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Joint ventures: the inter-relationship between contract and fiduciary law

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This article revisits the area of establishing fiduciary obligations between parties to unincorporated **joint ventures** and emphasises the importance to the courts of the contractual context of the joint undertaking. This was again evident in a recent New South Wales decision, *Farah Constructions Pty Ltd v Say-Dee Pty Ltd*.¹

Introduction

The application of fiduciary law to commercial transactions has progressed significantly since the dissent of Mason J to the majority decision in *Hospital Products Ltd v United States Surgical Corporation* (*Hospital Products/Surgical Staples* case).² Courts are now far more willing to examine commercial transactions on their merits in order to ascertain whether they manifest the characteristics of a fiduciary relationship. By their very nature, joint venture relationships are collaborative -- the parties must ensure that they act to protect and further the joint objective. In circumstances where a relationship of trust and confidence exists in order to achieve this objective it is more open to the courts to find the existence of fiduciary obligations. The courts' primary focus is to analyse the contractual context of the relationship between the parties.

The critical importance of the contractual context of a joint venture transaction cannot be overstated. The courts will examine the actual agreement between the parties as evidenced by their course of dealings, with a view to ascertaining the nature of the relationship, what the parties have undertaken to do, whether there is a relationship of mutual trust and confidence, what powers or discretions may be exercised by the parties, and the relative vulnerability of the parties.

The contractual context will also determine the scope of any fiduciary relationship, or duties owed by the parties inter se. If a breach of duty within the scope of the fiduciary relationship can be established the advantages of fiduciary law are multifarious, both in method -- for example, the reversal of the onus of proof, presumptions of wrongdoing and disregard of notions such as causation, foreseeability and remoteness, and in remedy -- the flexible remedies of rescission, equitable damages, account of profits and constructive trust.³

The recent decision of the New South Wales Supreme Court in *Farah Constructions Pty Ltd v Say-Dee Pty Ltd*⁴ again illustrates this point.

Approaches to establishing fiduciary relationships in joint ventures

When and to what extent parties to a joint venture will be found to owe fiduciary duties to each other will depend on the approach taken by the court. Courts have developed a status-based test where the court looks for circumstances with which it can draw an analogy to established categories of fiduciary relationships. If, for example, an analogy can be drawn between the joint venture relationship in question, and a partnership or agency, then the fiduciary duties within the scope of those established relationships will apply. This was the approach of the courts in cases such as *United Dominions Corporation Ltd v Brian Pty Ltd*,⁵ *Mount Isa Mine Pty Ltd v Seltrust Mining Corp*,⁶ and *Canny Gabriel Jackson Advertising Pty Ltd v Volume Sales (Finance) Ltd*.⁷

Alternatively, if the relationship between the co-venturers is not necessarily analogous to one of the established

categories of fiduciary relationships, the court may undertake an analysis of the relationship between the co-venturers to establish if it exhibits certain indicia of a fiduciary relationship. This is a fact-based approach -- an analysis of the relationship from first principles to identify if any fiduciary obligations can be inferred from the circumstances. Examples of this approach can be found in the cases of *Pacific Coal Pty Ltd v Idemitsu (Queensland) Pty Ltd*,⁸ and *News Limited v Australian Rugby Football League Ltd*.⁹

Importance of contractual context

As **joint ventures** are contracts, it is also necessary in all cases for the courts to consider the inter-relationship of contract law and fiduciary law. Any fiduciary relationship must conform to the contract and not contradict it, and express terms will operate to the exclusion of any applicable fiduciary duties.¹⁰ Mason J made the following comments in this regard in *Hospital Products*:¹¹

That contractual and fiduciary relationships may coexist between the same parties has never been doubted. Indeed, the existence of a basic contractual relationship has in many situations provided a foundation for the erection of a fiduciary relationship. In these situations it is the contractual foundation which is all important because it is the contract that regulates the basic rights and liabilities of the parties. The fiduciary relationship, if it is to exist at all, must accommodate itself to the terms of the contract so that it is consistent with, and conforms to, them. The fiduciary relationship cannot be superimposed upon the contract in such a way as to alter the operation which the contract was intended to have according to its true interpretation.¹²

This passage was cited in *Noranda Australia Ltd v Lachlan Resources NL*¹³ in circumstances where the court made a non-fiduciary characterisation even though the joint venture agreement provided that the parties owed their duties as fiduciaries. This demonstrates the point that fiduciary duties are not consensual, and a fiduciary or non fiduciary characterisation will reflect an agreement's substantial form.¹⁴

Noranda was referred to by the New South Wales Supreme Court in the recent case of *Farah Constructions Pty Ltd v Say-Dee Pty Ltd*¹⁵ to illustrate the principle that fiduciary obligations cannot be extended to cast upon one party burdens which do not originate in the contract between the parties. The court found that the law of fiduciaries is not available to require a party to undertake responsibilities or obligations which have no source in its contractual responsibilities.¹⁶

Even within a collaborative relationship such as a joint venture there will be instances where the parties can choose their own interests ahead of the joint interest and in such matters there will be no fiduciary duties. Conversely, in a purely arm's length commercial relationship or transaction, a party may, in some matter within the agreement, be required to act in the other party's interests or in the joint interest and a fiduciary duty may arise within an otherwise non-fiduciary relationship.¹⁷

Australian cases have recognised that the existence of a fiduciary relationship may affect some only of the activities of the joint venturers,¹⁸ and even where a fiduciary relationship does exist, the relationship may not be relevant to the particular dispute.¹⁹ In other words, the fiduciary relationship will accommodate itself to the terms of the agreement.

An analysis of the contractual context is also essential for determining the scope of any fiduciary obligation which may exist. The scope of the duty must be determined before it can be found that a breach of duty has occurred.

Farah Constructions Pty Ltd v Say-Dee Pty Ltd

In *Farah Constructions Pty Ltd v Say-Dee Pty Ltd*²⁰ it was necessary to determine whether the scope of the fiduciary relationship in a joint venture extended to land development generally or was limited to the development of a particular site only. In that case the parties had agreed to acquire a parcel of land for redevelopment (no 11). Although no formal agreement was signed, the key terms of the joint venture were set out in a letter. Say-Dee was to provide the start up capital and Farah Constructions was to progress the development application, and manage the construction and sale of the development. The development application was lodged but approval was not granted because the proposed

development was too large for the site. The council suggested that the adjoining properties (nos 13 and 15) be acquired and amalgamated to maximise the development potential of no 11. Subsequently Mr Elias, who controlled Farah Constructions, and others bought nos 13 and 15 with a view to amalgamation and development of the larger site. Farah Constructions brought an application seeking the appointment of a trustee for sale of no 11. Say-Dee cross claimed and sought relief against Elias and others defendants for breach of fiduciary duty. Say-Dee alleged that Farah Constructions, in the course of the joint endeavour, acquired information which was highly pertinent to the partnership business, failed to disclose that information to Say-Dee and exploited that information for its own benefit to the exclusion of Say-Dee.

As Palmer J found that Say-Dee had been offered the opportunity to participate in the redevelopment of the amalgamated site,²¹ it was not strictly necessary to determine the scope of the fiduciary relationship. However His Honour dealt with the submissions on this issue for the sake of completeness.²² He held that the scope of the fiduciary relationship was limited to a development constructed within the boundaries of lot 11 only and said:

... The scope of the fiduciary duties of Farah are defined by the nature and scope of the obligations which it assumed in its contract with Say-Dee.

All that Farah contracted to do was to manage the development of no 11. It did not contract to provide opportunities for Say-Dee to participate in any project other than such development as could be constructed within the boundaries of no 11. The fiduciary obligations of Farah cannot be extended to cast upon it burdens which do not find their source in the contract which Farah entered.²³

Limitation clauses

It may be prudent, therefore to include a clause in the joint venture agreement which defines the scope of the relationship. Contents of such a clause might include the following:

The joint venture is, unless participants agree, strictly limited to the purpose set out in the purpose clause and is not to be construed as extending further by implication or otherwise; nothing in this agreement restricts in any way the freedom of a participant to conduct as it sees fit any business or activity whatsoever; a participant is not obliged to offer any business opportunity available to it to any other participant except pursuant to the provisions governing transfers of joint venture interests in any other specific provision agreed to in a particular clause.²⁴

It should be noted, however, that the effect of a clause which purports to limit the scope of any fiduciary obligations may be that there is no fiduciary relationship. In *Hospital Products Ltd v United States Surgical Corporation*,²⁵ Mason J concluded that a party's capacity to take action in some matters by reference to its own interest was 'inconsistent with the existence of a general fiduciary relationship'.²⁶ Accordingly, where there is a de-emphasis of any relationship based on trust and confidence and an emphasis on the commercial arms length nature of contractual relationship, fiduciary duties may be negated.²⁷ This was expressly acknowledged by Deane J in *Chan v Zacharia* in relation to a partnership agreement when he said that 'it is conceivable that the effect of the provisions of a particular partnership agreement, in the context of the nature of the particular partnership, could be that any fiduciary relationship between the partners was excluded'.²⁸

Where a clause specifically excludes all fiduciary obligations, it is possible that such a clause may, in itself, constitute a breach of fiduciary duty on the basis that public policy requires that a minimum level of core duties must be maintained.²⁹ In any event, although any attempt at exclusion of fiduciary obligations may still be overridden by the particular circumstances of the relationship between the parties, to be effective, the terms of any purported exclusion clause must effectively negate any reasonable expectation of fiduciary obligations including any perception of vulnerability.

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1 [2004] NSWSC 800. An appeal has been filed but has not been heard at the time of writing.

2 *Hospital Products Ltd v United States Surgical Corp (Hospital Products/Surgical Staples case)* (1984) 156 CLR 41; 55 ALR 417.

3 For a comprehensive discussion on all aspects of fiduciary relationships in the context of **joint ventures** see R **Chesmond** and T Cockburn, 'Fiduciary Obligations between Parties to Unincorporated **Joint Ventures**' to be published in B Duncan (ed) *Joint Ventures in Australia* 2nd ed Federation Press, 2005 (forthcoming).

4 *Farah Constructions*, above n 1.

5 (1985) 157 CLR 1; 60 ALR 741.

6 Unreported, SCWA, 5 July 1985, Rowland J.

7 (1974) 131 CLR 321; 3 ALR 409.

8 Unreported, Supreme Court of Queensland, 21 February 1992, Ryan J. In some contrast Deane J in *Hospital Products Ltd*, above n 2, considered that contractual requirements that parties act for the common benefit, or use their best efforts for some objective, did not impose a fiduciary relationship (at CLR 122, 123).

9 (1996) 64 FCR 410; 139 ALR 193.

10 G M D Bean, *Fiduciary Obligations and Joint Ventures*, Oxford University Press, 1995, p xlv.

11 Above n 2 at 96-7.

12 Cf *La Forest in Hodgkinson v Simms* (1994) 117 DLR (4th) 161, 174-5.

13 (1988) 14 NSWLR 1 at 13-16.

14 J Glover, *Equity Restitution and Fraud*, LexisNexis Butterworths, Sydney, 2004, p 83.

15 *Farah Constructions*, above n 1.

16 See also the recent case *iWave Pty Ltd v Break O'Day Business Enterprise Board Inc* [2004] TASSC 43 where the terms of the agreement were sufficient to constitute a trust and a fiduciary relationship between the parties.

17 As Lord Wilberforce said in *New Zealand Netherlands Society 'Oranje' Incorporated v Kuys* [1973] 1 WLR 1126 at 1130, that a person 'may be in a fiduciary position quoad a part of his activities and not quoad other parts: each transaction, or group of transactions must be looked at'.

18 For example, *Pacific Coal Pty Ltd*, above n 8.

19 This was evident in two cases: *Noranda Australia Ltd*, above n 13 and *Mount Isa Mine Ltd*, above n 6.

20 *Farah Constructions*, above n 1. See also *iWave Pty Ltd*, above n 16.

21 At [55], [62].

22 At [65]-[77].

23 At [74]-[75] *Noranda Australia Ltd*, above n 13, at 16.

24 P G Willis, 'Chinese Walls: Myth, Metaphor and Reality -- Living with Fiduciary Duties in Resource Relationships' *AMPLA Yearbook* 2002 558 at 571.

25 (1985) 156 CLR 41.

26 *Hospital Products Ltd*, above n 2 at CLR 98 per Mason J. Note however that recognition was given to fiduciary duties affecting some only of the parties' activities in contrast to a general fiduciary relationship. See also the discussion in Glover, above n 14, at [2.57] citing *John v James* [1991] FSR 397.

27 Ibid at 21. See also *Mount Isa Mine*, above n 6.

28 *Chan v Zacharia* (1984) 154 CLR 178 at 196; 53 ALR 417, cf *Gluckstein v Barnes* [1900] AC 240.

29 C Feasby, 'Fiduciary Obligations and Exculpatory Clauses' (1998) 36 *Alberta L Rev* 923 at 942, 954-55; see also Bean, above n 10 at 84-91.