

In our September edition of *Construction Matters*, in an article entitled “*Mineralogy v Sino Iron: A Match Not Made In Heaven*”, we discussed the ongoing dispute between Clive Palmer’s company Mineralogy and various other entities regarding the Sino Iron iron ore project.

In *Mineralogy Pty Ltd v Sino Iron Pty Ltd* [2017] FCAFC 55, the Federal Court of Appeal has upheld the decision of the primary judge (Edelman J) and dismissed Mineralogy’s appeal from an order that Mineralogy be permanently restrained from acting upon purported termination notices it issued.

In its judgment, the court dealt with some important legal issues relevant to construction projects.

## The Dispute

The principal issue at the trial before the primary judge was whether Mineralogy had terminated certain agreements, called “Facilities Deeds”, which it had with each of Sino Iron and Korean Steel. Sino Iron and Korean Steel entered into Facilities Deeds with Mineralogy while they were subsidiaries of Mineralogy. Subsequently, CITIC Ltd (then CITIC Pacific Ltd), through various intermediate holding companies, acquired all of the shares in Sino Iron and Korean Steel (the CITIC parties). If the Facilities Deeds had been terminated as alleged by Mineralogy, then the multibillion dollar project established by the CITIC parties would come to an end.

## Relief Sought By Mineralogy and Court’s Findings

Mineralogy sought a declaration that the termination notices were valid and effective and that the Facilities Deeds had terminated. A significant related issue affecting the validity of these notices was who was responsible for the operation and maintenance of the port facilities.

The Federal Court of Appeal held that the primary judge was correct in concluding that there was no doubt that the CITIC parties, not Mineralogy, were solely responsible for the operation and maintenance in the area of the port and the termination notices were “invalid and insubstantial”.

In reaching the court’s conclusions it dealt with the proper interpretation of the Facilities Deeds and related documents and found for the CITIC parties. These aspects of the case are contract-specific. But the court also discussed alternative grounds, such as estoppel and implied good faith obligations as well as what “serious or persistent breach” means in a termination clause.

## Estoppel by Convention

The primary judge concluded that if Mineralogy had the rights that it asserted under the facilities deeds to process, operate or maintain the port terminal facilities, then an estoppel by convention would preclude Mineralogy from exercising those rights.

The estoppel by convention was said to arise because Mineralogy, by its approval and submission of approved proposals (the “Proposals”) under the State Agreement,<sup>1</sup> adopted a common position with the CITIC parties that the Sino Iron Project would operate in a certain manner, as outlined in the Proposals.

The primary judge set out the five elements that needed to be satisfied before an estoppel by convention could arise:<sup>2</sup>

- Party A has adopted an assumption as to the terms of its legal relationship with Party B
- The Party B has adopted the same assumption
- Both parties have conducted their relationship on the basis of that mutual assumption
- Each party knows or intends that the other will act on that basis
- Departure from the assumption will cause detriment to one of them

The plea advanced by the CITIC parties was that they and Mineralogy had both adopted a common position (or assumption), that being that the Sino Iron Project would operate in the manner set out in the Proposals, which included provisions that Mineralogy was to have no implementation or operational role in the project. Accordingly, the primary judge was satisfied that the requirement for estoppel by convention had been established.

<sup>1</sup> Reference to the State Agreement is a reference to an agreement entered into by a number of parties, including Mineralogy, Sino Iron and Korean Steel on 5 December 2001. The State Agreement made provision for Proposals to be approved by the State and was ratified by Parliament, pursuant to the requirement that dealings with Crown land can only be authorised and supported by statute.

<sup>2</sup> Considering: *Con-Stan Industries of Australia Pty Ltd v Norwich Winterthur Insurance (Australia) Ltd* (1986) 160 CLR 226; *Eslea Holding Ltd (formerly Ipec Holdings Ltd) v Butts* (1986) 6 NSWLR 175.

The pleading relied upon by the CITIC parties at trial was that, on the basis of the common assumption, they commenced and continued the construction of the entire Sino Iron Project and that it would be unconscionable to allow Mineralogy to depart from the common assumption for the following reasons:

- Mineralogy jointly approved and submitted the Proposals to the state
- The CITIC parties, as Mineralogy knew, had incurred vast expense in the construction of the project in reliance upon the Proposals

The effect of the estoppel was said to have depended on the common assumption that Mineralogy was to have no implementation or operational role in the Sino Iron Project. The primary judge was satisfied that there were “many indicators”<sup>3</sup> that the CITIC parties acted upon the assumption from the Proposals that their entity would operate and manage all of the project and that Mineralogy would not operate or manage any part of the project.

In short, the primary judge was satisfied that:<sup>4</sup>

- The parties had adopted the common assumption based on the Proposals from 2 May 2008 that a CITIC subsidiary would be responsible for implementing and operating the project, while the company facilities were not shared facilities and that Mineralogy would have no role in operating and managing the company facilities.
- That as a party to the Proposals in the State Agreement, Mineralogy knew that the CITIC parties would proceed on the basis that the project would be implemented according to the Proposals.
- The common assumption was a significant factor in the CITIC parties commencing and continuing construction of the facilities, including the port terminal facilities in the manner in which they were constructed.
- The CITIC parties would suffer detriment if that common assumption was departed from because they spent at least hundreds of millions of dollars upon a design that would have been different. But for the assumption they made, there would have been occasioned considerable disruption and massive cost and delay to put the matter at its very lowest if part of the project were operated by a different operator.

On the appeal, Mineralogy contended that of the five estoppel elements, none had been satisfied on the evidence. Further, it argued that if, contrary to the primary judge’s conclusion, the matters referred to in the Proposals did not constitute terms of any agreement, then, not only can they not constitute contractually binding and enforceable agreements, but they cannot amount to assumptions commonly shared.

Mineralogy also placed emphasis on the uncertainty of the detriment said to be suffered by the CITIC parties and pointed to certain factors that it said demonstrated there was no common assumption.

In weighing up these factors, as well as related correspondence and the existence of an administrative fund (which Mineralogy contended was established to allow for the CITIC parties to pay Mineralogy for its cost of operating and maintaining the Facilities), the Federal Court of Appeal rejected this ground of appeal.

In reaching its conclusion, the court noted that the parties did not take issue with the five estoppel elements identified by the primary judge but rather whether the evidence met the elements. However, one would have expected the court to have corrected the elements if they considered them to be wrong.

The primary decision, therefore, remains a useful summary of the legal elements of estoppel by convention and the extent to which the concept applies to future rights and future conduct, and the case is a helpful example of evidence that meets these criteria.

## Implied Duty to Act Reasonably and in Good Faith

The primary judge rejected the CITIC parties’ argument that there was an implied term in the facilities deeds requiring Mineralogy to act reasonably and in good faith in issuing a purported termination notice on the basis that a clause in the deeds did not permit a termination notice to be issued in respect of a breach that is “persistent” but not “serious”.

In opposition, the CITIC parties contended that the arguments in favour of an implied term requiring Mineralogy to act reasonably and in good faith were compelling, given the scale of the investment, the period of time involved and complexity of operations involved in the projects, as governed by the facilities deeds, and in the interests of business efficacy.

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3 2017 FCAFC 55 at [340].

4 2017 FCAFC 55 at [343].

In support of the primary judge, the Federal Court of Appeal disagreed with the propositions of the CITIC parties on the basis that such commercial matters do not in and of themselves justify the existence of such an implied term. But the court did accept the proposition that a contractual discretionary power ought to be exercised for the purpose for which it has been conferred. If the reasonable and good faith term had been implied, the court commented that the primary judge's conclusions that the termination notices were not issued "reasonably" or "in good faith" had considerable force.

### **"Serious or Persistent" Breach**

The termination clause of the relevant agreements gave a right to terminate for a "serious or persistent" breach. The primary judge had concluded that a series of trivial breaches which have no serious consequences, individually or collectively, would not be a "serious or persistent" breach justifying termination.

The Federal Court of Appeal stated that this proposition was expressed too strongly – in some circumstances the nominated circumstances may amount to a "persistent breach". Further, a breach may be 'serious' if it is a breach of an essential term.<sup>5</sup>

In the context of the present case, this alternative formulation did not assist Mineralogy.

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<sup>5</sup> 2017 FCAFC 55 at [412].