to title, earning conditions, vesting, scope of venture, default, operating committee, operator, disposition of production, sole risk proposals, withdrawal, accounting procedures, and severance of terms.

Legislation:
Petroleum (Submerged Lands) Act 1967 (Cth) *
Trade Practices Act 1974 (Cth)
Foreign Acquisitions and Takeovers Act 1975 (Cth)
Banking (Foreign Exchange) Regulations 1959 (Cth)

*Minor amendment to this Act with regard to licences and permits, are currently before parliament.

Birch C. "Choosing the rights Joint Venture Structure for a Farm-in or Farm-out" (2002) 5(1) *Journal of Taxation* 60

Birch examines in detail, the compliance costs associated with income taxation of farm-outs, which will vary depending on the structure of the farmouts agreement, whether the taxpayer is a farmer or farmee, and whether the farmer and farmee is an equity participant.
He begins by describing a farmout, but notes the type of interest will vary according to the different structures associated with joint ventures (in an unincorporated joint venture, participants have a direct interest in the assets of the ventures, as tenants in common, whereas in an incorporated joint venture, the equity participants hold only a shareholding in a special Purpose Vehicle ("SPV") incorporated specifically for the venture purpose).

Birch discusses the practical and commercial reasons for using a farm-out, and the manner in which farm-outs can be legally structured, namely as a "deferred transfer farm-out" (where a farmee agrees to undertake certain obligations following which it is entitled to take an interest in the exploration title - these arrangements are usually drafted as an *option*, or an *executory contact to assign*) or as "immediate transfer farm-outs" (which involve an immediate transfer of an interest subject to an obligation to re-convey in the event of default in performance of farm-in obligations). Other farm-out arrangements exist, for example, stepped or incremental earning programmes and the definition of farm-out adopted by the Commissioner of Taxation in *Income Tax Ruling* 2378 (IT 2378, para 1) encompasses a wide variety of arrangements. The major types of farm-outs are described, namely, carried interest agreements, unitised agreements, earned obligation agreements, production payment agreements and overriding royalties, and equalisation agreements.

In the second part of his paper, Birch analyses in detail, the compliance costs of farm-outs of assets. Issues examined include the cost associated with characterising the profit from a farm-out, under the provisions of the *Income Tax Assessment Act* 1997 (ITAA97) according to the concepts of ordinary income and statutory income (including capital gains and expenses) and losses of either a revenue or capital nature. It follows that the proceeds from a farm-out of assets may be taxed in a variety of ways depending on the purpose for which the assets are held, before they are disposed of. Birch also discusses the situation where prospecting entitlements fall within the meaning of "trading stock" and problems in determining the cost price of trading stock. The implications for changes under the Ralph Review* to both these areas of tax law are also considered.

Birch draws attention to the complications that can arise when making depreciation balancing adjustments, if the parties' intentions are not sufficiently documented during the drafting phase of the farm-out agreement. He suggests that if parties enter into an agreement to transfer allowable capital expenditures, then a taxation clause could be included in the farm-out agreement. He provides a draft tax clause that may be used in the farm-out agreement (depending on the nominal value on the interests the subject of the farm-out) to cover the situation where a farmer disposes of its undivided fractional interest in exploration plant, or arguably to exploration or prospecting expenditures when a prospecting entitlement is disposed of.

Birch then examines in detail, the complex taxation problems arising under the ITAA97 in relation to (i) mining information; (ii) allowable deductions to the farmee for exploration and prospecting expenditures; (iii) capital gains provisions (eg. determining if a farmee has an equitable interest if it is under no obligation or limited obligation to earn an interest and determining what will amount to capital gains tax events) and (iv) calculating consideration on disposal.

The final part of the paper looks at the compliance cost of farm-outs of shares. Birch concludes that a farm-out structured as a disposal of assets bears more compliance costs than farm-outs structured as options over shares.

Legislation:
Income Tax Assessment Act 1997 (Cth)
Income Tax Ruling 2378

Reports:
* *Report of the Review of Business Taxation: A Taxation System Redesigned* (Canberra: AGPS, 1999)

Lowe, J.S. "Analyzing Oil and Gas Farmout Agreements" (1987) 41 *Southwestern Law Journal* 759

Written in a United States legal context, Lowe analyses the structure of typical farm-out agreements and considers problems and alternatives that practitioners must confront in drafting or reviewing farm-out agreements. His article discusses US tax law related to farm-outs (in particular Revenue Ruling 77-176 which deals with farm-outs) and the farmor's and farmee's purposes for entering a farm-out agreement, both of which will determine how the farm-out is structured. The distinction between farm-outs and operating agreements is drawn and definitions of support agreements, seismic option agreements, and other variations are given. The paper looks at preliminary matters to be considered, key characteristics of the agreement, and issues that must be addressed in preparing the farm-out agreement.

The essential elements of a typical United State farm-out agreement are analysed in detail. Many sample clauses are suggested in the course of the discussion. All aspects of the drilling process are considered (eg. subject matter; geological information; commencement procedures; measuring of the drilling process; and performance standards) followed by an equally detailed discussion on the drafting of provisions for other issues (eg. tax, liability, reassignment, and environment).

Lowe observes in summarising, that farm-out agreements are very much a function of tax rules, and that otherwise, the agreements will vary widely according to the goals of the parties. For this reason, farm-out agreements need to be flexible, and to this end, Lowe provides many possible alternative provisions.

2.4 Sole Risk and Non-Consent

Articles

Ryan G.L.J. "Sole Risk and Non Consent from Oil and Gas Exploration" [1983] ***Australian Mining and Petroleum Law Association Yearbook*** **272**

Ryan provides a clear and detailed examination of how sole risk and non-consent provisions operate in the context of oil and gas joint venture agreements. The author emphasises the need for very careful consideration to be given to commercial and technical issues in the drafting of such clauses, in particular as to what types of work can be the subject of a sole risk or non-consent programme, and the premiums associated with them. Ryan offers suggestions as to how sole risk issues of indemnity of non-participants, supervision, non-interference, time limits, joint venture and sole risk interests, and sharing of data may be approached. The paper sets out the factors to consider in measuring the success of a sole risk programme; the legal difficulties arising in relation to the interests in the joint venture of the non-participating venturers in the event they elect not to participate in further operations of the sole risk programme; the size and source of funding for any buy back premium; and taxation considerations attaching to any buy back scheme.

On the issue of whether a court would consider a buy back premium to be a legal 'penalty', Ryan submits that a court would not find the premium to be a penalty, as there has been no breach of contract. Similarly, even if the non-participating venturer loses its entire interest in a sole risk programme, the question of penalty would not arise, as the loss of interest is not due to a breach of contract, but is a consequence of electing not to participate.

Pliner R. and Coyle M. "The O'Dea-Allstates Case and the Implications for Exploration and Mining Joint Venturer Agreements" (1983) 2(3) ***Australian Mining and Petroleum Law Association Bulletin*** **37**

Pliner and Coyle examine the findings of the *O'Dea* case, and conclude that the premium paid for a non-participant to buy-back into a sole risk activity would not be considered a 'penalty' as there is no breach of contract involved. The non-participating party had made a voluntary decision not to contribute - the buy-back premium is merely a price to be paid to enable it to re-enter the sole risk activity, not an assessment of damages. Neither would a buy-back clause be considered a forfeiture of interest even where the non-participating party is unable to financially contribute the buy-back premium, as the resulting 'forfeiture' of interest is not a consequence of a failure to perform a covenant as required under the laws of forfeiture.

Cases:
O'Dea v Allstates Leasing System (WA) Pty Ltd (1983) 152 CLR 359