Mining – When Is Product "Shipped"?

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On 24 April 2020, the New Zealand Court of Appeal held that coal was "shipped" when it was transported by truck from a landlocked mine, making the miner liable for a US$40 million performance payment.

In *Bathurst Resources Limited v L&M Coal Holdings Limited* [2020] NZCA 113, a miner had purchased the rights to mine coal, with payments being deferred until certain quantities of coal had been "shipped from the Permit Areas". A first performance payment of US$40 million was required when 25,000 tonnes were shipped, and a second when 1 million tonnes were shipped.

No payment had been made by the time 50,000 tonnes were extracted and the miner mothballed the mine to concentrate on developing other mines in New Zealand. Small quantities of coal were sold from stockpiles at the mine for which the miner continued to pay royalties to the owner. The miner said it did not have to make the first payment because a royalty deed enabled it to choose between paying either the performance payment or royalties at a higher rate.

Before mining had begun, the sale agreement had been amended to provide that, "for the avoidance of doubt", a failure to make a performance payment was not an actionable breach or a default "for so long as the royalty payments continued to be made under the Royalty Deed". The miner relied on this clause to argue it had a choice between the performance payment and royalties.

When Is Product "Shipped"?

The court looked at not only the text, but also the overall commercial context to determine whether "shipped" meant the miner only became liable when coal was transported by ship, or when it was transported from the mine by any means. Here the predominant destination of the coal was the export market for coking coal, supporting the "transported by ship" interpretation, although some coal was sold domestically.

Counter to this interpretation was the miner's consistent acknowledgment in its financial statements for three consecutive years that the first performance payment had been triggered by production at the mine. There was also no distinction in the payment obligations between coal to be exported and that sold domestically.

Finding that "shipped" meant "transported", the court said that export coking coal was not the project's exclusive focus and that if liability for the first performance payment had depended only on export tonnages, a more sophisticated formulation "necessarily" would have been adopted.

Choice Between Performance Payment and Royalties

Did the amendment to the sale agreement give the miner a choice between making the performance payment and royalties? To answer this, the court looked at the purpose and context of the amendment. The purpose was to avoid impairing financing attempts by an announcement that the miner was in breach by non-payment of the first performance payment.

The context was, first, that the parties were already subject to binding obligations under the sale agreement and that this was a concession by the owner for which the miner gave no material consideration. Second, the owner had limited leverage over the miner to force it to get on with mining. Third, some mining had to have taken place to trigger the first performance payment obligation.

The owner's right to sue the miner for failure to make the first performance payment was expressly reserved in the sale agreement and not changed by the amendment. Royalties were payable at a higher rate to the end of mining if the performance payment was not made, but there was no excusing the performance payment, or a choice between the two.

Despite using the phrase "for the avoidance of doubt", the amendment was held to change rather than merely clarify rights. It conditionally suspended the otherwise unqualified right to sue if performance payments were not made. It did not give the miner a choice between those payments and higher royalties. Such an interpretation would fundamentally alter the economic balance in the miner's favour and would be commercially unrealistic given the miner provided no material consideration and was a supplicant without negotiating strength.

"For the avoidance of doubt" are not "the words or revolution" and do not indicate the significant change the miner's interpretation would produce, namely to "place a US$40 million debt on ice, indefinitely".

The court took the clear view that the amendment meant that the debt would not be payable for so long as the miner continued to pay royalties from continuing mining and sales at a level not materially less than had resulted in the first performance payment being triggered in the first place, i.e. 25,000 tonnes in about 12 months. This was not met by nominal royalties from a stockpile left after mining ceased.

Objective Theory of Contract

Time and again, the court emphasised the objective approach to interpreting contracts in the common law, where "the aim of contract interpretation is to ascertain the meaning the contract would convey to a reasonable person, having the background knowledge reasonably available to the parties in the situation they were in at the time of the contract". Coming to each of the conclusions in this judgment required recourse to the views of that reasonable person.

It is a little surprising that an intermediate appellate court still needs to expound on the objective approach to contract interpretation, almost 200 years after it originated in 1833, and from when it "has been the unbroken orthodoxy of the common law in interpreting contracts". It seems aspects remain heavily contested, such as the tension between the parties' common subjective state of mind and their objectively determined state, and reception of evidence of the former.

Comments and Reminders of Principle

The judgment makes these helpful comments and reminders of principle:

- Text is pre-eminent in interpretation, being an expression of the objective approach in that it is the best objective evidence of what was intended
- Evidence of subsequent conduct in reliance on the text is more readily received than that of prior negotiations
- Subsequent conduct, though, may merely be evidence of a mistaken interpretation of the contract
- The reasonable observer will bear in mind contractual purpose, relative bargaining strengths, character of the parties and other admissible context
- Interpretation is one of the three principal elements of contract construction, the others being implication and rectification
- Only in rectification is the subjective intention of the parties relevant
- Rectification ensures parties are not held to an objectively ascertained bargain they did not intend
- Rectification is a remedy that has been rather crowded out by contract interpretation being invited to undertake more than its proper task
- The most usual inference from a gap in the contract is that nothing at all was intended
- The inability to anticipate and provide for all eventualities means that when parties bargain incompletely, they engage the court as a reasonable bystander to bridge the gap and make the bargain work, if that can be done within the limits of construction
- Disputes bring about distorted, ex post thinking – what parties have to say with the benefit of hindsight about their contractual intentions is unlikely to be either reliable or helpful
- There is an unchallenged rule against the receipt of direct declarations as to intention in evidence to interpret instruments
- The objectivity principle recognises that there must be a limit to the extent to which it is gainful to dig into material beyond the confines of the contract to ascertain meaning
- Regard to extrinsic material is particularly restricted where third parties have acquired rights under the contract as they were not party to the negotiation process and will not have access to that material
- The wider the negotiating audience, the more restrictive the approach to receipt of extrinsic evidence may be
- The objective principle may give way to actual mutual intention in a case where the objective interpretation does not accord with that intent

Comment

The judgment shows a pragmatic, commercial approach to interpreting mining contracts, taking account of business realities and the background to the transaction. It could be considered quite a step to hold that relief from the performance payment applied while mining continued at a level not materially less than had resulted in the first performance payment being triggered in the first place, as these words were neither in the sale agreement nor in the amendment. They make commercial sense, however, and appear to accord with what usual business people would agree.

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