COMMENT ON OPERATOR OF A JOINT VENTURE — PRINCIPAL OR AGENT?

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It is comforting to the writer to be listed as a commentator on Mr. Justice Dowsett's paper and therefore, obviously, required to comment on it rather than criticise it. To adopt a critical approach would, having regard to the fact that this paper is delivered in his Honour's jurisdiction, no doubt involve contempt of Court. It is even more comforting that, even if the writer were of a mind to criticise, it would be virtually impossible to find anything in his Honour's careful and reasoned analysis of the law about which to be critical.

However, there is in his Honour's paper the assertion that 'Lawyers at a conference such as this tend to look at [the problem of whether an operator is a principal or agent] from the point of view of one or other of the parties to the agreement'. It is the writer's experience that those concerned with the drafting of joint venture agreements, at least those agreements concerned with oil or mineral exploration or production, are much more concerned with the power of the operator, and indeed each joint venturer, without approval to commit the joint venturers or do or omit anything which would result in a liability being imposed on them. The writer thinks that all would agree that it should not be too difficult to provide quite adequately for the relationships of the parties *inter se* and that, from that aspect, questions of partnership or otherwise are of little concern. There is no difficulty in effectively negativing the consequences that would flow from an arrangement being held to be a partnership rather than a joint venture, so far as the parties are concerned. The writer does not recall ever having seen a joint venture agreement, even the first draft of one, which did not contain a provision negativing partnership. Nor does he recall it ever having been suggested that such a provision was in any way ineffective so far as the parties are concerned.

There are two reasons for the automatic inclusion in a joint venture agreement of a provision negativing partnership. The first is a tax reason. A joint venture enables each joint venturer to treat his interest in the joint venture and make available elections for tax purposes in the way that best suits his circumstances and regardless of the manner in which any other joint venturer may act. This provision, coupled with a provision under which each joint venturer is given the entitlement to take his share of production in kind are, the writer thinks universally, regarded as being the magic passwords which will result in the arrangement being regarded as a joint venture for Australian tax purposes.

The second reason for the provision is the concern shared by all the parties that their liability should be limited, as far as possible, so that no one of them should, as a joint venturer, have the power to bind the others and that each should have at least a degree of control, consistent with the

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other provisions of the agreement, over his liability for commitments entered into as part of the joint venture.

However, the writer does not think that a provision negativing partnership between joint venturers is regarded as a shield that will in all circumstances protect them from being held to be, or at any rate to have the same liability as, partners so far as other parties are concerned. Rather, it is considered as one weapon, perhaps a basic one, in refuting any allegation to the contrary. But, in addition, it is recognised that the parties must at all times act in a manner consistent with there being no partnership between them and must not do anything that could be regarded as indicative of the existence of a partnership.

The writer should not be thought to be putting the view that a provision negativing partnership is completely effective in avoiding the application, as between the parties, of all incidents of a partnership to a joint venture, for example, the fiduciary obligations of each to the other and an obligation to contribute to losses.[1] Courts have, and no doubt in future will, whilst recognising a distinction between a partnership and a joint venture in appropriate circumstances, by analogy import into the latter particular incidents of the former. However, it is difficult to see how, faced with an agreement which provides expressly that no partnership exists between the parties, a court could hold that, as between the parties it did. It may well fill in gaps in the agreement by implying terms which are in essence terms that apply as between partners and perhaps the end result may be the same. But few of us will, it is presumed, be prepared to admit to such a deficiency in draftsmanship as to necessitate judicial reconstruction or expansion of our documents. If, then, one believes that any question of the real character of a joint venture, as between the parties, will certainly be adequately resolved by one's drafting, the question is academic.

However, while an analysis of the relationship is important to enable the draftsman to ensure that the structure devised avoids unwanted consequences, so far as internal rights and obligations are concerned, it may be quite critical in determining the rights and obligations of the parties so far as others are concerned. If it can be shown either that a partnership exists in fact, or that third parties have been induced, in one way or another, to believe that a partnership exists, then clearly the consequences of that state of affairs will have results which are well known to you all and need no cataloguing.

On the other hand, if it can be shown that there is neither in fact, nor as a result of representations, a partnership, what will be the consequence so far as third parties are concerned? In essence this question, in the context of the subject here being considered, concerns the liability of one joint venturer for the actions of his co-joint venturer. If it is established that there is no partnership, then there is, *ex hypothesi*, no liability as a partner. But since the liability of one partner for the acts and defaults of another is, in essence, a matter of agency, might it not be said that a joint venture also creates a relationship of agency as between the venturers. Or at least, if it

1 See *Television Broadcasters Limited v. Ashton's Nominees Pty. Ltd (No. 1)* (1979) 22 SASR 552.

cannot be said that there is an agency relationship between all the joint venturers is there such a relationship between the operator (whether also a joint venturer or not) on the one hand and the joint venturers on the other?

Such questions are interesting and perhaps an understanding of the principles of law which give rise to them is a prerequisite of recognition and avoidance of the problems that might arise. But might it not be more fruitful to consider how best parties to a joint venture might structure their relationships and conduct themselves so as either to avoid the questions altogether or, if that is impossible, to provide conclusive answers to them.

To the extent that one may have joint venture agreements for which there remains responsibility as draftsman, that is, joint venture agreements where the venture not having collapsed under the burden of legal fees still continues, it is probably too late to do anything about it and there is no point in one being made aware of one's omissions. One can simply hope that nothing arises that will reveal one's ineptitude. If one's worst fears are realised and some disaster occurs for which inadequate provision is made in the joint venture agreement, one can only leave resolution of the problem to determination by those, like his Honour, whose responsibility it is to interpret the unintelligible, determine what the parties (or the draftsmen) had in mind, might have intended or ought to have intended, and produce a just and fair result on the basis of proper legal principles. It will, the writer thinks, be more productive for those whose regular tasks more often involve constructing joint venture arrangements than construing them, to turn to the provision of structural components of those arrangements that will either avoid awkward questions being raised or, if that is unavoidable, provide answers that are reasonably clear, even to an articled clerk.

To return to focus on the subject matter — is the operator of a joint venture a principal or an agent? If it is accepted that it is possible to construct a joint venture in a way that will provide adequately for the rights and liabilities of the parties amongst themselves, then, as the writer has said, the question is academic, for regardless of whether the arrangement is a partnership or not, the agreement will govern the relationships of the parties. What is important is the relationship between the joint venturers on the one hand and third parties on the other. To some extent that relationship may be affected by the relationship between the joint venturers themselves. Thus, if there is a partnership, no real question as to the liability of the joint venturers to a third party is likely to arise, for the law is clear.

However, if the joint venture is not a partnership then it is necessary to examine all the relevant circumstances to ascertain in any particular case what the liability of the joint venturers is. In general, liability will arise either in contract or tort. Different considerations may apply according to whether the liability is contractual or tortious and it is convenient to deal with each type of liability separately. Before turning to this, however, it is necessary to deal with a preliminary matter, namely, the identity of the Operator. His Honour's paper and, so far, this commentary has proceeded

on the assumption that the Operator is one of the joint venturers. This is often the case. But not infrequently the Operator is not a joint venturer, although it may be associated with one or more of the joint venturers.

Where the Operator is not a joint venturer the question of whether or not there is a partnership between the joint venturers becomes less important, for even if the relationship is that of partnership, the Operator is not a partner and accordingly an agency does not automatically arise and the question will fall to be determined by reference to other factors. If the conclusion is reached, on the basis of those factors, that a non-joint venturer Operator is the agent of the joint venture, then the existence or otherwise of a partnership between the joint venturers may be relevant in determining the respective liabilities of the joint venturers among themselves, but is likely to be of little relevance so far as third parties are concerned.

In dealing with the contractual liability of joint venturers the writer proposes to pretend that there will basically be only two types of contract — major and minor. The writer does not propose to attempt to define the difference precisely, but thinks the reason for adopting this dichotomy will become clear. Where major contracts, *i.e.* those involving very substantial amounts of money, are concerned, the obvious question is what is the liability of the joint venturers to the other contracting party in the event of a breach by the Operator? That question will, of course, only arise where the contract is made only between the Operator and the other contracting party. Let one then ask why make the contract in that fashion? Would it not be better for the contract to be made between all the joint venturers on the one hand and the third party on the other? The writer should have thought that, from all points of view, the answer is so clearly 'yes' that it is surprising that major contracts are ever concluded in any other way.

Of course, there will be circumstances where the Operator is so clearly expert in the matter that he wants no interference from the other joint venturers and wishes to proceed quickly to conclude a contract. However, where large amounts are involved, the third party would be far more comfortable with a contract to which all the joint venturers were parties, rather than just the Operator. If, as is often the case, the Operator is not a joint venturer and, in particular, if it is a subsidiary of one of the joint venturers or jointly owned by all of them, and has an issued capital of $2, a third party would be foolhardy to contract with the Operator alone, at least without appropriate acknowledgements or guarantees from the joint venturers.

From the point of view of the joint venturers, their position can be made more secure if they are parties to the contract, for it becomes possible to stipulate any limitations on their respective liabilities, an important aspect where the interests in the joint venture are widely disparate.

More important, however, is the position of the joint venturers if it is the third party who is in breach of the contract. If the contract is made only with the Operator, and assuming it is clear that the Operator contracts as a principal, then the other joint venturers cannot sue for the breach and accordingly cannot recover damages. The Operator can, or course, sue and no doubt the joint venture agreement would, expressly or impliedly,

provide for the sharing of any damages recovered. But since only the Operator can sue he can only recover damages for the loss he suffered and the other joint venturers will not be compensated for their losses. And it is by no means certain that those losses will bear a direct relationship to their respective interests in the joint venture, for each may have quite different obligations which it is unable to fulfil as a result of the breach.

This result can obviously be avoided if the contract between the Operator and the contractor expresses that the Operator contracts as agent for the joint venturers, but if that is the case then the question of the capacity in which the Operator contracts does not arise. In any event, since the contractor under a contract containing such an express provision is most likely to require an acknowledgement from the joint venturers that the Operator is their agent for the purposes of the contract, there seems little to be gained by not having all the joint venturers as parties to the contract in the first place. And finally, it is customary to find in joint venture agreements, usually in the clause negativing partnership, a provision that no joint venturer is the agent of any other, so that the Operator, if he is one of the joint venturers, is not permitted to contract as agent.

Minor contracts may warrant a different approach. The arrangements between the joint venture and the local newsagent for the supply of paper clips can mostly conveniently be made by the Operator and it is unlikely that disputes as to liability will arise, or at any rate proceed beyond the local magistrates' court. Each contract needs to be considered separately to determine whether it is of a nature or magnitude that warrants all joint venturers to be named in and execute it or whether it is of such little relative importance that questions of liability, breach and damages are unlikely to arise, or if they do, are capable of resolution without regard to such questions.

The question of liability in tort involves quite different considerations, for it is hard to imagine circumstances where there is scope for documentation which can adequately record the character or capacity of the tortfeasor so as to avoid questions of the liability of others. Clearly, if the joint venturers are in partnership, the tort of the Operator who is also a joint venturer will be visited upon all joint venturers. If there is no partnership between them, then perhaps liability may be determined by reference to whether or not the Operator is a principal or an agent. This question will fall to be determined by a number of things. In part it may be determined by reference to documents, such as the joint venture agreements; and, if that agreement expresses the Operator to be the agent of the joint venturers, that would seem to be the end of the matter, for although the injured person may have had no knowledge of the provisions of the joint venture agreement immediately prior to contact having been made between the Operator's semi-trailer and his head (indeed it is likely that nothing was further from his mind) the joint venturers will not be heard to deny the agency.

More likely it is that the character of the Operator will be determined on the basis of the conduct of those involved and inferences to be drawn from that conduct. Such mundane things as the form of the

letterhead, the inscription on the sides of the joint venture's or Operator's vehicles and notices at the entrance to the mine site, may be crucial in reaching a conclusion as to the character assumed by the Operator or, at least, the character which the joint venturers have held him out to have.

Thus, for example, if the Operator's stationery bears the inscription "Gigantic Minerals Ltd, Operator for and on behalf of the Glory Hole Joint Venture" it is, in the writer's view, very likely that the Operator would be held to be the agent of the joint venturers, regardless of whether there was documentary evidence to the contrary. On the other hand, if the inscription were "Gigantic Minerals Ltd, manager of the Glory Hole Joint Venture" it would be considerably more difficult to maintain an agency relationship, at least in the absence of contrary documentary indication.

Other factors, although perhaps unknown to an injured party at the relevant time, may also be important, if not critical. For example, if employees are employed jointly by all joint venturers, a person injured as a result of the negligence of an employee in the course of his employment could clearly claim against all joint venturers without resort to an examination of the question of agency in the sense it is here being considered.

The conduct of the joint venturers can, of course, be important in determining contractual liability, for if a contract is silent as to the character in which the Operator contracts, that character may well be inferred from extraneous conduct in the same way it can in the case of tortious liability.

It is perhaps not going too far to suggest that ordinary questions of tortious liability are unlikely to be of great concern. The writer considers that, although the possibility of a major disaster may exist, from a practical point of view claims are likely to be of a relatively small amount. In any event, prudent joint venturers and prudent Operators will have taken out adequate insurance cover protecting all of them. Contractual liability is therefore likely to be the area in which questions of partnership and agency will arise.

As an articled clerk it was instilled into the writer that having no argument is better than having a good answer, a maxim to which the writer firmly adheres. It is therefore important to ensure, as far as possible, that all documents make abundantly clear where liability is to fall and that the conduct of the parties is consistent with that determination. If that approach is adopted, then the scope for arguments to arise will be limited, if it exists at all.

The writer's experience is that joint venturers generally perceive the Operator as a manager or an independent contractor charged with the responsibility of organising and supervising the operations of the joint venture and in the course of so doing to marshal and expend the funds of the joint venture. The Operator's functions will generally be controlled, in broad terms, by the joint venturers either directly or through a management or operating committee. If, as the writer has found customary, joint venturers wish to ensure that their liability for the actions of the Operator,

at least insofar as contractual liability is concerned, is limited in proportion to their interests in the joint venture, then they will be concerned to see that such limitations are expressed, at least in major contracts, and that they are signatories to those contracts. If it is intended by the parties that the Operator is to contract as a principal, then it is the simplest thing in the world for the contract so to specify.

Thus, although it may be tempting to draft documents so as to ensure that difficult questions of liability have a propensity to arise and thereby encourage an adequate flow of work to the litigation department, such questions should generally be capable of being avoided by proper drafting and adequate instruction to clients as to the manner in which they should represent their arrangements to the world at large.