SOME PRACTICAL PROBLEMS OF JOINT VENTURE AGREEMENTS
Decision-Making and Management

By Brian P. McCafferty*

In this segment of practical problems of joint venture agreements I propose to draw attention to circumstances in which the decision process of an exploration joint venture can be obstructed and also to some difficult situations in which a Manager or Operator may be placed by virtue of his position.

In the negotiations and drafting that surround the formation of an exploration joint venture particular emphasis is always given to important fundamentals such as the preservation of title, acquisition and dilution of interests, financial commitments and deadlock breaking mechanisms. By comparison, the points that I propose to raise appear at first sight to be insignificant and of little importance. That may be partly due to the fact that we expect others to behave in the same reasonable manner in which we always do. Regrettably, the history of human endeavours gives little cause to be optimistic on this point. It has been said that the vagaries of exploration are such that one cannot hope to cover all eventualities when drafting an exploration joint venture agreement. That may be true. It does not follow however, that Participants and draftsmen should rely any more than is necessary on the goodwill of all Participants to facilitate the decision making process and smooth management of a joint venture.

HINDERING THE DECISION MAKING PROCESS

One of the most difficult practical problems that from time to time faces Participants in an exploration joint venture is to find and implement an acceptable means of readily resolving deadlocks and obstructions that occur in the decision making process.

In an exploration joint venture the objective is to proceed swiftly. Delays can be expensive. Money that has been set aside by the Participants for expenditure on the exploration program may only be invested at short term rates; if it has been borrowed interest continues to accrue. Depending upon the nature of contracts for field work delays can increase the contract price. Labour and plant both of which are expensive may not be fully or properly utilized during a delay. A series of delays can jeopardize the Participants' good relations with the relevant Government Authorities. The on-set of a wet season which in many exploration ventures creates a hindrance to field work is another reason for avoiding delays. Finally, the ever present possibility of another competitive find which might adversely affect the economics of the subject joint venture requires that decisions be taken and progress be made without undue delay.

It follows therefore, that the decision making process of an exploration joint venture should ideally be swift and effective. At the same time however, it should be reasonable, for every Participant may at some stage or other be adversely affected by the decision making process. Further, prospective lenders may give consideration to the reasonableness of the decision making process when determining whether or not they will make an advance to a Participant for the purposes of the joint venture.

At the AMPLA Conference held in Sydney in June 1980, two papers dealt with deadlock breaking mechanisms.[1] But each of those papers dealt with the very serious situation of where a deadlock jeopardized the very existence of the joint venture. That of course is the ultimate deadlock. I do not propose again to examine that ultimate situation. I propose to draw attention to what might be termed preliminary skirmishes which may or may not herald that ultimate situation.

In an exploration joint venture, the decision making process usually occurs through meetings of the operating or management committee. Each Participant is entitled to appoint one or more members of the operating committee depending upon the percentage of such Participant's interest, and if there are two or more Participants with a small interest it is common for them jointly to appoint a member to the operating committee. If the Operator itself is a Participant, it frequently occurs that one of the Operator's designated members to the operating committee acts as chairman of the operating committee. Usually, decisions of the operating committee are taken by a majority vote but it is not uncommon to find that certain decisions such as areas to be relinquished or approval of a budget beyond a specified amount must be taken by unanimous vote of the operating committee or by a specified majority. Each Participant is bound by the vote of its designated representative and also by decisions of the operating committee properly taken. The operating committee usually meets at a specified minimum number of times during a year.

An operating committee has been likened to the board of directors of a company. I suggest that this is a dangerous analogy. The duties and responsibilities of directors of a company have been developed by the common law and enshrined in Statute in the context of a creature which though its prehistoric ancestors may have borne some resemblance to a joint venture has now evolved into an entity of its own that is far removed from joint ventures as we know them today. It is the Participants themselves that meet, discuss and take decisions as an operating committee. If an analogy were to be sought, it would be more appropriate to look at a partnership.[2]

As it is the Participants themselves who act on the operating committee, albeit through designated representatives, before looking at the actual process of decision making at a meeting of the operating committee it is helpful to consider whether or not there exist at law any fundamental obligations of Participants *inter se* that may be relevant to their conduct in connection with the decision making process.

When discussing the situation of management later in this paper, I draw attention to the fiduciary relationship that exists between Participants to a joint venture. Putting aside for the moment the special position of the Operator in his capacity as such, the extent of this fiduciary duty is difficult to circumscribe.

In cases where one Participant seeks to gain for himself to the detriment of other Participants some advantage from tangible or intellectual property which is properly that of the joint venture, the position is relatively clear. If at a meeting of the operating committee such Participant fails to make disclosure or misleads his co-venturers with consequential benefit to himself of some property or rights, he may be called to account. But in the absence of either such a motive or effect, a review of the Authorities gives no indication that a joint venturer at meetings of the operating committee has any obligation to facilitate the decision making process except in so far as he has agreed to do so pursuant to the joint venture agreement.

This general position is sometimes recognised in joint venture agreements which contain a clause along the following lines:

> "Each Participant shall be just and faithful to each other Participant and shall act reasonably in all dealings and other matters pertaining to the joint venture."

A clause such as that is an attempt with a broad brush to overcome some of the situations to which I will shortly refer. With respect to those who promote the inclusion of such a clause in joint venture agreements, not only do I suggest that it is inadequate but also I suggest that it may impose an undue hardship on the Participants.

The clause leaves open what is reasonable conduct in given circumstances. This may ultimately require determination by a Court. If there are other or additional means whereby the decision making process can be facilitated they must be preferred. Further, a specific obligation to act reasonably may very well be the subject of an objective test. The fact that a Participant is short of liquid funds and may only borrow at disadvantageous rates of interest may be sufficient reason to him for opposition to a program or budget beyond that originally contemplated. From an objective viewpoint however, the then current situation with the joint venture could render it unreasonable for any Participant to reject the proposal put forward by the Operator.

In an exploration joint venture, differences of opinion among the Participants usually arise in the following areas:

(a) Disagreement about the program;

The technical advice available to a Participant may differ from the advice proffered by the Operator and the Operator's recommendations; a Participant may have a particular interest in pursuing traces of an ore body different from the primary search.

(b) Disagreement about the budget;

Quite apart from the differing financial positions of the Participants, a Participant may not share the same sense of urgency as the Operator; a Participant may disagree with the Operator's proposed allocation of expenditure; a Participant may wish to control the Operator by restricting or even eliminating permissible overruns.

(c) Areas to be relinquished;

Subjective interpretation of analytical data may be different; a proposal to relinquish an area suitable for open cut in favour of a possibly richer but definitely underground prospect may not be immediately appealing to all Participants.

(d) Dissatisfaction with the Operator;

The Operator's performance though acceptable may not be entirely satisfactory with consequential friction between the Participants.

(e) Disagreement about policy — risk taking or conservative.

In any of those areas, a Participant though willing and ready to proceed with the business of the joint venture may have valid grounds for complaint and dissatisfaction. Such a Participant, whilst not being prepared to withdraw from the venture — if such course is available — may be prepared to take whatever measures are open to him short of terminating the venture in order to assert his position.

In the absence of specific and detailed provisions in the joint venture agreement it is in this kind of situation that the decision making process can almost grind to a halt. Regrettably, many joint venture agreements do not contain

sufficient specific detailed provisions relative to the decision making process in order to prevent or at least minimize obstruction and delay which does not constitute default.

Let us now turn to some of the situations that might offer a disgruntled Participant an opportunity to express his dissatisfaction short of going into default.

1. Appointment of Representatives to Operating Committee

Most joint venture agreements require Participants to appoint the appropriate number of representatives to the operating committee and to ensure that those representatives or their respective alternates duly appointed attend meetings of the operating committee. There is generally little problem with the designation of the first members of the operating committee. If there were, the joint venture would hardly start. Appointment of replacement members however, is sometimes a different situation.

When a Participant's designated member of the operating committee (and his alternate) retires from office, unless the Participant promptly designates another representative the decision making process may be hindered. This of course is subject to the particular circumstances and especially to whether or not the representative of that Participant is necessary to constitute a quorum. If the reluctant Participant's representative is not necessary to constitute a quorum at meetings of the operating committee then this avenue of obstruction would not be appropriate to that Participant. In the converse situation, it could be.

Assuming that the Participant concerned does not simply refuse to appoint a representative but rather delays the appointment giving apparently valid reasons (which may not be difficult in the case of an overseas Participant) mere delay itself as distinct from actual refusal may not constitute a default under the agreement. Perhaps the other Participants' ultimate remedy is to apply for a mandatory injunction. Even if this remedy is available however, it is hardly likely to be availed of not only because legal proceedings are likely to spell the end of the joint venture, but also because the natural preference of Participants in mining ventures is to endeavour to settle differences firstly by discussion and secondly by resorting to their interpretation of the relevant provisions of the agreement if one can be found.

If in the situation under review, the presence of the Participant's designated member of the operating committee is necessary to constitute a quorum at a meeting of that committee, the agreement may very well provide that if at any duly convened meeting of the committee a quorum is not present within a specified time, then the meeting is adjourned for a definite period until a definite time and place at which those representatives present, irrespective of their number, shall constitute a quorum. Assuming that in the absence of a designated member notice of meetings can be given to a relevant Participant (as distinct from the Participant's representative) so that a meeting of the operating committee can be properly called (and such a provision is helpful in many circumstances), the provision relative to a quorum at adjourned meetings will ultimately solve the problem.

It would be advantageous however, to have in addition in the joint venture agreement provision that a representative once designated remains a representative until his successor is appointed or perhaps a provision that if a Participant fails to appoint a representative to the operating committee within a specified period

after request by the Operator or the other Participants, then the other Participants may designate an individual who is deemed to be the duly designated member of the reluctant Participant.

2. Quorum

A meeting of any organisation requires the presence of a quorum to enable the meeting properly to transact business and to pass binding resolutions.[3] If a member or members whose presence is necessary to constitute a quorum refuses or fails to attend, the meeting cannot properly be held. Joint venture agreements commonly prescribe the minimum number of members whose presence is required to constitute a quorum of a meeting of the operating committee. It has also become common practice to provide that if within a specified period after the time for which the meeting is called a quorum is not present, then the meeting is adjourned to a specified time and place at which the members there present irrespective of their number of personnel will constitute a quorum. Implementation of a provision of this kind is not uncommon in meetings of voluntary organisations and sometimes at meetings of companies.

The situation sometimes occurs however, where, having attended at the required time and place and having participated in part of a meeting of the operating committee, a member or members whose presence may be thought necessary to constitute a quorum leave the meeting. The cause of their leaving may be valid and reasonable. On the other hand, it may be due to some strong disagreement with a proposal that seems to find favour amongst the other members of the committee, or due to a reluctance to have discussed and decided a subsequent item on the agenda.

Whether or not the meeting can validly continue in those circumstances is arguable. It is certainly doubtful if the joint venture agreement without more simply prescribes the quorum necessary for meetings of the operating committee. On the other hand, there is authority for the proposition that where the articles of association of a company provide that: "No business shall be transacted at any . . . meeting unless a quorum is present when the meeting proceeds to business", the presence of a quorum is only necessary at the commencement of the meeting and is not necessary when the meeting proceeds to vote.[4] There seems no palpable reason why except in special circumstances that authority should not apply to a similar provision in a joint venture agreement. Such a provision simply anticipates the earlier provision referred to that where a quorum is not present the meeting stands adjourned; it is however, another means of facilitating the decision making process.

3. Adequacy of Notice and Supporting Material

The general rule is that a notice calling a meeting of members of any organisation must reflect the general nature of the business to be discussed at the meeting. It is said that the purpose of notice is to enable members to take a decision whether or not to attend the meeting.[5]

But this general rule is subject to certain exceptions. In the case of meetings of directors of a company, notice of special business to be discussed at a meeting of the board is not necessary.[6] Another exception to the general rule is that the rules of the relevant organisation may prescribe the adequacy of notices calling meetings. It may be arguable that in a joint venture situation, at least in so far as taking decisions

at a meeting of the operating committee is concerned, vital matters affecting the joint venture may be brought up and decided at a meeting of the operating committee without prior notice. But most joint venture agreements remove the possibility of that argument.

It is common for joint venture agreements to provide that a specified period of notice of operating committee meetings must be given unless all members of the committee agree to accept shorter notice. Joint venture agreements also usually provide that with the notice calling the meeting of the operating committee there shall be furnished a copy of the agenda and such supporting information in reasonable detail as may be requisite to enable members to discuss and take a decision on the various agenda items. It is also customary to provide that only matters specified on the notice paper shall be considered at the meeting of which notice is given unless all members of the operating committee otherwise agree.

Again, joint venture agreements usually provide that meetings of the operating committee shall be called by the Operator (or by the chairman if he is not a representative of the Operator) but that any member of the committee upon giving to the Operator (or the chairman) an agenda item with supporting material may either require the calling of a meeting of the operating committee or request that a particular matter be included on the agenda at the next regular meeting of the committee.

In cases where there is a running antipathy between Participants, this field of adequacy of notice of operating committee meetings can provide a fertile source for hindering the decision making process.

For example, a member may complain that the supporting material is inadequate or deficient. There may be justification for this because it often happens that due to the length of notice calling meetings of the operating committee the Operator will furnish the latest information either shortly before the meeting or even at the commencement of the meeting itself. Irrespective of that however, if a member is determined to hinder the decision making process his objection cannot be taken lightly. It may not be of much assistance for all other members present to disagree from his point of view because, if the objecting member leaves the meeting on that ground, then although a quorum may still remain, those who do remain would need to make sure that no further information at all concerning the agenda item in dispute was furnished at the meeting as this may very well establish the validity of the objecting member's argument.

One consequence of this rather untidy situation may very well be that the dissenting member who leaves the meeting is not bound by the decision that is taken in his absence. If the decision involves a further contribution towards expenditure, he may accordingly be relieved from his shares of that obligation. It is even feasible that subsequently he may comply with the decision and at the same time reserve his rights generally leaving the matter in an unsatisfactory state.

The safest alternative for the remaining members may very well be to have another meeting of the operating committee called. However, if the joint venture agreement provides that unless a majority of the members of the operating committee otherwise determine, the Operator (or the chairman as the case may be) shall be the sole and final arbitrator of the adequacy of the contents of the notice paper and supporting material, then provided the Operator or the chairman has acted reasonably, an objecting Participant may have little room to hinder the decision making process on this point.

Another example, but on the reverse side of the coin, is the situation where the Operator (or the chairman) fails by design or otherwise to include on the agenda of a notice calling a meeting of the operating committee an item (with supporting information) requested by a Participant. This action or inaction on the part of the Operator, whilst no doubt being in breach of the spirit of the joint venture agreement, may not necessarily be a breach of the agreement, depending upon how the relevant provision is drafted. In any event, if the Operator is in charge of the calling of meetings, his action or inaction on this point may not be a breach of his duties as Operator.

Joint venture agreements do not usually provide that if the person responsible for the calling of meetings of the operating committee fails to include in the agenda an item of which due notice has been given by a member, then such member may within a limited time after receiving the notice of meeting, circularise other members with notice of the agenda item and supporting papers whereupon such agenda item shall form part of the business to be discussed at the forthcoming meeting. It may be an improvement if such a provision were made.

4. Chairman

Joint venture agreements often provide that the Operator's designated representative (or his alternate) on the operating committee shall act as chairman at all meetings of that committee. In some cases, it is provided that a representative of one Participant shall act as chairman on an annual or biennial basis, the office rotating among representatives of all Participants. Whilst there are many arguments in favour of the latter concept, whichever principle is adopted, there should be scope for the removal and replacement of the chairman of the operating committee.

A chairman of the meeting is usually not vested with dictatorial powers and is generally subject to the wishes of the meeting which may disagree from his rulings or in the ultimate case remove him and appoint another chairman.[7] At committee level where relatively few people are present, most of the strict rules of debate are not followed. At committee level the mark of a good chairman is to ensure that with due allowance for human frailty and the need for occasional light relief, discussion is kept to the point, each member is given reasonable opportunity to express his views and the agenda is completed as soon as practicable. But even at committee level, if there is antipathy between the Participants, the position of the chairman can be used to inhibit the decision making process.

If for example, the chairman of any meeting makes a ruling or a series of rulings that may be contrary to the wishes of the majority at the meeting, the ultimate remedy is for the majority to remove the chairman and to appoint another in his place. But if the constitution (and in the context of joint ventures this is the joint venture agreement) provides that a named or indentifiable person shall be chairman of all meetings unless he is absent then this swift and efficient remedy is not available. Other and more drastic remedies may be available such as removal of the Operator but obviously that is a step not to be taken lightly. This is another area where the decision making process can from time to time be obstructed unless of course the joint venture agreement itself contains an adequate safeguard to facilitate the removal of a chairman of the operating committee and the appointment of his replacement.

It is not my task to expound on the law or practice relating to the holding or

conduct of meetings. The preceding comments are designed simply to illustrate how in certain circumstances lack of precision or definition in joint venture agreements on this question can inhibit and create a continual series of delays in the decision making process. To those who might suggest that I have taken too theoretical a position and that if the circumstances which I have outlined arose, then the subject joint venture would be doomed — and such a suggestion would not be unreasonable — I make three further points.

Firstly, if one Participant took every obstructive point to which I have referred and indeed many others which may be available to him, then I agree that the joint venture may very well be doomed. But it is open to any Participant who for reasons earlier alluded to wishes at least temporarily to slow things down to occasionally take one or more of the points I have mentioned.

Secondly, I have seen in one joint venture two separate Participants at different times take some of the points I have mentioned and effectively slow down the decision making process. All the Participants were interested in the venture and the attitude of the two protaganists did not cause the joint venture to dissolve. On the contrary, there was engendered a healthy respect for the unpredictable attitude of the two parties concerned which may very well have had the effect of causing the Operator to be particularly careful in the conduct of operations and in his reporting to the Participants. In the ultimate that may have been for the benefit of the venture but it certainly did not facilitate the decision making process.

Thirdly, those of you who have had the experience of advising the chairman of a forthcoming contentious meeting, will no doubt agree that reliable authority on many arguable points that surround the calling and conduct of meetings is simply not available and that most difficulties arise by reason of lack of precision or even lack of reference at all in the governing constituent document.

And this is where I suggest more attention can be given in the drafting of joint venture documents. Participants are usually very keen to analyse and criticize the accounting procedures governing the application of expenses of a joint venture. This is where the pocket is obviously hit. But the pocket can also be hit as a result of obstruction or delays in the decision making process and I suggest that consistent with the constraints of commercial realism, closer attention to the drafting of the provisions relative to the calling and conduct of operating committee meetings, or even the incorporation of standing orders in the joint venture document, will assist Participants by removing grounds for intentional delay.

MANAGEMENT

The structure of joint venture exploration agreements that have been in common use in Australia calls for the appointment of a manager of the operations (an expression which should be carefully defined), frequently called the Operator. This has been found to be the most practical, convenient and perhaps efficient means of organising and implementing the works program.

Customarily the Operator is given the exclusive right to conduct operations subject to instructions given from time to time by the operating committee. In addition, specific powers and obligations are generally imposed on the Operator. These include:

Preparation of drilling and exploration programs;
Organisation and supervision of the labour force;
Acquisition of necessary plant and equipment for the joint account and possession

and custody of the same;
Implementation of programs approved by the operating committee;
Maintenance of titles in good standing and compliance with necessary statutory requirements;
Periodic reporting to the operating committee;
Preparation of budgets;
Incurring of expenditure within budgets;
Calling of regular meetings of operating committee;
Payment of expenses for the joint account;
Right to recover expenditure from Participants.

Whether or not he is a Participant, the Operator usually attends meetings of the operating committee. If he is a Participant he usually appoints the chairman of that committee.

The Operator is usually the Participant who holds the greatest percentage interest. This is not however the major reason why an Operator is so chosen. Depending upon the size and nature of the venture it is usually important for an Operator to have available to him from within his own organisation resources which he can utilize for preparation of the works programs and budget, the making of feasibility studies, the maintenance of good relations with government departments and local authorities and the continuous review of possible markets and other financial considerations to encourage the Participants to proceed with the operations.

It often happens that by reason of the magnitude of expenditure required for some prospects, notwithstanding the resources available to the Operator, the Participants are not content to rely entirely upon the Operator's technical ability. In consequence technical committees are formed on which Participants have representatives and the function of which is to keep Participants directly informed and to provide a check on the Operator's recommendations. Nevertheless, it is the Operator who usually puts forward the formal recommendations to the operating committee.

Operators have been careful to endeavour to contract out of as much as possible of their liability to other Participants. A typical clause in a joint venture agreement runs as follows:

> "Operator, its employees or agents, shall not be liable to the parties hereto, or any of them, for any acts done or omitted to be done in good faith in the performance of any of the provisions of this agreement, unless in doing or omitting to do any such acts, the Operator shall have been grossly negligent or guilty of wilful misconduct."

The scope of the Operator's powers and the restriction on his liability to other Participants at first glance places him in an enviable position — power without responsibility. Subject to what circumstances may constitute gross negligence as distinct from ordinary negligence (and in many cases the distinction may be fine), if the relationship between Operator and Participants is that of independent contractor an exclusion clause such as that just referred to may give an Operator a high degree of immunity. Not necessarily so however, if the relationship is that of agent and principal.

Although there is considerable judicial and academic debate as to the elements of agency, it appears that nearly all authorities agree that the essential characteristic of an agent is that he is invested with a legal power to alter his principal's legal relations with third persons.[8]

Perhaps the simplest means of understanding the typical features of agency

is to compare the principal-agent relationship with similar relationships particularly those of master and servant and employer and independent contractor. Halsbury compares the three relationships in the following manner[9]: "The relation of agency arises whenever one person, called "the agent", has authority express or implied, to act on behalf of another, called "the principal" and consents so to act.

An agent is to be distinguished on the one hand from a servant, and on the other from an independent contractor. A servant acts under the direct control and supervision of his master, and is bound to conform to all reasonable orders given him in the course of his work; an independent contractor, on the other hand, is entirely independent of any control or interference, and merely undertakes to produce a specified result, employing his own means to produce that result. An agent, though bound to exercise his authority in accordance with all lawful instructions which may be given to him from time to time by his principal, is not subject in its exercise to the direct control or supervision of the principal. An agent, as such, is not a servant, but a servant is generally for some purposes his master's agent, the extent of the agency depending upon the duties or position of the servant, and in some cases an independent contractor may also be an agent."

Under many exploration joint venture agreements the Operator is given wide powers in the performance of operations leaving little scope for control or direction by the Participants. In many respects such Operators would appear to have all the essential characteristics of independent contractors. But although some text book writers such as Friedman[10] take strong exception to the view that an agent strictly so called can also be both a servant or an independent contractor, it must still be strongly arguable that unless it can be shown that an Operator is completely free of control from the Participants and has no authority to alter the Participants legal relations with the third parties, the Operator should properly be classified as an agent.[11] This would be so notwithstanding an express disclaimer of agency in the joint venture agreement itself.[12] In the words of Johnson J.A.:

> "If in fact agency is created by the agreement a denial of that fact in the agreement will not prevent it being so."[13]

One of the consequences of the agent-principal relationship is the fiduciary duty thus created. But apart from that relationship an Operator/Participant is in a fiduciary position to the other Participants.

There can now be little doubt that joint venturers stand in a fiduciary relationship to one another. Perhaps the leading statement of the duty imposed upon joint venturers under American law is to be found in the landmark case of *Meinhard* v. *Salmon*[14], wherein Cardozo J. said:

> "Joint Adventurers, like co-partners, owe to one another, while the enterprise continues, the duty of the finest loyalty. Many forms of conduct permissible in a workaday world for those acting at arms length, are forbidden to those bound by fiduciary ties. A trustee is held to something stricter than the morals of the market place. Not honesty alone, but the punctilio of an honour the most sensitive, is the standard of behaviour. As to this there has developed a tradition that is unbending and inveterate. Uncompromising rigidity has been the attitude of the Courts of equity, when petitioned to undermine the rule of undivided loyalty by the disintegrating erosion of particular exceptions. Only thus has the level of conduct for fiduciaries been kept at a higher level than that trodden by the crowd. It will not conscientiously be lowered by any judgment of this Court."

In view of the unequivocable language used by Cardozo J. it is perhaps not

surprising to learn that Professor H.R. Williams, co-author of "Oil and Gas Law", believes that the most important characteristic of a joint venture is the fiduciary relationship of trust and confidence which arises therefrom. Professor Williams states as follows:

> "Each party has the right to demand and expect from his associates full, fair, open and honest disclosure of everything affecting the relationship. One party may not exclude his associates from an interest in properties which are the subject matter of the joint venture by purchasing it for his individual account, nor may he acquire an interest therein antagonistic to the interests of his associates; if he does acquire such antagonistic interest he must account to the other Participants in the joint venture therefor."[15]

This is not a new development in the law. As long ago as 1826 an English Court in the case of *Russell* v. *Austwick*[16] held that a party to a joint venture was under a very stringent fiduciary duty to his co-venturers. In that case, a party to a joint venture, negotiated a contract with the Royal Mint for the carriage of coin along a particular route the object of the joint venture being the carriage of goods along that route as common carriers. He subsequently negotiated another contract with the Mint for the carriage of coin along a different route and claimed the benefit of this contract for himself and one of the other joint venturers. The other members of the joint venture while admitting that the second contract had no connection with the route of the joint venture, nonetheless claimed the benefit of it on the grounds that it was entered into by the Mint as connected with and a continuation of the joint venture agreement. The presiding Judge, Sir John Leach, found that the defendant ". . . did not apprize them that he was treating for himself in exclusion of the plaintiffs . . . and upon the settled principles of equity, therefore, he could not exclude them from the same proportion of the profits as they were entitled to under the first agreement."

Although there is little guidance to be gained from the English authorities as to the nature of a joint venturer's fiduciary duty, the American authorities indicate that once a joint venture is entered into each Participant owes to all the other Participants the duties of scrupulous honesty, utmost good faith, fair dealing and of protection of the rights of all other Participants to the same extent as his own.[17]

These duties, strict as they might be, appear to be stricter in the case of a joint venturer in charge of the management or operation of the business of property of the venture namely an Operator/Participant.

In *Spiritas* v. *Robinowitz*[18] it was held that a managing "partner" for a joint venture owed each other joint venturer one of the highest fiduciary duties recognized by law.

The position of a party who is both Participant and Operator of a joint venture was described by Cardozo J. in *Meinhard* v. *Salmon*[19] in the following terms:

> ". . . Salmon had put himself in a position in which thought of self was to be renounced, however hard the abnegation. He was much more than a co-adventurer. He was a managing co-adventurer . . .. For him and those like him the rule of undivided loyalty is relentless and supreme."

In agency arrangements, particularly those of a commercial character, it may be possible to exclude some or all of the fiduciary duties and responsibilities of the agent.[20] Having regard to the cautious eye of the Courts to protect beneficiaries one might expect that specific and explicit exclusory provisions would be required. Indeed, in a joint venture agreement which appears to have as its foundation a

fiduciary relationship, if this relationship can be excluded or restricted at all one might expect that the exclusion or restriction would need to be set out in some detail. Especially in the case of an Operator/Participant which, or related corporations of which, act as Operator for or are interested in other exploration or mining ventures apart from the subject joint venture. As yet the practice is not to set out such detailed provisions.

Let us now examine some of the circumstances in which an Operator in the course of managing a joint venture exposes himself to the risk of breach of fiduciary duty and possible action.

Supply of Information:

It is axiomatic that all information gained by an Operator/Participant from the conduct of operations is property of all Participants. Further, the Operator has a fiduciary duty to disclose such information to the other Participants.

Joint venture agreements usually impose upon an Operator an obligation to furnish to all Participants a periodic report on operations including relevant information gained in the course of the operations. An Operator is also usually obliged to furnish to a Participant such further information as the Participant reasonably requires relative to operations although this may be at the requesting Participant's expense. In addition, an Operator is generally required to permit access at reasonable times by the other Participants to operations.

But subsequent circumstances may reveal that provisions such as those outlined are not sufficient to protect an Operator/Participant from a claim of breach of fiduciary duty. If for example during the course of operations, there appear indications of an ore body or some other manifestations are revealed which for any number of reasons are not regarded as significant by the Operator and are not drawn to the attention of the Participants. If subsequent to the withdrawal by a Participant from the venture, either by accident or through a change in circumstances investigation is made into the area of interest previously discarded by the Operator and a project results in which the Operator has an interest, what is the position of the former Participant? Accepting his difficulties of proof, it may very well be that the former Participant is entitled to participate in the venture turned project or to seek his proportionate share from the Operator. The principle applied in Keech v. Sandford[21] is very strict. It is said that that principle does not apply after the fiduciary relationship has been terminated provided the renewal (sic. project) is obtained in a completely independent transaction and without misuse of the fiduciary position.[22] But it is doubtful whether the Operator could take advantage of that exemption.

It is even more doubtful whether or not an exclusion clause of the type earlier referred to would be sufficient to relieve the Operator.

A similar situation arises in relation to adjoining lands. An Operator may not acquire for his own benefit interests in property on the basis of information acquired in the performance of his duties. He will be held to be a constructive trustee for any interests so acquired.

Before a constructive trust can be imposed however, the Courts must first satisfy themselves that the interest acquired falls within the scope of the fiduciary duties. As a general rule it is irrelevant that the profit making opportunity arises as a result of the information derived as venturer or Operator. The important matter is whether or not that opportunity relates to a transaction falling within the scope of

the joint venture.[23] This is also important in the case of a withdrawn Participant who seeks re-entry or compensation from the Operator relative to a project commenced after he withdrew but founded initially on information not disclosed to him whilst he was a Participant. Obviously the project must be one that was within the scope of the original joint venture.

Clearly if an Operator purchases or otherwise secures for himself mining rights over property needed for the successful operation of the business or venture, that would be a matter within the scope of the venture and the Operator would be in breach of his fiduciary duties.

Similarly, one would expect that an Operator who uses confidential information and knowledge derived from geological and geophysical studies or from drilling on the joint venture property to acquire leases upon adjoining areas would be in breach of his fiduciary duties. However, this may not necessarily be correct if the scope of a joint venture is clearly defined and it is apparent from the agreement itself that the parties did not intend to extend the venture into other areas.

This point is well illustrated by an American decision — *British American Oil Producing Co.* v. *Midway Oil Co.*[24] The two companies agreed on a joint venture to exploit the petroleum resources of a designated area. The contract between them spelt out that area in detail as well as the mutual obligations of each party in the venture. British American while developing the area obtained information which induced it to take up oil leases over an area adjacent to the contract area. These leases proved profitable and Midway claimed a half interest in them. The claim was rejected because of the very specific nature and scope of the joint venture:

> "Here each party owed a high degree of loyalty to the other, as applied however to the assembling of leases and the drilling and developing of the specified area involved, and the further duty of faithfully accounting for the income . . .. But when every such duty has been discharged in full, no Court has the right to enlarge the duty of British American and create new rights in Midway by decreeing to Midway a share of profits made by British American from a private risk in a separate enterprise. This cannot be fairly done even in the name of a fiduciary relationship . . . however sacred in a law are these relationships."[25]

Some conclusions may be drawn from the above dissertation. Firstly, it is important if not essential particularly from the Operator/Participant's point of view that the scope of the joint venture be defined in very specific terms in the joint venture agreement. Secondly, at the risk of accepting unwelcome or even apparently unnecessary visits or requests from other Participants, an Operator/Participant may be well advised to be generous in making available the fullest information concerning all aspects of the venture to the other Participants. Thirdly, an Operator/Participant would be well advised to insist on incorporating in the joint venture agreement and in the most explicit terms a complete discharge from a withdrawing Participant and consent for the Operator to make use for his own benefit after a Participant has withdrawn of any information relative to the venture to which Participants had access, notwithstanding that such information may not have been actually furnished by the Operator as distinct from being accessible on file. It is to be expected that such a discharge may more readily be incorporated into the joint venture agreement than obtained when a party is about to withdraw. Fourthly, the joint venture agreement should provide in specific terms the manner in which after acquired lands or titles may or may not be acquired. In the absence of such a provision a Participant but particularly an

Operator/Participant is at risk if he acquires an interest in lands adjacent to the original working area unless his co-venturers have approved of the acquisition after full disclosure.

Use of Operator's Equipment and Personnel

It is the obligation of an Operator to carry out or have carried out field and other work and to be reimbursed for this work in accordance with the accounting procedures either set out in the agreement or otherwise accepted by the Participants. If the Operator subcontracts work to a related corporation and charges excessive rates there would seem little doubt that he is in breach of his fiduciary duties unless he has first made full disclosure to the other Participants. However, even where a subcontractor who is a related corporation charges competitive rates the Operator is likely to be bound to reimburse the other Participants for any profits made as a result of the related corporations' services unless full disclosure has been made beforehand. Accordingly, joint venture agreements should normally give the Operator the right to conduct operations with his own personnel or through related corporations at competitive rates.

Competition

In Australia, many large companies and institutions are directing their investible funds in exploration for oil, gas, coal and other minerals. Some are interested in several ventures of a similar kind. Quite apart from any problem that may arise in relation to adjacent areas, it is possible that an Operator/Participant of a venture may have an interest in another venture which some may claim is competitive.

Notwithstanding the strictures of the Trade Practices Act but no doubt with the sanction of the Australian Government having possible export revenue in mind, most large Australian companies manage to live with the possibility or even the reality of being Participants in joint ventures that might be regarded as competitive.

Even assuming that this is the situation and that the attitude will not change, there remains the risk that a Participant who holds even a minor interest may complain that his Operator/Participant is in breach of his fiduciary duty. Certainly an agent is under a fiduciary duty not to compete with his principal. An Operator/Participant would normally be subject to an obligation not to compete with other Participants.

It goes without saying therefore that if an Operator/Participant is engaged either solely or with others in the same field of endeavour as the subject joint venture, the subject joint venture agreement should make provision to enable the Operator to compete with the joint venture and indeed with any of the Participants therein.

Sanctions

In a two party exploration joint venture, one of the sanctions available to the Operator/Participant against the other Participant who defaults in his contributions is the suspension or withdrawal of certain benefits under the joint venture agreement. A common form of this is the right to withhold from the defaulting Participant information obtained during operations.

One Canadian commentator[26] has suggested that an Operator may be in

breach of his fiduciary duty by exercising this sanction and may be compelled to hold benefits obtained from such information on constructive trust for the defaulting Participant.

High though the Operator's fiduciary duties might be, it is difficult to determine whether that suggested approach would be followed by the Australian Courts. In the absence of Authority one can be expansive, but if the agreement specifically authorised the withholding of information from a defaulting Participant and a Participant did default it might be expected that the withholding of information could only be regarded as a breach of duty when the duty to supply the information formed the subject matter of the joint venture as where, for example, the purpose of the joint venture was to obtain information. The point is, however, arguable.[27]

A similar problem arises under those joint venture agreements which give the Operator the right to suspend operations during such period as a non-Operator fails to meet his financial obligations to the Operator. Under these agreements it is questionable whether the Operator may regard his fiduciary obligations to the defaulting Participant as also being in suspension during the period of default. If the Operator obtains information in his capacity as Operator during such period is he still obliged to hold that information in trust for the defaulting Participant until such time as the default has been remedied? Again, as far as I am aware, this question has not been the subject of judicial consideration. The better view probably is that unless the defaulting Participant remedies his default he would only be entitled to the benefit of such information if the Operator's duty to supply it formed the subject matter of the joint venture.

If, as I have suggested, the joint venture agreement identifies those obligations of the Operator/Participant which give rise to a fiduciary duty, an aggrieved Participant will usually be restricted to suing in contract under the agreement rather than in equity for breach of fiduciary duty. I suggest that for the protection of the Operator/Participant it is better to err on the side of caution and to give full disclosure and get prior ratification from the other Participants before the dangerous area of activity is encountered. It may be possible to reduce the scope of an Operator/Participant's fiduciary obligations by including specific provisions to that effect in the joint venture agreement but it is arguable whether the existence of all fiduciary duties can be completely negatived. The reason for this is that those fiduciary duties constitute the very essence of the joint venture relationship. In the words of Professor Williams, "a joint venture like a constructive trust is an adjective rather than a substantive concept: its main employment by the Courts is to provide a basis on which to find a fiduciary relationship on which to found a constructive trust".[28]

In any event, an Operator/Participant cannot afford to think he has power without responsibility. Further, irrespective of how well a joint venture agreement is drafted, before taking any step that may disadvantage his co-venturers, an Operator/Participant should always carefully consider the possible consequences of his action.

I am grateful for the assistance given to me by John Hawgood, Solicitor, of Brisbane in the preparation of this Paper.

*B.A., LL.B. (Queensland)

FOOTNOTES

1. Michael Sharwood, "Deadlock Breaking Mechanisms and Default Provisions in Mining and Petroleum Joint Venture":
   Michael Coyle, "Deadlock Breaking Mechanisms in Mining and Petroleum Joint Ventures".
2. See Michael Sharwood's Paper, *ibid.*
3. R. K. Yorston, E.E. Fortesque & S.R. Brown, *Australian Secretarial Practice*, 6th Ed., (The Law Book Company Limited) p.251.
4. *ibid* at p.251. See also Re Hartley Baird Ltd. (1954) 3 W.L.R. 964.
5. P.E. Joske, *The Law and Procedure at Meetings in Australia and New Zealand*, 6th Ed., Chapter 3.
6. *La Compagnie de Mayville* v. *Whitley* (1896) 1 Ch. 788.
7. Joske, *Supra*, n. (5) Ch. 5.
8. F.E. Dowrick, "Relationship of Principal and Agent" 17 M.L.R. 24.
9. Halsbury's *Laws of England*, 3rd Ed.; Butterworths, Vol. 1 pp.145-6.
10. G.H.L. Fridman, *Fridman's Law of Agency*, 4th Ed.; Butterworths at pp.15-25.
11. *Shell Oil Company* v. *Prestidge* 249 F. 2d 413.
12. *Commissioners of Customs and Excise* v. *Pools Finance* (1937) Ltd. (1952) 1 ALL. E.R. 775.
13. *Midcon Oil and Gas Ltd.* v. *New British Dominion Oil Co. and Brook* (1957) 21 W.W.R. 228 at 236.
14. *Meinhard* v. *Salmon* (1928) 164 N.E. 545.
15. Williams and Mayer, *Oil and Gas Law*, Vol. 2 at pp.521-522.
16. *Russell* v. *Austwick* (1826) 1 Sim 52.
17. 26 — 8th Digest 1966-1976 p. 902, et seq.
18. *Spiritas* v. *Robinowitz* 544 S.W. 2d 710.
19. *Supra*, n. (14).
20. For some support see *New Zealand and Aust Land Co.* v. *Watson* (1881) 7 QBD 374 at 382 also "Relationship of Principal and Agent" by F.E. Dowrick 17 M.L.R. at 31
    But see also: J.B. Ballem, "The Scope of the Fiduciary Relationship" 3 *Alberta Law Review* p.349.
21. *Keech* v. *Sanford* (1726) 2 Eq. Cas. Abr. 741.
22. See Finn, *Fiduciary Obligations*, The Law Book Company Ltd. p.262.
23. Finn, *supra*, at pp.232-234.
24. *British American Oil Producing Co.* v. *Midway Oil Co.* (1938) 82 P. (2d) 1049.
25. *Ibid* at 1053 per Welch J. for the Supreme Court of Oklahoma.
26. Richard H. Bartlett, "Rights and Remedies of an Operator *vis-a-vis* A Defaulting Non-Operator under Joint and Unit Operating Agreements", *Alberta Law Review* Vol. 10 at p.288.
27. See J.B. Ballem, *supra* note 20.
28. Williams and Mayer, *supra* note 15 but at p.524.