IN THE SUPREME COURT OF NEW ZEALAND

SC 98/2009
[2010] NZSC 117

BETWEEN	GREYMOUTH GAS KAIMIRO LIMITED, GREYMOUTH GAS PARAHAKI LIMITED, GREYMOUTH GAS TURANGI LIMITED AND GREYMOUTH PETROLEUM TURANGI LIMITED First Appellants
AND	SWIFT ENERGY NEW ZEALAND LIMITED Second Appellant
AND	GXL ROYALTIES LIMITED Respondent

Hearing: 5 August 2010

Court: Elias CJ, Blanchard, Tipping, McGrath and William Young JJ

Counsel: M D O'Brien and B S Clarke for First Appellants
G M G Joe for Second Appellant
J S Kós QC, M A Corlett and O C Gascoigne for Respondent

Judgment: 22 September 2010

JUDGMENT OF THE COURT

A The appeal is dismissed.

B The appellants are ordered to pay the respondent costs of $15,000 and reasonable disbursements.

REASONS

(Given by William Young J)

The case at hand

[1] This case concerns a petroleum exploration permit[1] in which an 80 per cent ownership interest was held by Swift Energy New Zealand Ltd (Swift). GXL Royalties Ltd (GXL) has a royalty interest in the permit. Swift wished to assign its interest to the first appellants (to whom we will refer collectively as "Greymouth"). This required the consent of GXL under cl 7.2 of the royalty deed, which permits Swift to assign its interest in the permit if:[2]

> [T]he Grantor [Swift] obtains the prior consent of the Grantee [GXL], which consent shall not be unreasonably withheld, where it is established that the purchaser, assignee or transferee [Greymouth] has sufficient financial capability to meet the obligations under the Permit and this Deed.

[2] Despite GXL withholding consent, Swift and Greymouth implemented the assignment. This resulted in GXL issuing proceedings in the High Court seeking, inter alia, a declaration that the transfer was unlawful on grounds that included complaints that its consent had not been obtained and it had not been established that Greymouth had sufficient financial capability.

[3] In its statement of defence and counterclaim, Greymouth alleged that GXL had refused consent from Swift to Greymouth for collateral purposes, unrelated to Greymouth's financial capability. GXL refused to plead to this allegation, saying that it had a contractual right to withhold consent unless and until the financial capability of Greymouth was established on an objective basis. Accordingly, it maintained that its motive for withholding consent is irrelevant.

[4] Greymouth sought an order in the High Court for more explicit pleadings from GXL requiring it to plead to the allegation of collateral purpose.

[5] In the High Court, Dobson J concluded that a collateral purpose on the part of GXL (if established) might be relevant, and he therefore ordered GXL to plead to that allegation.[3] We note that when the case was before Dobson J, there may have

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1 Petroleum Exploration Permit No. 38742.

2 Clause 7.2(a)(1) of the Deed of Assignment and Overriding Royalty (27 July 2004).

3 *GXL Royalties Ltd v Swift Energy New Zealand Ltd* HC Wellington CIV-2008-485-1776, 30 January 2009.

been some ambiguity as to GXL's stance. According to its notice of opposition, it was relying only on the alleged failure to establish financial capability. But there does not appear to have been any express abandonment of the separate complaint (as pleaded in the statement of defence and counterclaim) that the assignment had proceeded without its consent. This arguably left in contention the reasonableness or otherwise of GXL's withholding of consent.

[6] GXL appealed to the Court of Appeal.[4] It argued that the cl 7.2 requirement that consent not be unreasonably withheld applied only once financial capability had been established. It disclaimed any claim or entitlement to withhold consent on any other basis. On this approach, Swift and Greymouth would win the case if financial capability had been established and would otherwise lose. The actual motivations of GXL were thus irrelevant. Accordingly, GXL maintained that there was no point in inquiring into whether there was a collateral reason for withholding consent.

[7] The Court of Appeal agreed with this argument:[5]

> We are satisfied ... that whatever (if any) collateral purpose GXL may have had in refusing consent is irrelevant. ... We therefore agree with GXL that Greymouth's pleading was irrelevant and GXL should not have been required to plead to it. As a result, it will not need to be considered at trial what, if any, collateral purpose GXL may or may not have had for refusing consent.
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> In summary, GXL's refusal to grant consent will be objectively assessed based on whether or not it received sufficient financial information on which to assess Greymouth's financial viability and, if it did so, whether or not Greymouth had the necessary relevant financial viability. What, if any, collateral motive GXL may have had will not inform this objective analysis.

[8] Greymouth and Swift now appeal to this Court.

The broader legal context

[9] The arguments for the appellants relied heavily on the way in which the courts have addressed limitations on assignment as between landlord and tenant. This necessitates a brief discussion of the relevant principles.

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4 *GXL Royalties Ltd v Swift Energy New Zealand Ltd* [2009] NZCA 433.

5 At [34]-[35].

[10] As between landlord and tenant, the ability of the tenant to assign is usually subject to obtaining the consent of the landlord, with the landlord unable (by reason of either express provision in the lease or the operation of s 224 of the Property Law Act 2007) to withhold consent unreasonably. Where the entitlement to withhold consent to an assignment is subject to a general reasonableness limitation, there can be inquiry into why the consent was withheld.[6] This requires a two-stage inquiry, first into the actual basis for withholding consent and secondly as to whether that basis provides reasonable grounds for withholding consent. Where consent has been withheld unreasonably, the proposed assignment can be implemented without consent and this can be effected on an assign first and litigate later basis.[7] The most likely legitimate reason which a landlord may have for withholding consent is where the assignee may not be able to meet the financial obligations imposed by the lease.

[11] Where consent to assignment is required in other contractual settings, the landlord and tenant cases may well provide assistance. This is particularly so where the language of the clause in question is analogous to what customarily appears in leases and the financial position of the proposed assignee provides the most plausible legitimate reason for withholding consent. In such cases, an approach similar to that taken as between landlord and tenant is likely to be adopted by the courts.[8] Each case must, however, be determined on the basis of the actual contractual wording agreed on by the parties.

Would a collateral purpose on the part of GXL be relevant to the resolution of the case?

[12] Under cl 7.2:

(a) The entitlement of Swift to assign is made subject to the consent of GXL being obtained;

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6 Illustrative cases are *Lovelock v Margo* [1963] 2 QB 786 (CA) and *Tollbench Ltd v Plymouth City Council* [1988] 1 EGLR 79 (CA).

7 *Bromley Park Garden Estates Ltd v Moss* [1982] 1 WLR 1019 (CA).

8 This is adequately illustrated by *WEL Energy Group Ltd v Electricity Corporation of New Zealand Ltd* [2001] 2 NZLR 1 (HC and CA).

(b) GXL's entitlement to withhold consent is made subject to a reasonableness limitation; and

(c) This reasonableness limitation is triggered only if it is established that the assignee has sufficient financial capability.

[13] Before us there was debate whether "sufficient financial capability" is to be "established" to GXL's reasonable satisfaction (that is, a subjective test) or whether it is to be "established" objectively. If the test is subjective, this would leave GXL with a judgment to make. If so, there might be scope for inquiry into the actual reasoning processes of GXL and thus into whether it was motivated by collateral purposes. If, on the other hand, the financial capability criterion is to be assessed objectively, then it might be thought reasonably obvious that GXL's reasoning process is immaterial to whether the criterion was satisfied.

[14] Against that background, the submissions of Mr O'Brien (who carried the burden of the arguments for the appellants) raise two arguments which we must address.

[15] Mr O'Brien contended that the financial capability criterion falls to be considered under the general limitation that GXL may not withhold consent unreasonably. Essentially he argued that cl 7.2 required financial capability to be established to GXL's reasonable satisfaction rather than on an objective basis. In effect, he invited us to construe the clause as if it provided:

> [T]he Grantor [Swift] obtains the prior consent of the Grantee [GXL], which consent shall not be unreasonably withheld, where it is established *to the reasonable satisfaction of the Grantee* [GXL] that the purchaser, assignee or transferee [Greymouth] has sufficient financial capability to meet the obligations under the Permit and this Deed. (emphasis added)

We see this as Mr O'Brien's first and primary argument.

[16] Mr O'Brien also advanced a second and alternative argument. He contended that, even if the financial capability criterion operates objectively, the time-constrained circumstances in which the clause must operate mean that, at least in the first instance, financial capability is required to be assessed by GXL. He contended

that if this assessment was affected by a collateral purpose, Swift was free to assign to Greymouth without consent.

[17] We do not accept Mr O'Brien's first argument. We prefer to construe the clause as meaning what it says.

[18] The effect of cl 7.2 is that GXL did not have to address whether to give its consent unless and until it was established that Greymouth, as proposed assignee, had sufficient financial capability. As GXL has agreed to limit itself to that question (that is, to accept the validity of the assignment if it is held that sufficient financial capability was established), the whole case turns on that issue. GXL's motives, and its reasoning generally, have no relevance to an objective determination by the High Court as to whether it had been established that Greymouth has sufficient financial capability. The Court of Appeal was therefore correct in its determination of the pleading issue.

[19] To adopt Mr O'Brien's construction, we would have to read into the clause words which are not there. If his construction were taken to its logical conclusion, a collateral motive on the part of GXL for withholding consent would enable the transfer to proceed even if Greymouth did not have the required financial capability. We see this as inconsistent with a sensible commercial construction of the clause. As well, on the construction advanced by Mr O'Brien, a dispute as to the validity of a withholding of consent is likely to involve major litigation instead of a relatively confined contest as to whether financial capability was established.

[20] We likewise do not accept Mr O'Brien's second argument. If Swift and Greymouth cannot establish that the financial capability criterion was satisfied (so that the reasonableness limitation was triggered) there was no requirement for GXL to do anything and an inquiry into whether it generally acted reasonably or, alternatively, with collateral purpose would not be consistent with the legal obligations created by cl 7.2. To put this another way, we cannot see how Swift and Greymouth could obtain relief against GXL on the basis that its actions were legally correct but it had a collateral motive.[9]

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[9] Compare *Bradford Corporation v Pickles* [1895] AC 587 (HL).

Disposition

[21] Accordingly, and for those reasons, we are of the view that an inquiry into alleged collateral reasons which GXL may have had for withholding consent is irrelevant to the determination of the case.

[22] The appeal should therefore be dismissed and the appellants ordered to pay the respondent costs of $15,000 and reasonable disbursements.

Solicitors:
Bell Gully, Wellington for First Appellants
Simpson Grierson, Wellington for Second Appellant
Russell McVeagh, Wellington for Respondent