Sovereign Risk: Commentary

*Denis Gately**

Introduction 173
State Agreements in Queensland—Flexible Entrenchment 176
Executive Necessity or Political Expediency 182
Introductory concepts under the GOC Act 185
Legislative intention 186
How is a GOC created? 187
Accountability and management 188
Continuing government direction 189
Limits on legal capacity of GOC 191
Conclusion 192

INTRODUCTION

Many of the significant and now mature resources projects in Australia were planned and implemented in times when the notion of "sovereign risk" was not seen as a significant investment risk in this country. Australia was considered to have stable and predictable processes of government, coupled with a mature legislative process—and in any event, the push for development in the third quarter of this century was paramount: project interests seemed to prevail over sectoral and social interests.

But then the pace of development stabilised—even slowed, perhaps—and the balance of interests adjusted. In the process, the Australian legislature developed a heightened awareness of the "public interest". And, as the investment cycle took on more of a roller-coaster profile, so governments in this country saw the need to have in place more stable, longer-term, social policy objectives which ought to prevail over project interests.

That brought into sharp focus the investor/developer's need for long-term certainty: juxtaposed against that need was the growing realisation by government that it could not afford, socially or electorally, to fetter its ability to ride the sharpening peaks and troughs of the investment cycle. And, so, sovereign risk became a real issue in the Australian investment landscape.

* BA, LLB (Syd), Solicitor, Brisbane.

This was amply demonstrated by at least three decisions at that time, namely *Cudgen Rutile (No 2) Pty Ltd v Chalk,*[1] *Commonwealth Aluminium Corp Ltd v Attorney-General*[2] and *Murphyores Inc Pty Ltd v Commonwealth*[3]—where aggrieved developers saw the apparent security of their State Agreements displaced by the operation of other legislation, with a resultant shift in the balance of risk against their interests.

Interestingly, at its conference in Sydney in 1988, the International Bar Association's Section on Energy and Natural Resources Law focused on just this risk, with its stated theme of "Coping with Government Intervention in Resource Projects".[4] That conference identified "responsiveness" and "security" as the key issues in the interplay of interests between government and developer. The responsiveness of the natural resources regime to supervening economic, legal, social and political conditions was seen as a prime requirement of government. Against that, the investor/developer was principally motivated by the need for planning and investment security: the legal terms which led to the original investment decision must remain stable and not be altered to the investor/developer's disadvantage by such legislative or administrative action.

Alastair Lucas set the scene well when he said:

> "The basic objective of state natural resource systems is production of public benefits. Ideally, this means maximising public benefits. Economists characterise these benefits more specifically, in terms of maximisation of 'economic rent' from the resources—that is, the difference between the market value of resources, and the cost, in terms of labour, capital and materials, necessary to produce and market them. The implication is that if rent is maximised and if government appropriates as much as possible, then social welfare may be maximised . . .
>
> To the economists' view must be added the broader political dimension. This introduces a wide range of other societal objectives that may directly or indirectly conflict with rent maximisation. These include regional development, industry sector support and environmental protection goals. The relative government-industry share of rents will also reflect a range of public objectives including cultural and territorial sovereignty, basic political choices, such as direct rather than indirect private sector employment creation, as well as goals such as minimum state intervention, that may be characterised as ideological.
>
> This precarious relationship between governments and natural resource developers is the setting for consideration of responsiveness and security within resource regimes."[5]

1. [1975] AC 520.
2. [1976] Qd R 231.
3. (1976) 136 CLR 1.
4. See International Bar Association Series, *Energy Law* (1988), pp 261-410.
5. Ibid, pp 295-296.

In their comparative analysis of legislative regimes around the world, Zillman, Mestad and Laitos pointed to a marked change emerging in the last quarter of this century:

> " 'National sovereignty over resources' is as legitimate a rule of international law as 'no arbitrary expropriation'. The contemporary natural resources development agreement with its considerable attention to development goals of the host country is a far cry from early concession agreements that turned over title to resources wealth in return for trivial bonus payments and royalty shares. Quite probably, a standard of unconscionability has arisen to invalidate a development agreement that takes too one-sided a view of the responsibilities of developer and host country . . .
>
> While outright state acquisition of vested private property without compensation is improper, more vexing questions remain as to the steps a government may take short of uncompensated acquisition . . . Powers to change tax regimes or to respond to threats to the natural and human environment are recognised by constitutional provision or judicial decision at least in the absence of a specific stabilisation agreement. The question is one of degree. At some point, the line between permissible government adjustment and impermissible taking can be drawn."[6]

Those postulations were made five years ago: the authors foreshadowed that in the ensuing decade, a significant issue for natural resources development would be the law of constraint on legislative action. What has been the extent of that development (if any) in Australia?

Peter Turner identifies growing government concern at a time when the pace of development in Australia was slowing. He points to the observation made by the Industry Commission in the course of its 1991 inquiry into mining and minerals processing, that sovereign risk then represented a serious impediment to the efficient development of those industries in Australia. In realpolitik this might be seen as recognition by government that its preoccupation with responsiveness of the natural resources regime had led to insufficient recognition of the developer's need for security in making the investment. That balance of conflicting interests needed to be redressed, by reducing the impact of sovereign risk.

Mr Turner's definition of "sovereign risk" is a useful one, and he is right to contrast it with "political risk" and "country risk". It should properly be seen as an abstract or process risk, rather than one which derives from peculiar or intrinsic characteristics of a particular country or its political system or process.

The author clearly states that the scope of his paper does not permit an exhaustive survey of all issues arising out of sovereign risk—rather does it focus on a number of the more fundamental legal matters which confront resources lawyers in their dealings with government. In my commentary, I propose to pick up on at least two of those issues—

6. Ibid, p 289.

namely, the history of State Agreements in Queensland and the demise of the principle of double entrenchment, and the efficacy of the doctrine of executive necessity in the emerging regime of government-owned corporations.

STATE AGREEMENTS IN QUEENSLAND—FLEXIBLE ENTRENCHMENT

The paper explores in some detail the usefulness of specific legislative sanction in the form of State Agreements to bind governments to their agreements, promises and representations, and to prevent their later exercise of discretionary powers to the detriment of resource projects. This contractual approach to the risk management process has long been recognised and is principally directed at meeting the developer's requirement for security. It is generally a device that is used only after the high risk exploration stage has been successfully completed, and a proven resource has been identified: usually it will precede any commitment by the developer to significant levels of capital expenditure in developing that resource.

The paper also considers the notion of "double entrenchment" of those agreements so as to inhibit their later amendment or repeal by the relevant legislature. The author concludes, correctly in my view, that a double entrenchment provision cannot be effective if an underlying intention is to give the investor/developer control over the legislative amendment process.

This Association first considered the notion of State Agreements in 1977. Ken MacDonald then identified a principal reason for the use of State Agreements as being the developer's need to obtain a guarantee of co-ordinated co-operation by governmental departments, instrumentalities and authorities in order to ensure the viability of the project.[7] Nowhere then, nor in subsequent forays in the area, was the concept or notion of sovereign risk expressly referred to in that context—yet the authors have at all times focused on those very components of that risk as identified by Mr Turner in his paper and on a number of the specific issues which he addresses. In particular, Mr MacDonald considered the enforceability of State Agreements, in light of the then recent decision in the *Comalco Case*[8] and the type of relief which might be available to an investor/developer against the State: he concluded that once a State Agreement was given the force of law, the misgivings expressed by Dunn J in the *Comalco Case* (as to whether the damage suffered by the investor-developer is cognisable by the courts) are removed to some extent.

Then, in the context of a government seeking to avoid its contractual obligations under a State Agreement, Mr MacDonald considered the issue of entrenchment and left open the possibility that a careful drafter could

7. (1977-1978) 1 *AMPLJ* 29.
8. [1976] Qd R 231 at 262.

achieve the desired objective. In this respect, however, Professor Enid Campbell in her commentary concluded that:

> "the *Comalco Case* does not rule out the possibility of devising a statutory formula which will effectively inhibit parliamentary power to vary and override the terms of a franchise agreement which has itself been given statutory force. There is no constitutional objection to the delegation of power to vary such agreements, though by themselves such delegations do not affect parliamentary power to enact overriding legislation. Equally there is no constitutional bar to the enactment of a statute which removes or restricts Parliament's power to amend or repeal, though such a statute will not effectively limit parliamentary power unless it is coupled with a further statutory provision which controls the manner in which Parliament makes laws to override its prior enactment delimiting its power. This further provision may be one requiring a special parliamentary majority. However if it is one which requires the consent of an unelected and unrepresentative extra-parliamentary agency, it may fail to qualify as a binding manner and form requirement on either or both of two grounds:
>
> (a) it is in substance a law respecting the powers of the representative legislature; and
>
> (b) it removes from that legislature legislative power in relation to a given subject matter and reposes it in a body which does not answer the description of a representative legislature."[9]

That analysis must in my view be correct and it is one which is likely to receive judicial endorsement given the recent High Court decisions in *Australian Capital Television Pty Ltd v Commonwealth (No 2)*[10] and *Nationwide News Pty Ltd v Wills*.[11] In these watershed decisions, the High Court restated the fundamental constitutional principle or doctrine of representative government in Australia, a system of government by which the executive is responsible to the legislature which is in turn appointed by and responsible to the electorate. The court noted that it was necessarily implicit in that principle or doctrine that there be freedom of speech. It is only a short step from that stance to observe that to permit a non-elected body (such as a developer being a party to a State Agreement) the power or capability of directing the enactment of laws is inconsistent with the system of responsible government, so that any laws passed pursuant to that power are unconstitutional.

It is difficult to add anything useful to the excellent and comprehensive treatises on State Agreements delivered to this Association at its conferences in 1982 and 1988 by Leigh Warnick.[12] What I propose, however, is to examine in a little more depth the most recent evolution of the form of State Agreement consistently used in Queensland for resource projects in the third quarter of this century.

9. (1977-1978) 1 *AMPLJ* 58.
10. (1992) 108 ALR 577.
11. (1992) 108 ALR 681.
12. (1982) *AMPLJ* 1 and (1988) 62 *Australian Law Journal* 878.

Mr Warnick quite correctly notes that the consistent drafting approach employed in Queensland is remarkable when compared to the other States.

What I shall call "the Queensland model" had its genesis in the *Electricity Supply Corporation (Overseas) Agreement Act* of 1947 in relation to certain coal deposits near Blair Athol—as that project never proceeded, the Queensland model was not tested in a practical sense until the *Commonwealth Aluminium Corp Pty Limited Agreement Act* in 1957. It was thereafter adopted for the purposes of the *Thiess Peabody Coal Pty Ltd Agreement Act* 1962, the *Alcan Queensland Pty Limited Agreement Act* 1965, the *Central Queensland Coal Associates Agreement Act* 1968, the *Greenvale Agreement Act* 1970 and the *Aurukun Associates Agreement Act* 1975.

Relevantly, the Queensland model provided that:

- upon the making of the Agreement its provisions were to have the force of law as though the Agreement was an enactment of the Act;
- the Agreement may be varied pursuant to a further agreement between the Minister and the developer with the approval of the Governor-in-Council by Order-in-Council, and no provision of the Agreement may be varied, nor may there be any derogation from the powers and rights of the developer, except in that manner;
- any Order-in-Council intended to operate as a variation is required to be placed before the Parliament within 14 days and the Parliament may by resolution of which notice is given within a further period of 14 days resolve to disallow the Order-in-Council.

Also, in the case of Comalco at least, the Agreement provided for particular fixed rates of royalty. The strength of those provisions was then tested in 1974 when the Queensland Parliament passed a new *Mining Royalties Act* which operated so as to increase substantially Comalco's royalty obligation above the rates set out in the Agreement. This new legislation was passed without any agreement by Comalco, as Comalco contended was required by the variation clause in the Agreement. The court affirmed the principle established in *McCawley v The King*[13]—that Parliament can always amend or repeal any Act merely by passing inconsistent legislation—for reasons which are amply well analysed by Mr Warnick.[14]

And if a developer might find some comfort in the principle enounced in *Bribery Commissioner v Ranasinghe*[15]—that if there is an express legislative provision concerning the manner and form of such amending legislation, that manner and form must be observed—that hope was dashed by the decision of the South Australian Court in *West Lakes Limited v South Australia*[16] in terms resembling Professor Campbell's analysis to which I have earlier referred. There, the court considered a provision in the Agreement which stated that "the Premier and the

13. [1920] AC 691.
14. (1982) 4 *AMPLJ* 1 at 7-13.
15. [1965] AC 172.
16. (1980) 25 SASR 389.

corporation may from time to time . . . by agreement in writing amend this indenture", and held that if it had been possible to construe this clause so as to prevent Parliament from legislating at large inconsistently with the indenture, the clause could not have been construed as a legitimate "manner and form provision":

> "a provision requiring the consent to legislation of a certain kind of an entity not forming part of the legislative structure . . . does not to my mind prescribe a manner or form of law making but rather amounts to a renunciation pro tanto of the law-making power. Such a provision relates to the substance of the law-making power not to the manner and form of its exercise".[17]

There was then a subtle change in the Queensland model following the *Comalco Case*. In 1977, in the *Queensland Cement and Lime Company Limited Agreement Act*, the enabling statute contained no statement of the variation procedure required—rather did the Act provide that:

> "[The variation provisions in the Agreement] shall not be construed to restrict the Parliament in making laws that affect the rights and obligations of the parties under this Agreement."[18]

The variation provisions of the Agreement, in turn, simply provided that it may be varied pursuant to an agreement between the Minister and the company with the approval of the Governor-in-Council by Order-in-Council—but the Agreement went on to provide that there must first be consultation between the company and the appropriate State authorities, corporations and instrumentalities.

In this form the Queensland model attempted to restate the principle in *McCawley v The King*, insofar as that principle applied to State Agreements, and recognised at least the process of consultation and consensus which underpins the contractual model (in the form of State Agreements) used to manage sovereign risk. That variant of the Queensland model appeared again in the *Rundle Oil Shale Agreement Act* 1980.

Writing in 1982, Mr Warnick noted that the principal objective of State Agreements—to provide a stable set of legal rules under which a development can proceed—foundered on the principle in *McCawley v The King*. On the issue of the security of State Agreements, he propounded that:

- it should be possible to draft an "amendment only by consent" provision in the shape of a manner and form provision and to doubly entrench that provision;
- but such a provision is arguably not "manner and form" and in fact relates to the substance of the law-making power;
- and in any event on a practical and political level, the States now seem to be making deliberate efforts to avoid tying the hands of their successors in office.[19]

17. Ibid at 398 per King CJ.
18. s 3.
19. (1982) 4 *AMPLJ* 1 at 14-15.

Then, in 1985, a further variant yet of the Queensland model emerged with the *Mount Isa Mines Limited Agreement Act*, the most recent of State Agreements relating to resource projects. There, the Parliament endorsed an agreement entered into by representatives of the State and MIM, legislating that the Agreement was:

> "ratified and approved, and given the force of law and shall take effect as if its provisions were expressly enacted in this Act, and such provisions shall apply and prevail notwithstanding inconsistency in any respect with any other Act or law."[20]

While this provision might be construed to operate to the detriment of the principle in *McCawley v The King*, the enabling Act nonetheless went on to provide for a variation procedure in the same terms as the Comalco Agreement—only by agreement between Minister and developer, revocable by resolution of the Parliament—but incorporated the express caveat first employed in the QCL Agreement in 1977, namely, that the variation provisions were not to be construed so as to restrict the Parliament in making laws which affected the rights and obligations of the parties.

As Mr Warnick then pointed out in 1988,[21] the *Comalco Case* highlights the insecurity of State Agreements against inconsistent legislation and it is dangerous to rely upon the "as if enacted" formula of the Queensland model for its face value:

> "State Agreements are vulnerable to legislative changes in the rules, and the only form of security [developers] can get is security against interference with their rights under the Agreement by the executive arm of government. How secure they are on this front depends on the form of words use to give legislative endorsement to their Agreements."[22]

In his view, the Queensland model will operate so as to compel the government to fulfil its express obligations under the Agreements and to refrain from exercising discretionary and regulation-making powers in such a way as to prejudice the developer's contractual positions. The developer's contractual rights are given statutory force—and as a result the ambit of other statutory powers is limited. However, I suggest that in order to put the issue beyond doubt the Queensland model would best be augmented by a statutory direction to the State instrumentality to perform its obligations under the Agreement (as propounded in the paper).

The conclusion which I believe must be drawn is that the Queensland model in its present form does not offer the investor/developer adequate protection against sovereign risk, to the extent that subsequent legislative action can derogate from the rights of the developer and inconsistent executive action is not conclusively prohibited. Interestingly, in his comments on Mr Warnick's paper in 1982, Geoff Witham noted that while the notion of entrenchment probably was dead, there was still a

20. s 2.
21. (1988) 62 *Australian Law Journal* 883.
22. Ibid at 891.

case for a review of the principle in *McCawley v The King*: there should be an ability to fetter legislative authority especially at least in the case of contractual obligations entered into with express parliamentary approval. Privity of contract should, in his view, prevail over political necessity.[23]

If a State Agreement is not adequate security against legislative action, can it be effective against inconsistent executive action? The thin end of the wedge here first appeared in certain remarks of Dunn J in the *Comalco Case*, to the effect that the enforcement of a State Agreement was not a matter justiciable by the Supreme Court, because of the political nature of the State's obligations:[24] in 1982 Mr Warnick expressed concern that to release the State in its executive capacity from obligations to keep its promises is unnecessary, incorrect and dangerous—and it is, in my view, difficult to postulate seriously a contrary view. To permit the State to renege on its contractual promises is to expose sharply the concern expressed at the same time by Mr Witham and to expose the developer to an unacceptable level of sovereign risk.

It is useful in this context to consider the provisions of the *Crown Proceedings Act* 1980 (Qld). That Act was introduced for the purpose of consolidating and amending the law relating to proceedings against the Crown, and provides in s 10 that the court, when dealing with any proceedings against the Crown, is to have the same power with respect to its judgment as it has in any proceedings between subject and subject, and otherwise to give such appropriate relief as the particular case requires. That section seems to me to permit relief in the nature of specific performance, and injunctions, to be available to a developer (if not also third parties) seeking to enforce the terms of a State Agreement against the State.

In *Ansett Transport Industries (Operations) Pty Ltd v Commonwealth*[25] Mason J considered whether an express covenant in the Airlines Agreement could be enforced specifically as well as by an action for damages:

> "the doctrine that an agreement of the kind in question may constitute an anticipatory fetter on the exercise of a statutory discretion is closely connected with the question whether the agreement is authorised by statute, or is prohibited by, or incompatible with it. If the agreement is authorised, then it is valid, and any breach of the undertaking it contains will be enforceable by damages, but only when the effect of statutory approval is to convert the discretion into a duty whether it be enforceable specifically . . .
>
> Here, all that emerges is that the exercise of the discretion [to relax the prohibition imposed by the *Customs (Prohibited Imports) Regulations* against the importation of aircraft] is in conformity with a policy enunciated by the Minister or with a policy of which the

23. 1983 *AMPLJ* 84.
24. [1976] Qd R 231 at 261.
25. (1977) 139 CLR 54.

Minister approves. If the policy were inconsistent with the contractual obligations of the Commonwealth . . . even if it could give rise to a liability in damages, it could not ground relief by way of injunction."[26]

His Honour had considered the doctrine of executive necessity, and in particular the *Amphitrite*[27] case and *Commissioners of Crown Lands v Page*,[28] and came to the conclusion that:

"In the absence of specific words, an undertaking which would affect the exercise of discretionary powers to be exercised for the public good, should not be imputed to the Commonwealth."[29]

The argument is well open, however, that, at least in the case of contracts with the State of Queensland, equitable remedies in the nature of specific performance and injunctions are available to protect and enforce obligations of the Crown as if the Crown were a natural person.

EXECUTIVE NECESSITY OR POLITICAL EXPEDIENCY

Even before the *Amphitrite* case in 1921, the doctrine of executive necessity was considered in Australia, by the Supreme Court of Victoria. In *Attorney-General v Goldsborough*,[30] Higginbotham J put the rule in the following terms:

"An undertaking by a Minister of the Crown, on behalf of the Crown, that the Crown by its representative will do a certain act at a future time, conditional upon the occurrence in the meantime of an event yet uncertain, amounts to a conditional undertaking by the Minister that he will give certain advice to the Crown at a future time in a certain event. It has been contended by the plaintiff in this case that an undertaking of the same kind, relied on by the defendants, is one which Her Majesty's responsible Ministers had no power or authority to enter into so as to bind the Crown, and I concur in that view."[31]

For myself, the pithy brevity of Aronson and Whitmore has great appeal:

"Put bluntly the idea lying behind this principle, which is sometimes referred to as the doctrine of executive necessity, is that, in some circumstances, government authorities ought to be able to renege on contractual promises in the broad public interest."[32]

Perhaps the leading Australian case on the doctrine of executive necessity is the *Ansett* case.[33] Admittedly, in that case the doctrine was

26. Ibid at 77, 83.
27. *Rederiaktiebolaget Amphitrite v R* [1921] 3 KB 500.
28. [1960] 2 QB 274.
29. (1977) 139 CLR 54 at 78.
30. (1889) 15 VLR 638.
31. Ibid at 645.
32. Aronson and Whitmore, *Public Torts and Contract* (Law Book Company Limited, 1982), p 194.
33. Op cit, p 25.

not applied—yet it was the subject of considerable comment by members of the court. Elizabeth Nosworthy usefully identified three principles which emerged from the decision relevant to the executive necessity argument, namely:

- a confirmation of the doctrine in respect of attempts to fetter statutory discretions;
- the creation of an exception to the doctrine in circumstances where the anticipatory fetter is itself authorised by statute; and
- an acceptance that there must be some limits to the application of the doctrine in order to preserve public confidence in government contracts.[34]

It is that need for certainty in contracting with the Crown which strikes such a receptive chord in the resources sector: where so many of the other risks are so high, and where the capital cost of investment is so significant, it is difficult to resist a call for superiority of a privity of contract when contracting with the Crown.

True it is that the *Amphitrite* case distinguished between discretionary powers of the Crown to be exercised for the public good, and the exercise by the Crown of its executive power to enter into commercial contracts: Aickin J in the *Ansett* case was not struck by the distinction[35] and Mr Turner, in his paper, concludes that nothing turns on the characterisation of a contract as "commercial" or otherwise.

However, Ms Nosworthy undertakes a very useful analysis of this aspect of the *Amphitrite* case. In her view, the reference to commercial contracts can be meaningful if consideration is given to the incompatibility test developed in a number of early English decisions dealing with the fettering of discretions of statutory corporations: in those cases, the courts generally inquired whether the action of the statutory corporation should be held to be invalid on the basis that it was incompatible as a statutory purpose of the corporation. The test of incompatibility was accepted as a factual test—however, the question was then asked whether there was in fact some reasonable probability that the action proposed might at some future date interfere with the statutory purpose of the corporation. If that reasonable probability existed then the proposed action was invalid—if not (and notwithstanding some remote possibility of interference with the exercise of statutory power) the action was held to be valid. Ms Nosworthy believed that it was possible to approach anticipatory fetter of the executive power of the Crown in the same manner and she suggested that the following principles should apply:

"(i) Where the Crown enters into a contract which expressly fetters a future exercise of a statutory discretion, the contract will be invalid except in circumstances where it is specifically authorised or approved by a statute.

(ii) Where the Crown enters into a contract which expressly fetters a future exercise of prerogative power then the contract will

34. See papers presented at 22nd Australian Legal Convention, 1983, p 103.
35. Op cit, p 113, n 25.

probably be invalid except in circumstances where it is specifically authorised or approved by a statute.

(iii) Where no express fetter appears in the contract but the terms of the contract are incompatible with exercise of a statutory or prerogative discretion and there is a reasonable probability in fact that the carrying out of the contract will fetter the future exercise of that discretion, then the contract will be invalid.

(iv) Where the Crown enters into a contract which does not fall within categories (i) to (iii) above the contract is valid but will be read subject to the right of the Crown at any time to exercise its statutory and prerogative powers.

(v) . . . the balance of authorities at the moment suggests that in any of the cases referred to in paragraphs (i) to (iii) above, the contractor will not be entitled to damages against the Crown. It is suggested that this approach would also be followed in cases referred to in paragraph (iv) save in circumstances where it can be found that the Crown has deliberately sought to frustrate or breach the contract as distinct from circumstances where the Crown has properly exercised its discretion and, as an incident of so doing, has frustrated or breached the terms of the contract."[36]

All of that suggests that there is a considerable degree of risk in contracting with the Crown in Australia: however, the reality is as Mr Turner puts it, namely, that any contractual undertaking by the Crown which does not involve any issue of national interest or public welfare, and does not fetter any statutory duty or discretion, is unlikely to be avoided by operation of the doctrine of executive necessity.

There is a recent trend in Australia, however, to corporatise certain government functions. I refer in particular to recent legislative developments such as the *Government Owned Corporations Act* 1993 in Queensland, which was passed on 19 May 1993 but is at the time of writing still awaiting royal assent.[37] In large measure, it follows the trail blazed by Victoria with its *State Owned Enterprises Act* 1992 which was assented to on 26 November 1992. Are contracts or contractual representations made by or on behalf of such government-owned

36. Op cit, pp 103-104, n 34.

37. It is proposed that most of Queensland's major "government owned enterprises" will be corporatised by late 1995 in accordance with the following timetable:

Queensland Industry Development Corporation	January 1994
Port of Brisbane	July 1994
Port of Gladstone	July 1994
Harbours Corporation	July 1994
Queensland Investment Corporation	July 1994
Queensland Electricity Supply Industry	July 1994
Suncorp	January 1995
State Gas Pipeline	January 1995
Queensland Rail	June 1995
Remaining Ports	July 1995
Forestry	By 1995-1996
Water Resources	By 1996-1997

corporations likely to be the subject of the doctrine of executive necessity?

Legislation such as that in Queensland and Victoria must raise the issue of the extent to which a body corporate with some nexus to government should be able to rely on the common law doctrine of executive necessity to avoid its contractual undertakings. Essentially, the argument against the application of that doctrine would assert that a governmentally created body, intended to operate commercially and competitively with other privately owned enterprises on the same playing field, should be subject to precisely the same playing rules as those private enterprises. More precisely, the argument would propose that, once such a body starts competing with private enterprise, it should sacrifice any common law advantages which might give it an unfair competitive edge, and (subject to specific legislative exceptions) shed any common law disabilities which might actually work to its detriment. Certainly, if that were to occur, the government body would be more likely to achieve the objectives of the legislature in providing for the corporatisation of the body.

This section of the paper will, by way of case study, briefly consider the major features of Queensland's *Government Owned Corporations Act* and then highlight, by reference to particular statutory provisions, why it would be inappropriate for a government-owned corporation (for brevity, in both the Act and this paper referred to by the acronym "GOC") formed under that legislation to be able to avail itself of the benefit of the common law doctrine. I hope also to demonstrate that, although the common law doctrine should not apply to a GOC, the legislature has in any event included provisions into the GOC Act akin to a statutory embodiment of certain aspects of the policy underlying that doctrine. In that regard, indeed, if a government entity is to become truly corporatised, then surely the only satisfactory way in which the special position of such an entity should be acknowledged is by enacting specific legislative provisions, rather than by relying on a nebulous common law doctrine the ambit of which has not been finally determined in this country. In that way, at least if the playing rules are not the same, all parties are on notice of any handicaps which exist and the precise effect that they might have on the outcome of the game.

Introductory concepts under the GOC Act

The express purpose of the Act is to enable nominated government-owned enterprises to become bodies corporate, on a common basis more akin to companies under the Corporations Law than under the plethora of various statutes under which a number of them are already statutory bodies corporate. Essentially, the process of "corporatisation" (to be distinguished from "privatisation") involves the application of private sector commercial principles to public utilities and financial institutions in an attempt to improve their economic performance while retaining government or public sector ownership. These government-owned entities are to be managed by experienced and commercially oriented boards, subject only to limited areas of government direction.

Candidates for corporatisation range from existing statutory bodies corporate, to State instrumentalities, agencies and authorities, to government departments, and to any "entity prescribed by regulation".[38]

A GOC will be any government entity which is established as a body corporate either under an Act or under the Corporations Law and which is declared by a regulation to be a GOC. A GOC established under a specific Act is a statutory GOC, and that established (by incorporation or registration) under the Corporations Law is a company GOC:[39] the most significant difference between those two types is the extent to which the Corporations Law applies. A statutory GOC is subject to the Corporations Law only to the extent to which that Law is expressly applied to the GOC by regulation,[40] whereas the Corporations Law applies to a company GOC except to the extent that the GOC Act otherwise provides.[41] In fact, the GOC Act provides that the Corporations Law is to apply to a GOC to the greatest extent possible subject to any necessary modifications and any modifications prescribed by regulation.[42]

Legislative intention

A review of the background and objectives of the GOC Act (as set out in Pt 5 of Ch 1 of the Act) must in my view support the proposition that the doctrine of executive necessity should not apply to the contractual representations and dealings of a GOC, whether statutory or company. In particular, the language of the following provisions is inconsistent with the retention of such an advantage:

- Section 16(a) provides that corporatisation is a structural reform process for nominated government entities which:

  > "changes the conditions and (where required) the structure under which the entities operate so that they operate, as far as practicable, *on a commercial basis and in a competitive environment*".

- Section 17 states the objectives of corporatisation to be the improvement of Queensland's overall economic performance, and the ability of its Government to achieve social objectives, by improving the *efficiency, effectiveness and accountability* of GOCs.
- Section 18 adopts four "*key principles of corporatisation*" (particularised in s 19). Of particular interest is "Principle 4—Competitive Neutrality", which includes the following elements:

  > "The efficiency of overall resource use in the state is promoted by ensuring that *markets are not unnecessarily distorted*;

38. ss 5, 24.
39. ss 65, 66.
40. s 67.
41. s 69.
42. s 14.

—. . . to ensure, wherever possible, *that each GOC competes on equal terms with the private sector and any special advantages and disadvantages of the GOC because of its public ownership or its market power will be removed, minimised or made apparent.*"

- Section 20(1) provides that a key objective of a GOC is to be "commercially successful" in the conduct of its activities.

Those provisions at least underscore the key characteristics of commerciality and competitiveness in the operations of a GOC. And the principle of competitive neutrality provides a strong argument against the application of the common law doctrine of executive necessity to the operations of a GOC.

How is a GOC created?

In general terms, the relevant government entity first acquires the status of a "candidate GOC" before becoming either a statutory GOC or company GOC—and a statutory GOC must again become a candidate if it is to subsequently convert to a company GOC. In either event, it becomes a candidate simply by virtue of its nomination as such by regulation.

A candidate GOC is given a corporatisation charter, setting out the steps by which it will become a GOC (or, if then a statutory GOC, by which it will convert to a company GOC) and how the key principles of corporatisation will in its case be implemented.[43] A candidate will become a GOC following preparation and implementation of its corporatisation charter, although the GOC Act does countenance "appropriate cases" where an entity may do so even though it has not prepared or implemented such a charter.

The GOC Act provides mechanisms to facilitate the corporatisation process: a presently unincorporated entity may by regulation become a body corporate on a specified day; and an existing statutory corporation similarly becomes a body corporate when by regulation the person constituting the entity vacates that office. The regulation may in either case deal with existing assets and liabilities, and their transfer to and assumption by the body corporate.[44]

If the relevant entity is to become a company GOC, then it is expressly authorised by s 60 of the GOC Act to transfer its incorporation to the Corporations Law and become registered under Div 3 of Pt 2.2 of the Law (which deals with the registration of non-companies as companies). Specifically, s 135(a)(i) of the Law provides that a non-company is not entitled to be registered under that Division unless transfer of its incorporation is authorised under the law of its place of origin.

Existing legal relationships are intended to remain undisturbed by the corporatisation process: the process is not to render the entity or the State in breach of contract or confidence, or guilty of a civil wrong, nor

43. s 28.
44. ss 51, 52, 54.

in breach of any instrument (including restrictions on transfer of rights or disclosure of information); and no other party will thereby be entitled to accelerate the termination of any obligation or the payment of any money, nor released itself from any obligation.[45] This immunity is to extend notwithstanding anything in any instrument, express or implied and whether given in writing or orally.

A government-owned entity in fact becomes a GOC upon the Governor-in-Council being satisfied (and so declaring by regulation) that its corporation charter has been sufficiently implemented or that the entity is "otherwise ready", and that it has fulfilled the relevant provisions of the GOC Act.[46] In the case of a statutory GOC, the entity must be established as a body corporate under an Act, must not be registered under the Corporations Law, must have a board of directors and must have a share capital and issued shares. In the case of a company GOC, the entity must be a public company limited by shares within the meaning of the Corporations Law.

It should be noted that a statutory GOC will be an "exempt public authority" for the purposes of the Corporations Law, but a company GOC will not be.[47] The relevance of that definition is that a "corporation" is, in turn, defined by s 9 of the Corporations Law not to include an "exempt public authority". Accordingly, those provisions of the Corporations Law which purport to regulate "corporation" will not apply to a statutory GOC.

Accountability and management

A statutory GOC must have only two shareholders, holding an equal number of shares and equal rights; those shareholders will be its responsible Ministers, being the GOC Minister (presumably the Treasurer) and the portfolio Minister (being the Minister charged with the duty of administering the legislation under which the entity was originally established).[48] A company GOC must have only five shareholders, two of which must be voting shareholders and three of which must be non-voting shareholders. The voting shareholders being its responsible Ministers must have an equal number of voting shares and must be in a position to cast an equal number of votes. The non-voting shareholders must be Ministers nominated by the Premier.[49]

A statutory GOC has a board of directors responsible for:

- its commercial policy and management;
- ensuring that the GOC acts in accordance with its statement of corporate intent and carries out its objectives;

45. s 65.
46. s 63.
47. Section 9 of the Law defines an "exempt public authority" to include a body corporate incorporated within Australia which is:
    (a) a public authority; or
    (b) an instrumentality or agency of the Crown in right of the Commonwealth, a State or a Territory.
48. ss 71, 72, 73.
49. ss 76, 77, 78, 79, 80.

- accounting to its shareholders for the GOC's performance; and
- otherwise ensuring that the GOC performs its functions in a proper, effective and efficient way.

The GOC Act does not make express provision for a board of directors in the case of a company GOC; presumably, that requirement flows from s 221(1) of the Corporations Law, which provides that a public company must have at least three directors. However, s 96 of the GOC Act provides that the board of a company GOC is to comprise those directors so appointed by the Governor-in-Council and that the provision is to have effect notwithstanding anything to the contrary in the memorandum and articles or the Corporations Law. The responsibilities of the board of a company GOC are expressed in the GOC Act in the same terms as those of the board of a statutory GOC.

A statutory GOC is required to have a chief executive officer ("CEO") who will manage the GOC.[50] This officer is to be appointed by the Governor-in-Council on recommendation of the GOC's board. Anything done by the CEO in the name of, or for, the GOC will be taken to have been done by the GOC. A company GOC will have a CEO appointed in the same way, notwithstanding anything to the contrary in the Corporations Law.[51]

Every GOC is required to have a corporate plan which must comply with any guidelines about form and content issued by the GOC Minister.[52] A draft of the corporate plan is prepared by the GOC's board in respect of each financial year and then submitted to the shareholding Ministers for their agreement.[53]

Also each financial year the GOC must adopt a statement of corporate intent consistent with its corporate plan.[54] This statement must include financial and non-financial performance targets, community service obligations, an employment and industrial relations plan, as well as the additional matters set out in s 115(1) of the GOC Act. Once again, the statement must be prepared by the board and then submitted to the shareholding Ministers for agreement.

Continuing government direction

The scheme of the GOC Act as outlined briefly above, with its emphasis on commerciality and extensive parallels with company law and practice, certainly supports the contention that the common law doctrine of executive necessity should not be available to a GOC. Indeed, rather than providing a regulatory framework for a company GOC which is merely analogous to the Corporations Law, a company GOC will in fact be governed by the Corporations Law subject only to the exceptions set out in the GOC Act. However, notwithstanding that

50. ss 97, 98.
51. s 102.
52. s 103.
53. s 106.
54. s 111.

the common law doctrine of executive necessity may have been displaced as a result, the GOC Act itself expressly sets out the circumstances in which the government might still in some way direct the entity's activities even after corporatisation.

The nexus between a GOC and the government is provided by the appointment of "responsible Ministers": these Ministers take on their responsibility upon the entity becoming a candidate GOC. They are not to be treated as directors, however, and do not incur any civil liability for anything done honestly and without negligence (in any event, any liability will attach to the State, not the Minister). These Ministers essentially are analogous to the promoters of a company and control the preparation and implementation of the GOC's corporatisation charter; thereafter, they remain influential in the affairs of a GOC either as its sole shareholders (in the case of a statutory GOC) or its voting shareholders (in the case of a company GOC).

A GOC is required, in its statement of corporate intent, to set out the community service obligations which it will perform.[55] These are defined as obligations to perform activities that are not in the commercial interests of the GOC and which arise because of a direction or notification by the shareholding Ministers or some other duty imposed by the GOC Act, rather than because of the application of certain key principles of corporatisation.[56] In particular, they arise out of the exercise of what are described as the "reserve powers" of shareholding Ministers to notify the GOC board of public sector policies, to give directions in public interest or to direct that assets not be disposed of.

Here the Act crystallises the inherent tension between public interest and commerciality: it expressly contemplates that the government directions which prescribe community service obligations (and which could loosely be regarded as a statutory reformulation of executive necessity) will operate in circumstances in which compliance with those directions, although in the public interest, may well run contrary to the commercial interests of the GOC.[57]

For example, if the shareholding Ministers are satisfied that it is necessary in the public interest, they may notify a GOC that a particular public sector policy is to apply to and to be adopted by the GOC: the GOC's board must ensure that the policy is carried out notwithstanding that it might not be in the commercial interests of the GOC.[58] Similarly, the shareholding Ministers may give a GOC a direction if they are satisfied that, because of exceptional circumstances, it is necessary to give that direction in the public interest: once again, the board must ensure that the direction is complied with notwithstanding that compliance might not be in the commercial interests of the GOC.[59]

However, the GOC Act does limit the extent to which any such direction or notification might work against those commercial interests.

55. s 114.
56. s 121.
57. s 121(1)(a).
58. s 123.
59. s 124.

Where its board suspects that a GOC will or may become insolvent and the cause or a substantial cause of the suspected insolvency would be compliance with a direction or notification of the shareholding Ministers, then the board is required to give notice of that fact to the shareholding Ministers. The ministerial notification or direction is then suspended until, effectively, the board's suspicions are rejected or the direction or notification is revoked.[60]

Further scope for government direction or intervention exists in relation to the disposal of assets and undertakings. The shareholding Ministers have a reserve power, after consultation with the board, to direct that the GOC not dispose of specified assets.[61] Similarly, a GOC may only dispose of any of its main undertakings with the prior written approval of the Minister—"main undertakings" are defined as the undertakings specified as such in the GOC's most recent statement of corporate intent.[62]

Limits on legal capacity of GOC

A statutory GOC is given all the powers (including legal capacity) of a natural person, and the doctrine of ultra vires is expressly abolished consistent with the policy embodied in the Corporations Law.[63] And while a statutory GOC is subject nonetheless to restrictions on its powers expressly imposed under any Act, or by its statement of corporate intent and any directions by its shareholding Ministers, the consequences of any contravention are ephemeral and do not extend to the validity of dealings with outsiders.[64] Again, to reflect the provisions of the Corporations Law, the GOC Act prescribes an "indoor management rule" for a statutory GOC, available not only for a third party dealing directly with the GOC but also for any other party having dealings with a third party which acquired title to property from the GOC—the benefit of the rule may only be displaced by actual knowledge, or by imputed knowledge having regard to the relevant party's connection or relationship with the GOC.[65]

The GOC Act has no need to descend to that level of detail in the case of a company GOC which is of course subject to the provisions of the Corporations Law and general company law. The Act does, however, expressly confer an incidental power to enable the company GOC to do "all things necessary or convenient to be done for, or in connection with, the performance of its functions".[66] Once again, however, the company GOC's powers are said to be subject to any restrictions expressly imposed by any Act[67]—although they are not limited by its

60. s 125.
61. s 161.
62. s 162.
63. ss 148, 149.
64. s 150.
65. s 151.
66. s 152(1).
67. s 152(2).

statement of corporate intent or by directions from shareholding Ministers (as is the case with the powers of a statutory GOC).

It seems clear then that the power of a company GOC to enter into a contract with a third party, and its compellable obligations to perform its contractual undertakings, cannot be subject to the common law doctrine of executive necessity: such a GOC is in no different a position than any other body corporate in its ordinary business dealings. That is the clear intent of the legislature and must displace the operation of the doctrine. I believe the same conclusion can be drawn in relation to a statutory GOC, subject only to the limited scope for ministerial control afforded by s 150(2)(b)—but there again, the "relevant directions, notifications or approvals" relate to the power to enter into the contract, and not to the duty to perform contractual undertakings once entered into.

Conclusion

Whatever justification may exist today for permitting the operation of the doctrine of executive necessity in relation to government entities generically, that justification should not be available in the case of a GOC established under the GOC Act. A gauge of the possible judicial opinion on this matter is provided by the High Court's consideration of an analogous issue in *Bropho v Western Australia*.[68] There, the court had to consider the entrenched presumption that statutory provisions worded in general terms are to be construed as prima facie inapplicable to the Crown. In the course of considering whether such a presumption and the policy considerations which initially gave rise to it were anachronistic in the context of the present proliferation of government enterprises, Mason CJ and Deane, Dawson, Toohey, Gaudron and McHugh JJ observed, in their joint judgment, as follows:

> "Whatever force such considerations may continue to have in relation to legislative provisions which would deprive the Crown 'of any part of [the] ancient prerogative, or of those rights which are . . . essential to [the] regal capacity' . . . , they would seem to have little relevance, at least in this country, to the question of whether a legislative provision worded in general terms should be read down so that it is inapplicable to the activities of any of the employees of the myriad of governmental commercial and industrial instrumentalities covered by the Crown. So to say is not to assert the possibility of drawing a clear and fixed distinction between functions which are properly or essentially governmental and those which are not . . . it is simply to point to the fact that the historical considerations which gave rise to a presumption that the legislature would not have intended that a statute bind the Crown are largely inapplicable to conditions in this country where the activities of the executive government reach into almost all aspects of commercial, industrial and developmental endeavour and where it is a commonplace for governmental commerical, industrial and

68. (1990) 171 CLR 1.

> developmental instrumentalities and their servants and agents, which are covered by the shield of the Crown either by reason of their character as such or by reason of specific statutory provision to that effect, to compete and have commercial dealings on the same basis as private enterprise. It is in that contemporary context that the question must be asked whether it is possible to justify the preservation in our law of an inflexible rule."[69]

Quite simply, if a government enterprise such as a GOC set up under the GOC Act wishes "to compete and have commercial dealings on the same basis as private enterprise", then the old colloquial (if not also equitable) maxim "you cannot have your cake and eat it too" should apply. On that basis, such an enterprise should not be able to avail itself of the common law doctrine of executive necessity, and should be restricted only to express reservations made in the legislation under which the enterprise has been established. Ultimately, such an approach could prove favourable for all parties involved: private parties contracting with such enterprises would have greater certainty in their dealings with such enterprises; and the enterprises themselves would be more truly commercial in their operations and might then be more likely to fulfil legislative objectives such as, say, improving efficiency, effectiveness and accountability as set out in s 17 of the GOC Act.

69. Ibid at 19.