NEW SOUTH WALES COURT OF APPEAL

CITATION:
United Group Rail Services Limited v Rail Corporation New South Wales [2009] NSWCA 177

FILE NUMBER(S):
40454/2008

HEARING DATE(S):
3 June 2009

JUDGMENT DATE:
3 July 2009

PARTIES:
United Group Rail Services Limited
Rail Corporation New South Wales

JUDGMENT OF:
Allsop P Ipp JA Macfarlan JA

LOWER COURT JURISDICTION:
Supreme Court - Equity Division

LOWER COURT FILE NUMBER(S):
55095/2008

LOWER COURT JUDICIAL OFFICER:
Rein J

LOWER COURT DATE OF DECISION:
18 December 2008

LOWER COURT MEDIUM NEUTRAL CITATION:
[2008] NSWSC 1364

COUNSEL:
M A Pembroke SC, P Liney, T J Breakspear (Apellant)
S G Finch SC, G K J Rich, S Robertson (Respondent)

SOLICITORS:
Mallesons Stephen Jaques (Appellant)
Clayton Utz (Respondent)

CATCHWORDS:
CONTRACTS - Certainty of terms - agreement to undertake genuine and good faith negotiations in a commercial dispute resolution clause - sufficient certainty to be valid and enforceable - meaning

CONTRACTS - certainty of terms - severance - mediation agreement void for uncertainty because nominated dispute centre did not exist - arbitration clause severable.

LEGISLATION CITED:
Australia Acts 1986 (Cth) and (UK)
Civil Procedure Act 2005 (NSW)
Judiciary Act 1903 (Cth)
Law and Justice Legislation Amendment Act 1988 (Cth)

CATEGORY:
Principal judgment

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DECISION:
Appeal dismissed with costs.

JUDGMENT:

IN THE SUPREME COURT
OF NEW SOUTH WALES
COURT OF APPEAL

40454/2008

ALLSOP P
IPP JA
MACFARLAN JA

3 July 2009

UNITED GROUP RAIL SERVICES LIMITED v RAIL CORPORATION NEW SOUTH WALES

Judgment

1 **ALLSOP P:** This appeal concerns the content and operation of a clause dealing with dispute resolution in the General Conditions of Contract of two contracts between Rail Corporation New South Wales, formerly the State Rail Authority of New South Wales ("Railcorp") and United Rail Group Services Limited, formerly known as A. Goninan & Co Limited ("United") under which United undertook to design and build new rolling stock for Railcorp. The relevant provisions are identical and reference need only be made to one group of provisions.

2 The dispute resolution clause, cl 35, is long and detailed, reflecting the parties' careful attention to the subject. The clause commenced with a broadly expressed provision (cl 35.1) dealing with the scope of the clause, as follows:

> "**[35.1] Notice of Dispute**
>
> If a dispute or difference arises between the Contractor and the Principal or between the Contractor and the Principal's Representative in respect of any fact, matter or thing arising out of or in connection with the work under the Contract or the Contract, or either party's conduct before the Contract, the dispute or difference must be determined in accordance with the procedure in this Clause 35.
>
> Where such a dispute or difference arises, either party may give a notice in writing to the Principal's Representative and the other party specifying:
>
> (a) the dispute or difference;
>
> (b) particulars of the dispute or difference; and
>
> (c) the position which the party believes is correct."

3 That clause is to be read liberally as required by the common law of Australia: *Francis Travel Marketing Pty Ltd v Virgin Atlantic Airways Ltd* (1996) 39 NSWLR 160 at 165-166 (Gleeson CJ with

whom Meagher JA and Sheller JA agreed) and *Comandate Marine Corporation v Pan Australia Shipping Pty Ltd* [2006] FCAFC 192; 157 FCR 45 at 87-93 [162]-[187] (Allsop J with whom Finn J and Finkelstein J agreed). See also the law of international commerce: *Fiona Trust & Holding Corporation v Privalov* [2007] UKHL 40; [2008] 1 Lloyd's Rep 254 (see [31] for the phrase "law of international commerce") and *Threlkeld & Co Inc v Metallgesellschaft Limited (London)* 923 F 2d 245 (2nd Cir. 1991). So reading the clause, it can be seen to require the totality of likely disputes between the parties to be dealt with by the clause. No evidence is needed to appreciate that an engineering contract for the designing and building of new rolling stock for Railcorp could lead to complex disputes, which, if litigated, could be productive of very large legal and associated forensic costs. As I said in *Comandate* at 95 [192]:

> "An ordered efficient dispute resolution mechanism leading to an enforceable award or judgment by the adjudicator, is an essential underpinning of commerce. Disputes arising from commercial bargains are unavoidable. They are part of the activity of commerce itself. Parties therefore often deal with the possibility of their occurrence in advance by the terms of their bargain."

4 In cl 35.2 to 35.9, the contract provided for expert determination of certain kinds of dispute. Clause 35.2 provided as follows:

"**[35.2] Submission to Expert Determination**

If the dispute or difference is in relation to a Direction of the Principal's Representative under one of the Clauses referred to in Attachment 'A', the dispute or difference must, if it is not resolved within 14 days after a notice is given under Clause 35.1, be submitted to expert determination to be concluded by:

(a) the independent industry expert specified in Attachment 'A'; or

(b) where:

(i) no such person is specified; or

(ii) the independent industry expert specified in Attachment 'A' or person appointed under this Clause 35.2:

(A) is unavailable;

(B) declines to act;

(C) does not respond within 14 days to a request by one or both parties for advice as to whether he or she is able to conduct the appraisal; or

(D) does not issue his or her decision within the time required by Clause 35.7,

a person agreed between the Principal and the Contractor and failing agreement within 21 days then a person appointed by the President for the time being of the Institution of Engineers, Australia."

5 For present purposes, it is unnecessary to dwell on the details of Attachment A, including the types of dispute to be dealt with by experts and the identity of the experts.

6 Clause 35.3 made clear that the expert was not an arbitrator and could reach a decision from his or her own knowledge and experience.

7 Clause 35.4 provided for the procedure of the expert determination by the adjudicator.

8 Clause 35.5 provided for disclosure of interests of the adjudicator.

9 Clause 35.6 provided for each party to bear its own costs of the expert determination.

10 Clause 35.7 provided for a determination by the adjudicator within 28 days of acceptance by him or her of the appointment, unless the parties otherwise agreed.

11 Clause 35.8 provided for the terms of an adjudication agreement between the parties and the adjudicator.

12 Clause 35.9 dealt with the determination in the following terms:

> "**[35.9] Determination**
>
> The determination:
>
> (a) must be given in writing by the Adjudicator;
>
> (b) will be final and binding unless a party gives notice of appeal to the other party within 7 days of the determination; and
>
> (c) is to be given effect to by the parties unless and until it is reversed, overturned or otherwise changed under the procedure in the following Clauses 35.10 to 35.12."

13 Clause 35.10 provided that if a notice of appeal is given under subcl 35.9(b) or if the dispute is of a kind that is not required by cl 35.2 to be sent to expert determination:

> "[T]he dispute or difference must be determined by arbitration in accordance with the following Clauses".

14 It is to be noted that the parties expressed the process of what was thereafter to occur as the dispute or difference being "determined by arbitration", though, of course, the following words were "in accordance with the following Clauses."

15 Clauses 35.11 and 35.12 are the critical provisions in the appeal. They were as follows:

> "**[35.11] Negotiation**
>
> If:
>
> (a) a notice of appeal is given in accordance with Clause 35.9; or
>
> (b) the dispute or difference for which the notice under Clause 35.1 has been given does not relate to a Direction of the Principal's Representative under one of the Clauses referred to in Attachment 'A',
>
> the dispute or difference is to be referred to a senior representative of each of the Principal and Contractor who must:
>
> (c) meet and undertake genuine and good faith negotiations with a view to resolving the dispute or difference; and
>
> (d) if they cannot resolve the dispute or difference within 14 days after the giving of the notice under Clause 35.1 or 35.9 (whichever is later), the matter at issue will be referred to the Australian Dispute Centre for mediation.
>
> **[35.12] Arbitration**

If the senior representatives referred to in Clause 35.11 cannot resolve the dispute or difference or, where the matter is referred to mediation under Clause 35.11(d), the matter is not settled within 42 days after the giving of the notice under Clause 35.1 or Clause 35.9 (whichever is the later), or within such longer period of time as these representatives may agree in writing, the dispute or difference will be referred to arbitration.

The arbitration will be conducted before a person to be:

(a) agreed between the parties; or

(b) failing agreement within:

(i) 49 days after the giving of the notice under Clause 35.1 or Clause 35.9 (whichever is the later); or

(ii) where the senior representatives referred to in Clause 35.11 have agreed upon a longer period of time prior to reference to arbitration, 7 days after the expiration of that period,

appointed by the President for the time being of The Institute of Arbitrators and Mediators Australia.

The Rules for the Conduct of Commercial Arbitration of The Institute of Arbitrators and Mediators will apply to the arbitration.

The arbitrator will have power to:

(c) open up and review any Direction of the Principal's Representative and decision by the Adjudicator; and

(d) grant all legal, equitable and statutory remedies."

16 Clause 35.13 provided that cl 35 would survive termination of the contract.

17 Clause 35.14 provided for the continuation of the work under the contract despite the existence of a dispute between the parties.

18 Clause 2.2 of the General Conditions of Contract was an interpretation provision, which provided that unless the context indicated a contrary intention headings were for convenience only and did not affect interpretation.

19 Clause 2.14 dealt with severability in the following terms:

"**[2.14] Severability of Provisions**

If at any time any provision of this Contract is or becomes illegal, invalid or unenforceable in any respect under the law of any jurisdiction, that will not affect or impair:

(a) the legality, validity or enforceability in that jurisdiction of any other provision of this Contract; or

(b) the legality, validity or enforceability under the law of any other jurisdiction of that or any other provision of this Contract."

The issues

20 The parties were agreed that subcl 35.11(d), the mediation clause, was uncertain and unenforceable. The agreement of the respondent (Railcorp) to this proposition was based on the fact that the "Australian Dispute Centre" did not exist. The parties' agreement recorded by the primary judge at [5] in his reasons was that subcl 35.11(d) was "void for uncertainty."

21 United also asserted (and Railcorp denied) that subcl 35.11(c) was also uncertain and therefore void and unenforceable.

22 Most importantly, United asserted (and Railcorp denied) that cl 35.12 (providing for the reference to arbitration) was not severable from cl 35.11, such that in circumstances where subcl 35.11(d) or subcl 35.11(c) and (d) was or were void and unenforceable, cl 35.12 was likewise void and unenforceable. The result of this argument, if it were accepted, would be that any dispute will be justiciable in Court, where the power to send any dispute to a referee would be available. The consequences and commercial relevance of success of United's arguments were not explored.

The primary judge's decision

23 The primary judge (Rein J sitting in the Technology and Construction List of the Equity Division) rejected the arguments of United. His Honour found subcl 35.11(c) valid and enforceable. His Honour found cl 35.12 severable from the agreed voidness and unenforceability of subcl 35.11(d).

The primary judge's reasons and the arguments of the parties

24 As to the question of the certainty of subcl 35.11(c) the primary judge concluded by reference to various authorities, including in particular *Coal Cliff Collieries Pty Ltd v Sijehama Pty Ltd* (1991) 24 NSWSLR 1; *Burger King Corporation v Hungry Jacks Pty Ltd* [2001] NSWCA 187; 69 NSWLR 558; *Alcatel Australia Ltd v Scarcella* (1998) 44 NSWLR 349; and *Con Kallergis Pty Limited v Calshonie Pty Limited* (1998) 14 BCL 201 that the obligation to undertake genuine and good faith negotiations had sufficient content not to be uncertain.

25 As to the question of severability, the primary judge concluded (at [37] of his reasons) that it was not the intention of the parties that disputes would be referred to arbitration only if the negotiation and mediation clauses were valid. His Honour's reasoning was contained over the following eight pages and included reference to decisions at first instance of judges in the Commercial List. I intend no

disrespect to the thoughtful and careful reasons of the primary judge by not analysing those reasons. I agree with his Honour's conclusions, both as to the sufficient certainty and enforceability of subcl 35.11(c) and the severability of cl 35.12. In circumstances where there can be only one correct answer to a question (here legal questions as to the proper meaning and content of a provision of a contract and the severability of another provision based on the intention of the parties pursuant to the process of contractual construction and the application of legal reasoning) error or not in the primary judge's approach will be demonstrated in an appeal by way of rehearing by the appeal court considering the question for itself and reaching a different or the same conclusion.

26 Thus, it is essential for this Court to consider the questions for itself, assisted by the careful analysis of the primary judge.

27 The parties filed detailed and elaborate submissions subjecting the primary judge's reasoning and each other's submissions to minute analysis, often in the alternative. I have had careful regard to all the arguments. It would lengthen these reasons and make them more complex than is necessary if I were to analyse each strand of the parties' arguments. I propose to explain my reasons for my agreement with the conclusions of the primary judge and in so doing deal with the essential structure of the parties' arguments. Again, I intend no disrespect to the parties or their legal advisers in taking this course. Their submissions were of great assistance and I express my gratitude to them for their clarity and comprehensiveness.

Subclause 35.11(c) and good faith negotiations

28 The obligation on the parties in subcl 35.11(c) is to refer the dispute or difference to a senior representative of each party (a category of employee, agent or officer which no one said was uncertain). Those persons must meet and undertake negotiations. The qualification is that negotiations must be "genuine and good faith negotiations". Though the drafter used adjectives to describe the noun "negotiations", the meaning is clear that the obligation is upon the contracting parties to have their respective senior representatives negotiate genuinely and in good faith. The phrase is a composite one, each limb of it informing the other. I will come to its contents in due course.

29 The status of a clause purporting in terms to create a legal obligation to negotiate or to negotiate in a particular way, such as here – genuinely and in good faith and, in particular, whether such a clause is intended to be legally binding, and, if so whether it has a sufficiently certain content to be enforceable has been the subject of some debate in the common law world for some time.

History of the authorities

30 At a time when the common law of England, to a significant degree, determined the common law in Australia (see for example: *Public Transport Commission of NSW v J Murray-More (NSW) Pty Limited* [1975] HCA 28; 132 CLR 336 at 341 and 349 and the *Judiciary Act 1903* (Cth), s 80 (before its amendment in 1988 by the *Law and Justice Legislation Amendment Act* 1988 (Cth), s 41)) the views of the English Court of Appeal and the House of Lords were often decisive. This is not now the case, and has not been at least since 1986: *Cook v Cook* [1986] HCA 73; 162 CLR 376 at 389-390 and the *Australia Acts 1986* (Cth) and (UK). Foreign (including English) precedents are useful to the degree of persuasiveness of their reasoning.

31 In 1932, in *Hillas & Co Limited v Arcos Limited* [1932] All ER Rep 494 at 505-507; 38 Com Cas 23 at 39-43, Lord Wright expressed the view that a contract to negotiate was enforceable, saying (at 505 and 39-40):

> "There is then no bargain except to negotiate, and negotiations may be fruitless and end without any contract ensuing; yet even then in strict theory, there is a contract (if there is good consideration) to negotiate, though in the event of repudiation by one party the damages may be nominal, unless a jury think that the opportunity to negotiate was of some appreciable value to the injured party."

32 In *Carr v Brisbane City Council* [1956] St R (Qld) 403, Mansfield SPJ dealt with a clause of a indenture dealing with the engagement of the plaintiff for removal and disposal of night soil and dead animals. After providing for payment, the relevant clause provided that if the contractor's costs increased the Council "will be prepared to negotiate … with a view to making good to him any such increased cost …". Notwithstanding the dictum of Lord Wright, Mansfield SPJ refused to recognise certainty of content in the clause, saying at 411:

> "… as the words clearly envisage further negotiations between the parties, they deprive the clause of the certainty required by law for it to constitute the basis of an enforceable agreement."

33 In 1975, Lord Denning MR and Lord Diplock in *Courtney & Fairbairn Ltd v Tolaini Brothers (Hotels) Ltd* [1975] 1 WLR 297, in extempore judgments, expressed their blunt and forceful views that Lord Wright was wrong in *Hillas v Arcos*. Lord Denning MR said at 301-302:

> "That tentative opinion by Lord Wright does not seem to me to be well founded. If the law does not recognise a contract to enter into a contract (when there is a fundamental term yet to be agreed) it seems to me it cannot recognise a contract to negotiate. The reason is because it is too uncertain to have any binding force. No court could estimate the damages because no one can tell whether the negotiations would be successful or would fall through; or if successful, what the result would be. It seems to me that a contract to negotiate, like a contract to enter into a contract, is not a contract known to the law. We were referred to the recent decision of Brightman J about an option, *Mountford v Scott* [1933] 3 WLR 884: but that does not seem to me to touch this point. I think we must apply the general principle that when there is a fundamental matter left undecided and to be the subject of negotiation, there is no

> contract. So I would hold that there was not any enforceable agreement in the letters between the plaintiff and the defendants. I would allow the appeal accordingly."

Lord Diplock said at 302:

> "I agree and would only add my agreement that the dictum; for it is no more, of Lord Wright in *Hillas & Co Ltd v Arcos Ltd* ... to which Lord Denning MR has referred, though an attractive theory, should in my view be regarded as bad law."

Lawton LJ agreed with both Lord Denning MR and Lord Diplock.

34 In *Mallozzi v Carapelli SPA* [1976] 1 Lloyd's Rep 407, the Court of Appeal (Megaw LJ, Roskill LJ and Goff LJ) was concerned with two contracts for the sale of oats and maize under a London Corn Trade Association form. The contracts dealt with the discharging ports as safe ports on the west coast of Italy, excluding Genoa, "[f]irst or second port to be agreed between sellers and buyers on the ship passing the Straits of Gibraltar." At first instance, Kerr J, on 2 July 1974 (five months before judgment in *Courtney)* citing Lord Wright in *Hillas v Arcos* said at [1975] 1 Lloyds 229 at 249:

> "But it is in fact possible to give some effect to this provision. In my view, it means or at any rate includes an obligation to the effect that the parties must be at least bona fide negotiate with a view to trying to reach agreement."

The Court of Appeal applied *Courtney* in rejecting this conclusion of Kerr J (at 412-413 and 414-415 and 415). It is to be noted, however, that Goff LJ was careful to say (at 415) that the conclusion reached by him depended upon the construction of "this particular contract".

35 At times, *Courtney* was distinguished. In *The "Didymi"* [1988] 2 Lloyd's Rep 108, an aspect of cl 30 of the New York Produce Exchange time charter was said in argument to be unenforceable. Clause 30 provided for adjustment of hire (up or down) depending on how speed and fuel consumption varied from owner's representations. The variation to hire was to be "equitably [decreased/increased] by an amount to be mutually agreed between Owners and Charterers". Hobhouse J (at first instance) and the Court of Appeal (Dillon LJ, Nourse LJ and Bingham LJ) had no difficulty reading the agreement to agree as a matter of machinery to implement a sufficiently objective calculation – by reference to average performance, represented performance and contract hire.

36 At other times, it was squarely followed: *The "John S Darbyshire"* [1977] 2 Lloyd's Rep 457 at 466; *The "Scraptrade"* [1981] 2 Lloyd's Rep 425 at 432; *Voest Alpine v Chevron* [1987] 2 Lloyd's Rep 547 at 561; *The "Jing Hong Hai"* [1989] 2 Lloyd's Rep 522 at 526; and *Paul Smith Ltd v H & S International Holdings Inc* [1991] 2 Lloyd's Rep 127 at 131.

37 There was an exception, however, in *Donwin Productions Ltd v EMI Films Ltd* (Pain J, QBD Crown Office List unreported 2 March 1984), to which I will come.

38 In July 1991, the New South Wales Court of Appeal delivered judgment in *Coal Cliff Colieries Pty Ltd v Sijehama Pty Ltd*. The case concerned a heads of agreement about a proposed joint venture for a new coal mine on the south coast of New South Wales. The heads of agreement outlined the basis of the proposal for the development of the joint venture and the coal mine. The heads of agreement commenced with the following statement:

> "This document will serve to record the terms and conditions subject to and upon which Coal Cliff Collieries Pty Ltd, Sijehama and Bulli Main agree to associate themselves in an unincorporated joint venture … **The parties will forthwith proceed in good faith to consult together upon the formulation of a more comprehensive and detailed Joint Venture Agreement (and any associated agreements) which when approved and executed will take the place of these Heads of Agreement, but the action of the parties in so consulting and in negotiating on fresh or additional terms shall not in the meantime in any way prejudice the full and binding effect of what is now agreed**."
> (emphasis added)

39 Negotiations took place. Numerous drafts of the proposed joint venture were prepared, without agreement; further drafts of heads of agreement were prepared, again with no agreement. Negotiations of some intensity lasted 16 months. Thereafter, negotiations continued less intensively for some years until one party withdrew from the negotiations.

40 Kirby P, in discussing the principles of contract formation and agreements to negotiate, referred (at 21-22) to the considerable American academic discussion dealing with negotiation in good faith. As Kirby P noted, that discussion revealed a divergence of opinion about the proper role of the law in the enforcement of contracts to negotiate. Kirby P recognised that the courts will not enforce an agreement to agree: *Booker Industries Pty Ltd v Wilson Parking (Qld) Pty Ltd* [1982] HCA 53; 149 CLR 600 at 604. His Honour referred to the rejection by the English Court of Appeal in *Courtney* of the "flirtation" by Lord Wright in *Hillas v Arcos*; to the following of *Courtney* in *Mallozzi v Carapelli* and to the other considerations including those attending the development of American law. His Honour expressed the view that if parties have bound themselves expressly to negotiate in good faith they should be held to it, if circumstances otherwise did not reveal a lack of intention to contract or the circumstances revealed no lack of certainty of content. Kirby P said at 26:

> "… I do not share the opinion of the English Court of Appeal that no promise to negotiate in good faith would ever be enforced by a court. I reject the notion that such a contract is unknown to the law, whatever its term [sic: terms]. I agree with Lord Wright's speech in *Hillas* that, provided there was consideration for the promise, in some circumstance a promise to negotiate in good faith will be enforceable, depending upon its precise terms. Likewise I agree with Pain J in *Donwin* that, so long as the promise is clear and part of an undoubted agreement between the parties, the courts will not adopt a general principle that relief for the breach of such promise must be withheld."

41 The reference to Pain J in *Donwin Productions Ltd v EMI Films Ltd* was to a passage in that judgment where, after referring to *May and Butcher Ltd v The King* [1934] 2 KB 17(n) and on appeal [1929] All ER Rep 679 at 683 and *Courtney*, his Lordship said:

> "I think it would by necessary implication be a term of such a contract that the parties would negotiate in good faith about the further terms to be inserted in the written agreement. While this term was not expressed it is plain from the conduct of the negotiations that it was the intention of the parties that this should be done. I am not overlooking the decision in *Courtney* … that the law does not recognise a contract to negotiate. But I do not think that decision prevents the implication of such a term as I have suggested once a firm agreement has been made and a further fuller agreement is in contemplation."

42 Kirby P continued at 26-27 as follows:

> "… I believe that the proper approach to be taken in each case depends upon the construction of the particular contract: see *Australia & New Zealand Banking Group Ltd v Frost Holdings Pty Ltd* [1989] VR 695; see note (1991) 65 ALJ 59. In many contracts it will be plain that the promise to negotiate is intended to be a binding legal obligation to which the parties should then be held. The clearest illustration of this class will be cases where an identified third party has been given the power to settle ambiguities and uncertainties: see *Foster v Wheeler* (1888) LR 38 Ch D 130; *Axelsen v O'Brien* (1949) 80 CLR 219 and *Biotechnology Australia Pty Ltd v Pace* [(1998) 15 NSWLR 130] (at 136). But even in such cases, the court may regard the failure to reach agreement on a particular term as such that the agreement should be classed as illusory or unacceptably uncertain: *Godecke v Kirwan* (at 646f) and *Whitlock v Brew* (1968) 118 CLR 445 at 456. In that event, the court will not enforce the arrangement.
>
> In a small number of cases, by reference to a readily ascertainable external standard, the court may be able to add flesh to a provision which is otherwise unacceptably vague or uncertain or apparently illusory: see, eg, *Powell v Jones* [1968] SASR 394 at 399; *Sweet and Maxwell Ltd v Universal News Services Ltd* [1964] 2 QB 699; cf *Meehan v Jones* (1982) 149 CLR 571 at 589; *Jillcy Film Enterprises* [593 F Supp 515 (1984)] (at 521); *Ridgeway Coal Co* [616 F Supp 404 (1985)] (at 408).
>
> Finally, in many cases, the promise to negotiate in good faith will occur in the context of an 'arrangement' (to use a neutral term) which by its nature, purpose, context, other provisions or otherwise makes it clear that 'the promise is too illusory or too vague and uncertain to be enforceable': see McHugh JA in *Biotechnology* (at 156) and *Adaras Development Ltd v Marcona Corporation* [1975] 1 NZLR 324 at 331."

43 I do not take these expressions of elucidation and qualification by Kirby P to be intended as a complete and self-contained code for application. Some of the submissions of United can be read as submitting that his Honour was intending such. His Honour, if I may respectfully put it this way, was cautiously, but decidedly, putting the view that an agreement to negotiate in good faith might be enforceable, depending on its terms and context. Kirby P was dealing with, if I may say so, the blunt, uncompromising and generally expressed views of Lord Denning and Lord Diplock in *Courtney*. His Honour was not stating an all encompassing generalised test or formula.

44 In the contract before the Court in *Coal Cliff*, Kirby P was of the view that the promise in the heads of agreement was too vague, illusory, and uncertain to be enforceable. The essential reasoning of his Honour was expressed succinctly at 27 as follows:

> "The review of the considerations which lead me to this conclusion has already been stated. This was not a case where an external arbitrator was nominated to resolve outstanding differences. There were many such differences at the time of the heads of agreement and a number remain even three years later when negotiations were finally broken off. A court would be extremely ill-equipped to fill the remaining blank spaces and to resolve questions which three years of painful negotiation between the solicitors for the parties had failed to

remove. A court could not, in this case, appeal to objective standards or to its own experience— as it might in filling a blank space in a lease of domestic premises or a contract less complex and more familiar than one for a major mining development. At stake are commercial decisions involving adjustments which would contemplate binding the parties for years and deciding issues that lie well beyond the expertise of a court. How mining executives, attending to the interests of their corporation and its shareholders might act in negotiating such a complex transaction is quite unknowable. Therefore, although I agree with Clarke J that some contracts to negotiate in good faith may be enforced by our law, this was not such a contract. I repeat the caution which I have expressed elsewhere (as I did in *Biotechnology Australia Pty Ltd v Pace*) that courts should hold back from giving effect to arrangements which the parties have not concluded, at least in circumstances such as the present. In *Austotel Pty Ltd v Franklins Selfserve Pty Ltd* (1989) 16 NSWLR 582 at 587, I said in words which, adapted, apply here:

> '… Doubtless, there will be cases where expedients must be adopted by a court in order to give effect to its conclusion that [the law] requires relief, but it strikes me as astonishing, in a multi-million dollar transaction designed to last for many years which substantial and well-advised parties have held back from completing, that a court should step in and determine so crucial and disputable an element in the parties' commercial relationship … and then to require the parties (one of whom is resisting) to proceed … with all the opportunities for friction and variation in the ongoing relationship which [that course] entails.'"

45 Handley JA approached the matter quite differently to Kirby P. His Honour saw an agreement to negotiate in good faith as necessarily illusory, saying at 41-42:

> "The existence or otherwise of good faith is relevant for many legal purposes. A familiar example is that fiduciary powers must be exercised in good faith. Good faith also defines the content of a duty imposed by law on parties negotiating for contracts of insurance. The High Court has held that a contract that is subject to the purchaser obtaining satisfactory finance is not uncertain even if a purchaser who relies upon the condition need only act honestly: see *Meehan v Jones*. In that case Gibbs CJ (at 578-579) referred to the well-known statement by Bowen LJ that 'the state of a man's mind is as much a fact as the state of his digestion'.
>
> In many cases the question of good faith arises in the context of an existing relationship which gives content and certainty to the issues which the court is called upon to decide: see *Hospital Products Ltd v United States Surgical Corporation* [(1984) 156 CLR 41] (at 137-138). In other cases the question relates solely to the knowledge and beliefs of one party to a transaction, for example, the question of bona fide purchase.
>
> Parties negotiating for a contract are free to pursue their own interests as they see fit. Within broad limits each is under no legal duty to consider the interests of the other. The parties are subject to the universal duty of honesty, any duty arising from a fiduciary or *Hedley Byrne* relationship [*Hedley Byrne & Co Ltd v Heller & Partners Ltd* [1964] AC 465], and statutory provisions such as s 52 of the *Trade Practices Act* 1974 (Cth). Common law and equity have taken a realistic and practical approach. Laudatory statements are not treated as representations and neither party is under a general duty of disclosure. The parties are considered to be dealing with each other at arm's length: see *Keith Henry & Co Pty Ltd v Stuart Walker & Co Pty Ltd* (1958) 100 CLR 342 at 351.
>
> Negotiations are conducted at the discretion of the parties. They may withdraw or continue; accept, counter offer or reject; compromise or refuse, trade-off concessions on one matter for gains on another and be as unwilling, willing or anxious and as fast or as slow as they think fit.
>
> To my mind these considerations demonstrate that a promise to negotiate in good faith is illusory and therefore cannot be binding."

46 (Handley JA then referred to *Beattie v Fine* [1925] VLR 363 and *Loftus v Roberts* (1902) 18 TLR 532 which were approved by the majority in *Placer Development Limited v Commonwealth* [1969] HCA 29; 121 CLR 353 at 356 and 360-361.) Handley JA continued at 43:

> "There are no identifiable criteria by which the content of the obligation to negotiate in good faith can be determined. This is left to the discretion of the parties. A court could determine whether some step in the negotiations had been taken in bad faith. However this does not define or even provide guidance as to the content of the obligation at any particular stage. I do not see how a court can say that good faith required a particular offer to be accepted or a particular counter offer to be made.
>
> The negotiations could be lengthy and in the result, as we know, they lasted four years. During such an extended period the circumstances of the parties and the economic climate could significantly change. A proposed joint venture which appeared attractive to both parties in 1981 may, in all good faith, have been assessed quite differently four years later. I cannot think that an obligation to negotiate in good faith would oblige the parties to leave out of account the effect of subsequent developments.
>
> In all the circumstances in my opinion the content of the promise was uncertain and the promise itself illusory. In my opinion the question should be decided by this Court in accordance with principles which are well established in English and Australian Law and are binding on this Court. Accordingly there is no need for me to consider the United States materials and the academic writings to which we were referred. In my opinion the promise to negotiate in good faith in the heads of agreement was not enforceable and was binding only in honour."

47 Waddell AJA agreed "generally" with the reasons of Kirby P.

48 Five months after *Coal Cliff* was handed down, argument took place in the House of Lords in *Walford v Miles* [1992] 2 AC 128. Judgment in *Walford v Miles* was delivered in January 1992. The case concerned a so-called "lock out" agreement in which one party agreed to terminate negotiations with a third party in return for a promise by the other to continue negotiations and that that comprised a completed collateral agreement to another agreement that was "subject to contract". Lord Ackner delivered the leading speech with which Lord Keith of Kinkel, Lord Goff of Chieveley, Lord Jauncey of Tullichettle and Lord Browne-Wilkinson agreed. Reference was made to United States' authority and in particular *Channel Home Centers, Division of Grace Retail Corporation v Grossman* 795 F 2d 291 (3rd Cir. 1986). Lord Ackner in dealing with *Channel Home* said at 138:

> "… While accepting that an agreement to agree is not an enforceable contract, the Court of Appeal [sic] appears to have proceeded on the basis that an agreement to negotiate in good faith is synonymous with an agreement to use best endeavours and, as the latter is enforceable, so is the former. This appears to me, with respect, to be an unsustainable proposition. The reason why an agreement to negotiate, like an agreement to agree, is unenforceable is simply because it lacks the necessary certainty. The same does not apply to an agreement to use best endeavours. This uncertainty is demonstrated in the instant case by the provision which it is said has to be implied in the agreement for the determination of the negotiations. How can a court be expected to decide whether, *subjectively*, a proper reason existed for the termination of negotiations? The answer suggested depends upon whether the negotiations have been determined 'in good faith'. However, the concept of a duty to carry on negotiations in good faith is inherently repugnant to the adversarial position of the parties when involved in negotiations. Each party to the negotiations is entitled to pursue his (or her) own interest, so long as he avoids making misrepresentations. To advance that interest he must be entitled, if

> he thinks it appropriate, to threaten to withdraw from further negotiations or to withdraw in fact in the hope that the opposite party may seek to reopen the negotiations by offering him improved terms. Mr Naughton, of course, accepts that the agreement upon which he relies does not contain a duty to complete the negotiations. But that still leaves the vital question - how is a vendor ever to know that he is entitled to withdraw from further negotiations? How is the court to police such an 'agreement'? A duty to negotiate in good faith is as unworkable in practice as it is inherently inconsistent with the position of a negotiating party. It is here that the uncertainty lies. In my judgment, while negotiations are in existence either party is entitled to withdraw from these negotiations, at any time and for any reason. There can be thus no obligation to continue to negotiate until there is a 'proper reason' to withdraw. Accordingly, a bare agreement to negotiate has no legal content.

Coal Cliff was not referred to.

49 In March 1992, in *Trawl Industries of Australia Pty Ltd v Effem Foods Pty Ltd* (1992) 27 NSWLR 326, the Court of Appeal (Kirby P, Samuels JA and Clarke JA) dealt with the topic of uncertainty of contracts. Kirby P referred to *Coal Cliff*. Samuels JA said the following at 343:

> "However, as I have observed, UBA's argument on the appeal was not that the contract was uncertain, but, I infer, that it was incomplete, and a contract that is incomplete is one that requires further agreement; or, in the present case, subsequent negotiation. In *Courtney*, as I have said, such a contract was said to go unrecognised by the law and the dictum to the contrary effect of Lord Wright, in *Hillas & Co, Ltd v Arcos, Ltd* [1932] All ER Rep 494 at 504; (1932) 147 LT 503 at 515; 38 Com Cas 23 at 37, was disapproved. However, following *Coal Cliff Collieries*, the law in New South Wales is presumably that the English Court of Appeal was wrong and Lord Wright was correct, and that in certain circumstances the law will recognise an agreement to negotiate; although what was said by a majority of the High Court (with whom Brennan J agreed) in *Booker Industries Pty Ltd v Wilson Parking (Qld) Pty Ltd* (1982) 149 CLR 600 at 604 seems not to be wholly consistent with that conclusion. Their Honours said:
>
> > 'It is established by authority, both ancient and modern, that the courts will not lend their aid to the enforcement of an incomplete agreement, being no more than an agreement of the parties to agree at some time in the future. Consequently, if the lease provided for a renewal 'at a rental to be agreed' there would clearly be no enforceable agreement.'
>
> In Greig and Davis, *The Law of Contract*, [(1987)] at 355-356, the learned authors distinguish uncertainty and incompleteness, while recognising that a particular clause in a contract may in certain circumstances be both uncertain and raise a question of incompleteness, a proposition of which *Scammell (G) and Nephew, Ltd v Ouston* [1941] AC 251 is an example. In my view, the pricing formula was neither uncertain nor incomplete. That is, it goes nowhere near satisfying Barwick CJ's test for uncertainty and does not leave anything to be determined by dint of some formula or machinery lacking in the terms of the contract itself."

Walford v Miles was not referred to.

50 In *Trawl*, Samuels JA made the valuable point (by reference to the learned authors, Greig and Davis in their text *The Law of Contract*) that uncertainty and incompleteness were different concepts. I agree. Samuels JA also considered that *Booker* may not be consistent with Kirby P's views in *Coal Cliff*. I disagree. *Booker* concerned incompleteness; *Coal Cliff* concerned uncertainty.

51 In 1994, in *Little v Courage Limited* (1994) 70 P & CR 469, the English Court of Appeal (the judgment of the Court being delivered by Millett LJ) applied *Walford v Miles* and stated (at 475-476) that English law does not recognise a pre-contractual duty to negotiate in good faith.

52 In 1998, in *Australis Media Holdings Pty Ltd v Telstra Corporation Ltd* (1998) 43 NSWLR 104 at 128, this Court (Mason P, Beazley JA and Stein JA) recognised that the House of Lords decision in *Walford v Miles* supported the approach of Handley JA, but made no further comment, other than to say no application was made to reconsider *Coal Cliff*.

53 Later that year, in *Healey v Commonwealth Bank of Australia* [1998] NSWCA 103, Giles JA (with whom Mason P and Fitzgerald AJA agreed) said that the law concerning an agreement to negotiate in good faith could not be regarded as settled, noting that the House of Lords in *Walford v Miles* had expressed views reflective of those of Handley JA in *Coal Cliff*.

54 In March 1997, the Court of Appeal of Victoria examined the question in *Con Kallergis Pty Limited v Calshonie Pty Limited* (Hayne JA, as his Honour then was, Charles JA and Callaway JA). The case concerned an agreement to negotiate. At 210-212 Hayne JA (with whom Charles JA agreed) discussed *Coal Cliff, Trawl, Courtney, Walford v Miles* and the decisions on the question up to that time: *Hooper Bailie Associated Ltd v Natcan Group Pty Ltd* (1992) 28 NSWLR 194 (Giles J); *Elizabeth Bay Developments Pty Ltd v Boral Building Services Pty Ltd* (1995) 36 NSWLR 709 (Giles J); *Smith & Smith v Nylex Corporation* [1994] A Contract Rep 90-048 (Prior, Olsson and Perry JJ). Hayne JA expressed the view that a contract to negotiate was not illusory and had sufficient certainty if there was a dispute resolution process that provided an end to the negotiation process. His Honour distinguished *Walford v Miles* on the basis that it was a case in which the parties could break off negotiations at any time. Hayne JA also said that the question is more complex than simple statements of it may suggest (implicitly referring to the kind of general statements contained in *Courtney* and *Walford v Miles) and* "the answer to the problem may vary according to the precise terms of the agreement". These propositions were generally in accordance with the views of Kirby P in *Coal Cliff.* In commenting on *Walford v Miles*, his Honour said at 212:

> "… Thus, even if *Walford v Miles* is to be regarded as good law in Australia (and there are indications in some of the authorities that I have mentioned that suggest there is at least room for doubt about the width of some of the propositions advanced in that case), I consider that on the assumptions I have mentioned the present contract does not suffer from the difficulties identified by their Lordships."

55 In New Zealand, the Court of Appeal in *Wellington City Council v Body Corporate 51702* (Wellington) [2002] 3 NZLR 486 considered the question of an agreement to negotiate. From 489 [10], Tipping J (delivering the judgment of the Court) examined *Coal Cliff, Walford v Miles, Courtney, Little v Courage* and the position in Canada which accorded with the English position. Tipping J summarised the New Zealand position at [30]-[34] as follows: that good faith, being a subjective concept, cannot give objective certainty to a purported obligation to negotiate in good faith; that *Walford v Miles* was

correct; but that there will be some "process contracts" (such as tenders) where a specific procedure is in issue that the Court can objectively determine; and that that is how Kirby P's views were to be accommodated with the English position, with which Tipping J essentially agreed.

Consideration of the proper approach

56 Before turning to the terms of the clause in question, given the juristic debate that has taken place about agreements to negotiate in good faith, it is helpful to begin with some essential propositions founded on accepted authority and principle. First, an agreement to agree is incomplete, lacking essential terms: *Booker* at 604. (That is not a question of uncertainty or vagueness, but the absence of essential terms.)

57 Secondly, the task of the Court is to give effect to business contracts where there is a meaning capable of being ascribed to a word or phrase or term or contract, ambiguity not being vagueness: *Upper Hunter County District Council v Australian Chilling and Freezing Co Limited* [1968] HCA 8; 118 CLR 429 at 436-437; *New Zealand Shipping Co Ltd v AM Satterthwaite & Co Ltd* [1975] AC 154 at 167; *Meehan v Jones* [1982] HCA 52; 149 CLR 571 at 589; and *Trawl Industries* at 332. (The commercial law should foster and support commercial practice, not fight it: see Devlin J writing extracurially "The Relation Between Commercial Law and Commercial Practice" (1951) 14 *Modern Law Review* 249.)

58 Thirdly, good faith is not a concept foreign to the common law, the law merchant or businessmen and women. It has been an underlying concept in the law merchant for centuries: L Trakman *The Law Merchant: The Evolution of Commercial Law* (Rothman 1983) at p 1; W Mitchell *An Essay on the Early History of the Law Merchant* (CUP 1904) at pp 102 ff. It is recognised as part of the law of performance of contracts in numerous sophisticated commercial jurisdictions: for example *Uniform Commercial Code* ss 1-201 and 1-203 (1977); *Wigand v Bachmann-Bechtel Brewing Co* 118 NE 618 at 619 (1918); *Farnsworth on Contracts* (3rd Ed) Vol 1 at pp 391-417 § 3.26b; *UNIDROIT Principles of International Commercial Contracts* (2004 Ed, Rome 2004) Art 1.7; R Zimmerman and S Whittaker *Good Faith in European Contract Law* (CUP 2000). It has been recognised by this Court to be part of the law of performance of contracts: *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234 at 263-270; *Hughes Bros Pty Ltd v Trustees of the Roman Catholic Church for the Archdiocese of Sydney* (1993) 31 NSWLR 91; *Burger King Corporation v Hungry Jack's Pty Ltd* at 565-574 [141]-[187]; and *Alcatel Australia Ltd v Scarcella* at 363-369. In *Alcatel* Sheller JA (with the express and unqualified agreement of Powell JA and Beazley JA) said the following at 369:

> "The decisions in *Renard Constructions* and *Hughes Bros* mean that in New South Wales a duty of good faith, both in performing obligations and exercising rights, may by implication be imposed upon parties as part of a contract. There is no reason why such a duty should not be implied as part of this lease."

59 There are other decisions of Australian courts and discussions by scholars recognising the obligation of good faith in a non-fiduciary context: see J Carter and E Peden "Good Faith in Australian Contract

Law" (2003) 19 *Journal of Contract Law* 155; Finn J writing extracurially "Good Faith and Fair Dealing: Australia" (2005) 11 New Zealand Business Law Quarterly 378; H Lucke "Good Faith and Contractual Performance" in P Finn (Ed) *Essays on Contract* (Law Book Company 1987) at p 155; *GEC Marconi Systems v BHP-IT* [2003] FCA 50; 128 FCR 1 at 208 [915] ff; *Hughes Aircraft Systems International v Airservices Australia* (1997) 146 ALR 1 at 36-37; *Far Horizons Pty Ltd v McDonald's Australia Ltd* [2000] VSC 310; *Garry Rogers Motors (Aust) Pty Ltd v Subaru (Aust) Pty Ltd* [1999] FCA 903; (1999) ATPR 41-703 at p 43,014 [34]-[35]; *Elfic Limited v Macks* [2000] QSC 18 at [109]; *Pacific Brands Sport & Leisure Pty Ltd v Underworks Pty Ltd* [2005] FCA 288; (2005) Aust Contract Reports 90-213; *Aiton Australia Pty Limited v Transfield Pty Limited* [1999] NSWSC 996; 153 FLR 236; *AMCI (IO) Pty Limited v Aquila Steel Pty Limited* [2009] QSC 139.

60 It is fair to say that caution (in some cases a lack of enthusiasm) has been expressed by some, for example: *Royal Botanic Gardens and Domain Trust v South Sydney City Council* [2002] HCA 5; 76 ALJR 436 at 445 [40], 452 [88] and 463 [155]; *Vodaphone Pacific Ltd v Mobile Innovations Ltd* [2004] NSWCA 15 at [183] ff; *Service Station Association Ltd v Berg Bennett & Associates Pty Ltd* (1993) 45 FCR 84 at 91-98; *NT Power Generation Pty Ltd v Power and Water Authority* [2001] FCA 334; 184 ALR 481 at 574; *Asia Television Ltd v Yau's Entertainment Pty Ltd* (2000) 48 IPR 283; *Central Exchange Ltd v Anaconda Nickel Ltd* [2001] WASC 128; 24 WAR 382 at 391-393 [16]-[22]; on appeal [2002] WASCA 94; 26 WAR 33 at 48-50 [45]-[55]; *Wenzel v ASX Ltd* [2002] FCAFC 400; 125 FCR 570 at 586-587 [80]-[81]; *Esso Australia Resources Pty Ltd v Southern Pacific Petroleum NL* [2005] VSCA 228; and *Jobern Pty Ltd v Break Free Resorts (Victoria) Pty Ltd* [2007] FCA 1066.

61 Whilst this necessarily incomplete review of authorities reveals that the law in Australia is not settled as to the place of good faith in the law of contracts, this Court should work from the position that it has said on at least three occasions (not including *Renard*) that good faith, in some degree or to some extent, is part of the law of performance of contracts. It is unnecessary to go beyond this proposition to gain assistance in the construction of this particular clause of this contract. Many issues arise in respect of any implication (whether as a matter of fact or by law) of any term requiring performance of a contract, or the exercise of contractual rights, in good faith. Those issues need not be explored here in a case dealing with an express clause as part of a dispute resolution clause.

62 Whilst there is some doubt as to the extent of concurrence of Waddell AJA in *Coal Cliff* (see the use of the word "generally"), nevertheless the considered reasons of Kirby P with which Waddell AJA agreed (generally) conform to the general approach taken by the Court in *Hughes, Alcatel* and *Burger King* and by the Victorian Court of Appeal in *Con Kallergis*.

63 Further, in my view, Kirby P's reasons are more persuasive than the competing authority. I say this with the utmost respect to those who have expressed a contrary view and recognising that the issue is one that has produced different expressions of view among great commercial judges on appeal: for example, Lord Wright, Lord Denning, Lord Diplock, Kirby P and Handley JA and among highly

experienced commercial judges at first instance in this Court: Clarke J, Giles J, Einstein J and Hammerschlag J.

64 I turn to the major contrary appellate decisions. In relation to *Courtney*, the reasoning of Lord Denning MR equated an agreement to negotiate with an agreement to agree. The latter is, of course, not enforceable: *Booker* at 604 (Gibbs CJ, Murphy J and Wilson J), as Kirby P recognised in *Coal Cliff*. It does not follow, however, that an agreement to undertake negotiations in good faith fails for the same reason. An agreement to agree to another agreement may be incomplete if it lacks essential terms of the future bargain. An agreement to negotiate, if viewed as an agreement to behave in a particular way may be uncertain, but is not incomplete. The objection that no court could estimate the damages because no one could tell whether the negotiations "would be" successful ignores the availability of damages for the loss of a bargained for valuable commercial opportunity: *Chaplin v Hicks* [1911] 2 KB 786; *Sellars v Adelaide Petroleum NL* [1994] HCA 4; 179 CLR 332 at 349 ff. The relevant question is whether the clause has certain content.

65 Nor, with respect, do I find the views of Lord Ackner in *Walford v Miles* persuasive. An obligation to undertake discussions about a subject in an honest and genuine attempt to reach an identified result is not incomplete. It may be referable to a standard concerned with conduct assessed by subjective standards, but that does not make the standard or compliance with the standard impossible of assessment. Honesty is such a standard: cf *Royal Brunei Airlines Sdn Bhd v Tan* [1995] 2 AC 378 and *Twinsectra Ltd v Yardley* [2002] UKHL 12; [2002] 2 AC 164. Whether it is capable of assessment depends on whether there is a standard of behaviour that is capable of having legal content. Asserting its uncertainty does not answer the question. The assertion that each party has an unfettered right to have regard to any of its own interests on any basis begs the question as to what constraint the party may have imposed on itself by freely entering into a given contract. If what is required by the voluntarily assumed constraint is that a party negotiate honestly and genuinely with a view to resolution of a dispute with fidelity to the bargain, there is no inherent inconsistency with negotiation, so constrained. To say, as Lord Ackner did, that a party is entitled not to continue with, or withdraw from, negotiations at any time and for any reason assumes that there is no relevant constraint on the negotiation or the manner of its conduct by the bargain that has been freely entered into. Here, the restraint is a requirement to meet and engage in genuine and good faith negotiations. For the reasons expressed below that expression has, in the context of this contract, legal content.

66 Of course, it must be that the certainty and content of any contract will depend on its specific terms and context. Sweeping generalised rules, however, are difficult to sustain and not of great assistance.

67 In the way I have expressed my understanding of them, I respectfully agree with the statements of principle by Kirby P in *Coal Cliff*. I do not consider that they should be construed (indeed, marginalised) in the way suggested by Tipping J in *Wellington City Council*.

68 In *Coal Cliff*, Handley JA said that any promise to negotiate in good faith is illusory because negotiations are entirely discretionary in their continuance, withdrawal from them and the offers, acceptances, concessions and trade-offs that are involved. This was one of the aspects of Lord Ackner's views with which I have dealt. Handley JA referred to *Beattie v Fine* and *Loftus v Roberts* which were referred to and approved in *Placer Development Ltd v Commonwealth* at 356 and 360-361. *Beattie* was a case of an incomplete contract with "rental to be agreed by the lessor". This gave one party a discretion to fix the consideration. *Loftus v Roberts* concerned an agreement to agree. *Placer* concerned consideration determined by one party. These cases are left untouched by the proposition that a negotiating process can be constrained by an obligation on a party to conduct itself in good faith.

69 It is unnecessary to express any opinion on the facts and the application of principle to the facts in *Coal Cliff*. Suffice it to say that despite the views of such an experienced commercial judge as Clarke J (the trial judge in *Coal Cliff*) that the clause did not lack certainty, there is force in the conclusions of Kirby P, given the open-ended nature of the operation of the obligation in that case; although, given the sophistication of the parties and their clearly expressed views, one could view many of the matters referred to by Kirby P as affecting breach or proof of breach, rather than legal content of the contractual obligation. It is also unnecessary to consider, in the abstract, a clause providing for good faith negotiations in bringing about a commercial agreement in the first instance. The concern in the present case is the express mutual promises of the parties to undertake genuine and good faith negotiations to resolve disputes arising from performance of a fixed body of contractual rights and obligations. The difference is of great importance.

70 What the phrase "good faith" signifies in any particular context and contract will depend on that context and that contract. A number of things, however, can be said as to the place of good faith in the operation of the common law in Australia. The phrase does not, by its terms, necessarily import, or presumptively introduce, notions of fiduciary obligation familiar in equity or the law of trusts. Nor does it necessarily import any notion or requirement to act in the interests of the other party to the contract. The content and context here is a clearly worded dispute resolution clause of an engineering contract. It is to be anticipated at the time of entry into the contract that disputes and differences that may arise will be anchored to a finite body of rights and obligations capable of ascertainment and resolution by the chosen arbitral process (or, indeed, if the parties chose, by the Court). The negotiations (being the course of treaty or discussion) with a view to resolving the dispute will be anticipated not to be open-ended about a myriad of commercial interests to be bargained for from a self-interested perspective (as in *Coal Cliff*). Rather, they will be anticipated to involve or comprise a discussion of rights, entitlements and obligations said by the parties to arise from a finite and fixed legal framework about acts or omissions that will be said to have happened or not happened. The aim of the negotiations will be anticipated to be to resolve a dispute about an existing bargain and its performance. Honest and genuine differences of opinion may attend the parties' views of their rights and obligations. Such things as difficulties of proof and uncertainty as to fact or law may perfectly legitimately strike the parties differently. That accepted, honest business people who approach a

dispute about an existing contract will often be able to settle it. This requires an honest and genuine attempt to resolve differences by discussion and, if thought to be reasonable and appropriate, by compromise, in the context of showing a faithfulness and fidelity to the existing bargain.

71 The phrase "genuine and good faith" in cl 35.11 is, as I have said, a composite phrase. It is a phrase concerning an obligation to behave in a particular way in the conduct of an essentially self-interested commercial activity: the negotiation of a resolution of a commercial dispute. Given that context, the content of the phrase involves the notions of honesty and genuineness. Whilst the activity is of a self-interested character, the parties have not left its conduct unconstrained. They have promised to undertake negotiations in a genuine and good faith manner for a limited period (14 days). As a matter of language, the phrase "genuine and good faith" in this context needs little explication: it connotes an honest and genuine approach to the task. This task, rooted as it is in the existing bargain, carries with it an honest and genuine commitment to the bargain (fidelity to the bargain) and to the process of negotiation for the designated purpose.

72 The notion of fidelity to the bargain can be seen as founded, at least in part, on the requirement of a party to do all things necessary to enable the other party to have the benefit of the contract: *Butt v McDonald* (1896) 7 QLJ 68 at 70-71, approved in *Secured Income Real Estate (Australia) Limited v St Martins Investments Pty Limited* [1979] HCA 51; 144 CLR 596 at 607 and upon the recognition that contractual obligations do not set up a choice or election to perform or pay damages: cf *United States Surgical Corporation v Hospital Products International Pty Limited* [1982] 2 NSWLR 766 at 800 in the discussion of New York law and the effect of the *Restatement of the Law: Contracts* (2d) by McLelland J (as he then was). Contractual promises (supported by consideration) comprise legal rights to performance: *Ahmed Angullia Bin Hadjee Mohamed Salleh Angullia v Estate and Trust Agencies (1927) Ltd* [1938] AC 624 at 634-635 and *Coulls v Bagot's Executor and Trustee Company Limited* [1967] HCA 3; 119 CLR 460 at 504. The encompassing of fidelity to the bargain within the concept of good faith, at least in the context at hand – the genuine and good faith negotiation of an existing dispute by reference to an existing contract — does no violence to the language used here by the parties. That the phrase "good faith" contains the notion of fidelity (or faithfulness) to the bargain conforms with what other jurisdictions have seen as the core of the concept and with historical uses of the phrase: H Lucke *op cit* at 161 ff. Most importantly, its strength lies in its closeness to the contractual jurisprudence of the common law (*Secured Income*) and the appreciation that the parties have expressly bound themselves to a good faith standard in seeking to resolve a dispute arising from an existing bargain about the resolution of which dispute they anticipate having different views. The parties have mutually agreed to bring an approach of genuineness and good faith to that process of seeking resolution of any such disagreement. That agreement carried with it, in ordinary language, a requirement to bring an honestly held and genuine belief about their mutual rights and obligations and about the controversy to the negotiations, and to negotiate by reference to such beliefs.

73 These are not empty obligations; nor do they represent empty rhetoric. An honest and genuine approach to settling a contractual dispute, giving fidelity to the existing bargain, does constrain a party. The constraint arises from the bargain the parties have willingly entered into. It requires the honest and genuine assessment of rights and obligations and it requires that a party negotiate by reference to such. A party, for instance, may well not be entitled to threaten a future breach of contract in order to bargain for a lower settlement sum than it genuinely recognises as due. That would not, in all likelihood, reflect a fidelilty to the bargain. A party would not be entitled to pretend to negotiate, having decided not to settle what is recognised to be a good claim, in order to drive the other party into an expensive arbitration that it believes the other party cannot afford. If a party recognises, without qualification, that a claim or some material part of it is due, fidelity to the bargain may well require its payment. That, however, is only to say that a party should perform what it knows, without qualification, to be its obligations under a contract. Nothing in cl 35.11 prevents a party, not under such a clear appreciation of its position, from vindicating its position by self-interested discussion as long as it is proceeding by reference to an honest and genuine assessment of its rights and obligations. It is not appropriate to multiply examples. It is sufficient to say that the standard required by the notion of genuineness and good faith within a process of otherwise tactical and self-interested behaviour (negotiation) is rooted in the honest and genuine views of the parties about their existing bargain and the controversy that has arisen in connection with it within the limits of a clause such as cl 35.1.

74 With respect to those who assert to the contrary, a promise to negotiate (that is to treat and discuss) genuinely and in good faith with a view to resolving claims to entitlement by reference to a known body of rights and obligations, in a manner that respects the respective contractual rights of the parties, giving due allowance for honest and genuinely held views about those pre-existing rights is not vague, illusory or uncertain. It may be comprised of wide notions difficult to falsify. However, a business person, an arbitrator or a judge may well be able to identify some conduct (if it exists) which departs from the contractual norm that the parties have agreed, even if doubt may attend other conduct. If business people are prepared in the exercise of their commercial judgement to constrain themselves by reference to express words that are broad and general, but which have sensible and ascribable meaning, the task of the Court is to give effect to, and not to impede, such solemn express contractual provisions. It may well be that it will be difficult, in any given case, to conclude that a party has not undertaken an honest and genuine attempt to settle a dispute exhibiting a fidelity to the existing bargain. In other cases, however, such a conclusion might be blindingly obvious. Uncertainty of proof, however, does not mean that this is not a real obligation with real content.

75 With respect, to the extent that the judgments of Giles J in *Hooper Bailie Associated v Nation Group Pty Ltd* and *Elizabeth Bay Developments* and of Hammerschlag J in *Laing O'Rourke v Transport Infrastructure* [2007] NSWSC 723 are to the contrary of these conclusions, I respectfully cannot agree with them.

76 In *Hooper Bailie* and *Elizabeth Bay Developments*, Giles J saw as crucial to his view that an obligation to negotiate in good faith was uncertain the "necessary tension between negotiation, in which a party is free to, and may be expected to, have regard to self-interest rather than the interests of the other party, and the maintenance of good faith": see *Hooper Bailie* at 209 and *Elizabeth Bay Developments* at 716. This was similar to the consideration that influenced Lord Ackner in *Walford v Miles.* I do not agree that the posited contradistinction exists, at least in a clause such as the present. First, the obligation to undertake genuine and good faith negotiations does not require any step to advance the interests of the other party. The process is the self-interested one of negotiation. Secondly, there is, however, a constraint on the negotiation, though this constraint is not one to advance the interest of the other party. Rather, it is a (voluntarily assumed) requirement to take self-interested steps in negotiation by reference to the genuine and honest conception of the pre-existing bargain, including the rights and obligations therefrom and of the facts said to comprise the controversy. Within that constraint of those genuinely and honestly held beliefs as to the bargain, the required behaviour is genuine and good faith negotiations with a view to settlement or compromise.

77 In *Laing v O'Rourke*, Hammerschlag J followed Handley JA in *Coal Cliff* and Giles J in *Elizabeth Bay Developments* on the basis that they exhibited the correct legal approach. With respect, I disagree. Hammerschlag J said at [50]:

> "It is not the tension between negotiation and good faith that is the lynch pin in the argument, it is the absence of an objective yardstick by which to measure the good faith or otherwise of a negotiating party's stance. An appropriate (and indeed often effective) negotiating strategy may be a refusal to negotiate."

I disagree that there is no yardstick. The yardstick is honest and genuine negotiation, within the framework of fidelity to the bargain and the posited controversy. If, by "refusal to negotiate", his Honour meant not undertaking negotiations, it is to be recognised that the parties, here, have agreed that they will "meet and undertake genuine and good faith negotiations". How a party does that, and whether it has done it, will be a question of fact. It is not necessarily helpful to point to hypotheses outside a real factual example. Once one appreciates that the content of such a clause, in the framework of existing legal obligations, includes fidelity to the existing bargain, including the clause itself, the constraint that a party has taken on by the voluntary and willing entry into the contract is that it is free to pursue its own interests in negotiation, but by reference the honest and genuine appreciation of the rights and entitlements arising out of the relationship and touching the controversy.

78 This is a dispute resolution clause. To require in such a clause this degree of constraint on the positions of the parties reflects developments in dispute resolution generally. The recognition of the important public policy in the interests of the efficient use of public and private resources and the promotion of the private interests of members of the public and the commercial community in the efficient conduct of dispute resolution in litigation, mediation and arbitration in a fair, speedy and cost efficient manner attends all aspects of dispute resolution: cf "just, quick and cheap resolution of the real issues": *Civil*

Procedure Act 2005 (NSW), s 56. Parties are expected to co-operate with each other in the isolation of real issues for litigation and to deal with each other in litigation in court in a manner requiring co-operation, clarity and disclosure: see for example *Baulderstone Hornibrook Engineering Pty Ltd v Gordian Runoff Limited* [2008] NSWCA 243 at [160]-[165] and *Bellevarde Constructions Pty Ltd v CPC Energy Pty Ltd* [2008] NSWCA 228 at [55]-[56]. As part of its procedure, the Court can order mediation: *Civil Procedure Act*, s 26. Section 27 of that Act states that it is the duty of each party to the proceedings that have been referred to mediation to participate "in good faith" in the mediation. Costs sanctions can attend this duty cf *Capolingua v Phylum Pty Ltd* (1991) 5 WAR 137.

79 The contract here is, of course, not one governed by the *Civil Procedure Act*. It is, however, a modern contract with a sophisticated and detailed dispute resolution clause seeking to employ various tools to resolve disputes. The definition of "Law" in cl 2.2 makes clear that the law of New South Wales (and, implicitly, the common law of Australia) is the proper law of the contract. One of the available tools of dispute resolution is the obligation to engage in negotiations in a manner reflective of modern dispute resolution approaches and techniques – to negotiate genuinely and in good faith, with a fidelity to the bargain and to the rights and obligations it has produced within the framework of the controversy. This is a reflection, or echo, of the duty, if the matter were to be litigated in court, to exercise a degree of co-operation to isolate issues for trial that are genuinely in dispute and to resolve them as speedily and efficiently as possible.

80 The public policy in promoting efficient dispute resolution, especially commercial dispute resolution, requires that, where possible, real and enforceable content be given to clauses such as cll 35.11 and 35.12 to encourage approaches by, and attitudes of, parties conducive to the resolution of disputes without expensive litigation, arbitral or curial.

81 The business people here chose words to describe the kind of negotiations they wanted to undertake, "genuine and good faith negotiations", meaning here honest and genuine with a fidelity to the bargain. That should be enforced. In my view, subcl 35.11(c) was not uncertain and had identifiable content.

82 Nothing in these reasons goes beyond, in my view, the proper role of an intermediate appellate court. The reasons are an explication of the views of Kirby P and Waddell AJA in *Coal Cliff* delivered in 1992 and reflected in related contexts in later Court of Appeal judgments.

Severance

83 Before examining the text of cl 35.12, it is necessary to make some comments about subcl 35.11(d). The reference to mediation is short and lacking detail. No detailed procedure was set down. If the relevant organisation had existed, it may well have had its own procedures. Nevertheless, the reference of a dispute to an organisation for mediation does not guarantee that a mediation will take place. This lack of specificity may be seen to be important when one comes to construing cl 35.12.

84 United submitted that the word "or" where it first appears in cl 35.12 created an ambiguity. This is so, it was submitted, because the reference to mediation in subcl 35.11(d) is mandatory. The primary judge (at [33] of his reasons) appeared to accept this submission.

85 United submitted that the ambiguity is fundamental at paras 18 and 19 of its submissions:

> "18. There are three possible responses to this ambiguity:
>
> (a) It is insufficiently clear what intention the parties had as to how the conflict between cl 35.11(d) and the first part of the disjunctive in cl 35.12 should be resolved. This is the appellant's primary submission;
>
> (b) If a sufficient intention can be discerned, or if it is obvious that an unintended absurdity has occurred justifying judicial interference:
>
> (i) the '*or*' should be read as '*and*' and the first part of the disjunctive should therefore be treated as otiose and merely prefatory or repetitive, so that it does not alter the balance of Clause 35.12 and is not in conflict with 35.11(d);
>
> (ii) an alternative path to the same result may be to delete the whole of the first part of the disjunctive and the '*or*'.
>
> 19. By whatever route is followed, Clause 35.12 is either invalid or should be construed as to provide for arbitration *conditional* on (at least) prior reference to mediation failing to resolve the dispute within the specified period. This is just as much a condition of arbitration as the giving of a notice referring the matter to arbitration (cf *PMT Partners (In Liq) v Australian National Parks and Wildlife Service* (1995) 184 CLR 301, 313, 323). Indeed, the express terms of both Clause 35.10 ('*arbitration in accordance with the following clauses*') and 35.12 (*'If ... where ...')* emphasise that prior mediation is a condition of arbitration."

86 There is no doubt that in the process of construction of a document words "may be supplied, omitted or corrected … where it is clearly necessary in order to avoid absurdity or inconsistency": *Fitzgerald v Masters* [1956] HCA 53; 95 CLR 420 at 426-427; see also *Homburg Houtimport B V v Agrosin Private Ltd* [2003] UKHL 12; [2004] 1 AC 715 at 741 [23] and 748 [53].

87 It is not certain that a mediation referred under subcl 35.11(d) will either take place or be successful. If referred to a body for mediation (the content of the obligation), that mediation may or may not take place. There is no default machinery. In these circumstances it may be that "or" is appropriate. In other circumstances, both negotiations and a mediation under subcll 35.11(c) and (d) may have taken place, in which case "and" may be more appropriate. Given the text of subcl 35.11(d) and the lack of detailed provision for the conduct of the mediation if the reference for some reason has a difficulty (in contradistinction to subcl 35.2(b)), the most sensible construction and one that gives operative flexibility to cl 35.12 is to view "or" as encompassing "or" and "and", that is the disjunctive and conjunctive "and/or". This approach eschews "subtleties and niceties" in a business document, which

should be given operation by the application of common sense: *Hamilton v Mendes* (1761) 2 Burr 1198 at 1214; 97 ER 787 at 795 (Lord Mansfield); *Glynn v Margetson* [1893] AC 351 at 359 (Lord Halsbury LC); and *Homburg Houtimport* at 737 [10] (Lord Bingham of Cornhill).

88 Thus read, no question of severance arises. No reference to mediation has occurred and so the matter is to proceed to arbitration. The agreed uncertainty of subcl 35.11(d) has no effect on the operation of cl 35.12.

89 If I am wrong about the meaning of "or" and it means "and", I would conclude that cl 35.12 is severable from subcl 35.11(d).

90 The principles to decide whether or not a contract or part of a contract is severable or not from some provision void for uncertainty are not, relevantly, in doubt. It is a question depending upon the intention of the parties to be gathered from the instrument as a whole: *Whitlock v Brew* [1968] HCA 71; 118 CLR 445 at 453; 457 and 461; *Life Insurance Company of Australia Limited v Phillips* [1925] HCA 18; 36 CLR 60 at 72; *Brooks v Burns Philp Trustee Co Ltd* [1969] HCA 4; 121 CLR 432 at 442; *Amoco Australia Pty Limited v Rocca Bros Motor Engineering Co Pty Ltd* (No 2) [1975] UKPCHCA 1; 133 CLR 331 at 342.

91 Significant emphasis was placed by United on the Full Court in *Brew v Whitlock (No 2)* [1967] VR 803. The decision was affirmed in the High Court. At [1967] VR at 807-808, in passages particularly emphasised by United, the Full Court said:

> "These authorities on severability in cases concerning uncertainty in a part of a contract point to the test as being the intention of the parties as to whether the operation of the contract apart from the impugned part was to be conditional on the efficacy of that part, or whether it was to take effect notwithstanding the failure of that part. That intention is to be ascertained from the construction of the contract as a whole. The process of construction will have regard to such considerations as the independence in form of the impugned part, any interdependence of that part in form or operation with the rest, the effect that severance would have on the operation or meaning of what is left, the nature of the subject-matter dealt with in the part and its relative importance in the setting of the whole bargain, whether the impugned part is one of several promises supported by different considerations or by a common consideration, or whether it is part of a single consideration supporting a promise or promises or whether it is one of several considerations, and, if so, whether it is a material or important part of the total consideration or merely subordinate.
>
> The considerations to which resort is had for the purpose of construction are not necessarily of the same force and effect, eg dependence in form or interdependence of operation or meaning would operate as a bar to severance, but independence in those respects may not be decisive in favour of severability. In the process of construction for the purpose of ascertaining the intention, in the case of a written contract intended to be the final and complete repository of the parties' intentions, the material to which resort can primarily be made consists of the content of the written instrument (see *Heisler v Anglo Dal Ltd*, [1954] 1 WLR 1273, at pp 1279-80), and the surrounding circumstances cannot be used except for the purpose of explaining the contract (see Cussen J, in *Cooper & Sons v Neilson and Maxwell Ltd*, [1919] VLR 66 at p 77; 25 ALR 36 at p 44[7])."

92 As was pointed out by Wilcox J and Finn J in *Rieson v SST Consulting Services Pty Ltd* [2005] FCAFC 6 at [60] the views expressed in the last paragraph of the above citation as to extrinsic evidence do not conform to the modern approach of the construction of contracts. The unqualified textual conclusion as to "dependence in form or interdependence of operation or meaning" (at 808) needs to be viewed in this light.

93 In *McFarlane v Daniell* (1938) 38 SR (NSW) 337 at 345 Jordan CJ said:

> "When valid promises supported by legal consideration are associated with, but separate in form from, invalid promises, the test of whether they are severable is whether they are in substance so connected with the others as to form an indivisible whole which cannot be taken to pieces without altering its nature: *Harwood v Millar's Timber & Trading Co Ltd* [1917] 1 KB 305, at p 315. If the elimination of the invalid promises changes the extent only but not the kind of the contract, the valid promises are severable: *Putsman v Taylor* [1927] 1 KB 637, at pp 640-1."

94 This passage was approved by the Privy Council in *Carney v Herbert* [1985] AC 301 at 310-311 and applied by both the Full Court in *Brew v Whitlock* [1967] VR 803 at 812-813 and by Wilcox J and Finn J in *Rieson* at [51].

95 Further, in *Brew v Whitlock* [1967] VR 803 at 813 the Full Court said:

> "What all this amounts to is this – that where parties in purporting to make a contract leave some part incomplete and uncertain, and that part, though independent in point of form, meaning and operation, is of such substance and materiality in the whole bargain that it cannot be severed from the rest, then, although the parties may have thought that they had made a contract, they have made none at all; and (estoppel apart) it does not matter which party marks the challenge to the validity of the contract."

McHugh J in *Humphries v Proprietors "Surfers Palms North" Group Titles Plan 1955* [1994] HCA 21; 179 CLR 597 at 621-622 approved of this expression of the matter by the Full Court in *Brew v Whitlock*.

96 Here, the parties have constructed a detailed dispute resolution clause that placed, in one part of the structure, a reference to mediation. I do not extract from either the form or context of the clause (even if "or" means "and") any unseverable nexus to bring down the arbitration clause in cl 35.12 with the failure of enforceability of the mediation clause in subcl 35.11(d). The parties would not be taken to be agreeing to something of a different kind or character if they were to go to arbitration only after the failure of senior representatives to agree. The contract is essentially the same – in the absence of agreement to settle (which need not be within the framework of cl 35.11), the dispute goes to arbitration. The conjunctive "and" does not answer the question in United's favour. The ultimate question is one of contractual meaning and intent. The subject matter and commercial intent of this part of the parties' bargain is important to appreciate at this point. A regime to avoid litigation in court has been constructed. There is an evident aim to have all disputes by the parties dealt with by the perceived advantages of expert determination and arbitration. The consecutive placement of less

formal methods of consensual resolution (negotiation and mediation) before arbitration says no more than the desire for the operation of those mechanisms. The "and" does not convey a necessarily contractually integrated pre-condition for arbitration. Even if one or both of subcll 35.11(c) and (d) is or are void for uncertainty, none of the words of cl 35, its context or the importance of arbitral resolution (or those three together) bespeaks (or bespeak) the intention of the parties that arbitration would only be agreed to and take place if the negotiation and mediation clauses were legally enforceable. The subject of arbitral resolution (with all its well-known perceived advantages: see for example M Holmes "Drafting an Effective International Arbitration Clause" (2009) 83 *Australian Law Journal* 305 at 305-307) is unlikely to be intended to be inseverably linked to the legal enforceability of either or both subcll 35.11(c) and (d), in particular when each can be undertaken, as a practical matter, in any event, even if the clauses are unenforceable. Further, the operation of cl 35.12 can work smoothly with time limits and procedures, notwithstanding the voidness of subcl 35.11 (d).

97 Clause 35.12 is severable from subcl 35.11(d). I reach this conclusion without reference to cl 2.14; but that is another clear and independent basis for the same conclusion. I reject the argument that cl 2.14 does not attach because it is not the enforceability of cl 35.12 being dealt with, but the absence of preconditions for its operation. Subcl 35.11(d) is void and unenforceable (so the parties have agreed). Cl 2.14 is designed to save the enforceability of any other provision. It is an apt use of language to maintain the continued enforceability of the arbitration clause (cl 35.12) notwithstanding the unenforceability of the mediation clause (subcl 35.11(d)).

98 Finally, if I am wrong in my conclusions as to subcl 35.11(c), my views on severance of cl 35.12 would be the same.

Orders

99 I would dismiss the appeal with costs.

100 IPP JA: I agree with Allsop P.

101 MACFARLAN JA: I agree with Allsop P.

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3 July 2009