

CONSENTS AND APPROVALS BOILERPLATE CLAUSE

Need to know

A consents and approvals clause establishes the process and manner by which a party may give or withhold consent or approval under a contract. If this clause is not included there is a real risk that courts may interpret the contract differently to the way in which the parties intend.

Key considerations when drafting this clause include:

- the form of providing or withholding the consent or approval (ie whether it is required to be in writing);
- the standard for providing or withholding the consent or approval (ie good faith, reasonableness etc);
- the timing for providing or withholding it (ie specific time stipulation, reasonable time etc); and
- any limitations to providing it (ie conditional, unconditional, absolute discretion etc).

Issues between parties relating to this clause most often arise where the clause states that consent must “*not be unreasonably withheld*” (or a similar phrase). The meaning of this phrase will always depend on the particular contract and circumstances, including the nature and object of the contract and the purpose of the clause.

Typically the grounds for withholding consent under this clause will not be “*unreasonable*” if they relate to, and are not extraneous to, the objects of the contractual relationship, or to the rights, benefits or obligations of the affected party under the contract. If, however, consent is withheld for arbitrary, capricious, dishonest or extraneous reasons, then the withholding will likely be classified as “*unreasonable*”.

THE SAMPLE CLAUSES

Option 1 – Consents and approvals – absolute discretion – neutral drafting

Except as expressly provided in this [deed/agreement], a party may conditionally or unconditionally in its absolute discretion give or withhold any consent or approval under this [deed/agreement].

Option 2 – Consents and approvals – not unreasonably withheld – drafting in favour of party seeking consent

Except as expressly provided in this [deed/agreement], a party may conditionally or unconditionally give or withhold any consent or approval under this [deed/agreement], but that consent is not to be unreasonably delayed or withheld.

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1 What is this clause and why is it used?

Contracts often require one party to obtain the consent or approval of another party to the contract before taking a particular step. A consents and approvals clause is used to clarify and govern the manner by which a party can give or withhold consent or approval under a contract.

1.1 Why is this clause important?

Where a contract is silent on the manner in which consent or approval may be provided, there is a real risk that courts may interpret the contract differently to the way in which the parties intend.

Presently there is uncertainty in Australian law about whether an implied duty of good faith attaches to a party's exercise of its powers under a contract and, if it does, how this duty is implied.¹ Until the High Court specifically examines this area of law, it is not possible to conclusively say whether an implied duty of good faith may be excluded by contract. Nevertheless, the weight of authority at this point suggests that an express exclusion of the duty is likely to negate its application.²

Generally speaking, the inclusion of a consents and approvals clause will substantially mitigate the risk of arguments being raised about implied terms and standards applicable to the provision (or withholding) of consent under a contract. Its inclusion provides a clear indication of the parties' intention about the standard of performance and process they wish to govern the provision of consent under the contract and to safeguard against consent being capriciously withheld or to reserve a party's right to withhold it in their absolute and unfettered discretion.

With this in mind, and to ensure that the appropriate position is adopted, it is imperative that you consider your client's commercial objectives prior to including either sample clause in a contract (ie, is your client more likely to be the provider of consent (option 1) or the seeker of consent (option 2), and does the sample clause need to be tailored further to suit your client and the transaction contemplated by the contract).

1.2 What is typically included?

A consents and approvals clause generally includes:

- specific details about the decision-making process, including which factors the party giving consent may or must take into account and whether reasons are required to support their decision;
- the nature of the consent (ie whether it is conditional);
- the form of the consent (ie whether it is required to be in writing);
- the duration for determining whether to provide consent and the consequence, if any, of not providing it within a required timeframe;
- implications, if any, of further performance of the contract if consent is not obtained; and
- representations or warranties that consent has already been obtained, is obtainable or is unnecessary, in specified circumstances.

2 Specific standards

A consents and approvals clause typically specifies the standard of behaviour to be applied to the decision-making process including:

- whether there is a prohibition on a party acting unreasonably (ie "... *consent must not be unreasonably withheld*". If this phrase is included in the contract "*unreasonable behaviour*" may be challenged (including both unreasonable decisions and any unreasonable delay in making a decision). If, however, it is not included a party has no general obligation to behave reasonably); or
- whether the discretion is absolute (ie, consent is provided "*in [Party X's] absolute discretion*"). That is, the named party has unfettered and complete / sole discretion to decide whether or not they wish to provide consent or approval.

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2.1 Unfettered / absolute / sole discretion

Contractual discretion can apply in a broad range of contexts including, for example, discretion as to whether or not to exercise a power or right and, most relevantly here, whether or not to provide consent or approval.

Where a discretion given to a party in a contract is intended to be unfettered, the discretion is generally expressed to be exercisable by that party in its “absolute discretion” (or sole / complete / exclusive discretion).

Courts have found that the expression “absolute discretion” generally means what it says. For example the New South Wales Court of Appeal, in *Topfelt v State Bank of NSW*,³ said that the words “absolute discretion” are words of ‘emphasis and surplusage’ and that they convey the intention that a party’s discretion is ‘theirs and theirs alone’.⁴ However, the phrase must always be construed in light of the contract as a whole.⁵ In *Railways, Commissioner for v Avrom Investments Pty Ltd*,⁶ the court held, although the lessor had an “absolute discretion” to approve or disapprove plans for a hotel on land subject to a lease, the discretion was qualified by subsequent wording in the contract that required the lessor to exercise its discretion “reasonably”.⁷

Relationship between clauses conferring “absolute discretion” and good faith

Generally, if a consent power is exercised for an improper purpose, arbitrarily, capriciously or unreasonably, the exercise of that power is deemed invalid.⁸ There are, however, some exceptions to the rule.

For instance, Hammerschlag J held, in *Solution 1 Pty Ltd v Optus Networks Pty Ltd*,⁹ that an implied term of good faith was inconsistent with the contract in question (ie which contained an express termination for convenience provision that allowed Optus to terminate the contract for “any reason and at any time” in its “absolute discretion”). In that case the court held, unless expressly excluded or inconsistent with other terms of the contract, parties are under an implied obligation to act in good faith when exercising their contractual powers.¹⁰ The court held that Optus was under no obligation to act in good faith in exercising the right to terminate and

if there was such an obligation that it had not been breached. This case suggests that including explicit wording about the exercise of discretions and rights in a contract may preclude the implied obligation to act in good faith.¹¹

2.2 Requirement to act reasonably

Disputes about the meaning of this clause most commonly arise where the consent or approval must “not be unreasonably withheld.”

Consent or approval clauses that include this phrase are most often disputed in leasing contracts and other real property transactions. There has, however, been judicial support for extending those authorities to a wider commercial context. Recent appellate authorities emphasise that the meaning of the phrase (“not be unreasonably withheld” and those like it), depends in each case on the particular contract and circumstances, including the nature and object of the contract and the purpose of the clause. These authorities are discussed briefly below.

Leading High Court authority

The leading High Court authority is *Secured Income Real Estate (Australia) Ltd v St Martins Investments Pty Ltd (Secured Income)*.¹² In *Secured Income*, a contract for the sale of land provided that all leases of the premises after the contract’s execution (prior to settlement) must be approved by the purchaser, where such approval must not be “capriciously or arbitrarily withheld”.

Mason J (with whom Gibbs, Stephen and Aickin JJ agreed) held that “arbitrarily” connotes “unreasonably” in the sense that what was done was done “without reasonable cause,” and doubted whether “capriciously” added anything further.¹³ On the issue of what constituted “unreasonableness” in this context, his Honour adopted an earlier statement of Walsh J that “the reason for refusal must be something affecting the subject matter of the contract which forms the relationship between the landlord and the tenant, and not something extraneous and dissociated from the subject matter of the contract.”¹⁴

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Secured Income principles extended to commercial contexts

In *Cathedral Place Pty Ltd v Hyatt of Australia Ltd*,¹⁵ Nettle J held that “*logic dictates*” that the approach taken to consents to assignments of leases in cases such as Secured Income should be extended to a hotel manager’s consent to the assignment of the hotel owner under a hotel management agreement.¹⁶ However, his Honour emphasised that the considerations which may relevantly be taken into account when reasonably withholding consent under such a provision will always depend on the particular contract.¹⁷

This approach was endorsed in *EDWF Holdings 1 Pty Ltd v EDWF Holdings 2 Pty Ltd (EDWF)*,¹⁸ which concerned a clause in a joint venture agreement. The clause provided that prior written consent to a change in control of a participant was required, with such consent not to be unreasonably withheld.

Buss JA (with whom Owen and Newnes JJA agreed) held that it was “*essential to exercise caution in reviewing authorities decided in different contractual settings.*” His Honour contrasted the nature of a joint venture transaction with that of a grantor / grantee of a right under a contract or a lessor / lessee relationship, which relationships do not involve the common pursuit of a venture, and in which the fundamental rights and interests of the parties in respect of the subject matter of the transaction will usually be opposed.¹⁹

Buss JA held that, in general, a joint venturer would not be acting unreasonably in withholding its consent if the grounds were held honestly, related to the objects of the joint venture or the rights of a party to it, were permissible under the joint venture agreement and were not unreasonable. If any of those factors was not satisfied then, in general, the joint venturer would be acting unreasonably.²⁰

Subsequently, in *Fulham Partners LLC v National Australia Bank Ltd*,²¹ Basten JA (with whom Bergin CJ in Eq and Barrett JA agreed) considered whether the refusal to agree to an assignment of an agreement to supply consultancy services was unreasonably withheld. His Honour cited the test in Secured Income, but

also noted the importance of the context. His Honour found that the considerations raised in refusing consent were all concerned with the status, both legally and financially, of the proposed assignor and assignee. His Honour held that these reasons were legitimate grounds on which to reasonably withhold consent because they did not relate to matters extraneous to the agreement and were not collateral or improper considerations.²²

While the court emphasised that the question of “*reasonableness*” must be determined by reference to the particular contract, the following principles were also useful in determining the “*reasonableness*” of the withholding. Namely, that:

- it is a question of fact whether the withholding is “*reasonable*” and the expression should be given a broad and common sense meaning;²³
- the “*unreasonableness*” of the withholding is determined objectively having regard to all the circumstances of the case, including the reasons given (or not given) to support the withholding;²⁴ and
- it is objectively unreasonable to withhold consent for the purpose of achieving an objective that is “*a collateral advantage outside the terms of the contract*”.²⁵

In *St Barbara v Hockley [No 2]*,²⁶ Beech J applied the approach outlined in EDWF above, but emphasised that the proper construction of the relevant contract was of “*central significance*” in determining whether the grounds for withholding consent relate to the pursuit of the objects of the contract (ie and are reasonable), or whether they are extraneous (ie and are unreasonable).²⁷

Critically, the party alleging “*unreasonableness*” has the onus of proof and must demonstrate that the withholding was *objectively unreasonable*.²⁸

It is worth noting, however, that facts not known to a party refusing consent, but existing at the time of refusal, may be used at a later time to support the “*reasonableness*” of their decision to withhold.²⁹ Equally, facts existing at the time consent was refused, but not actually or constructively known to the party refusing

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consent, may also be relied on to establish that a reason for the refusal was “unreasonable”.³⁰

2.3 Prescribed instances of “unreasonableness”

In *Lockrey v Historic Houses Trust of New South Wales*³¹ the NSW Court of Appeal gave effect to a consent provision that set out express examples in which consent could be deemed unreasonable.³² In that case, the lessor refused to grant consent for an assignment of a lease and, because the situation was covered by the contract it was unnecessary for the Court to determine the “reasonableness” of the refusal.

This demonstrates that one way to effectively rule out any ambiguity surrounding “reasonableness” is to expressly prescribe circumstances or provide examples in the contract where conduct would be deemed “unreasonable”.

3 Drafting and reviewing the sample clauses

3.1 About the clauses

There are two sample clauses.

Consents and approvals – absolute discretion

This clause is drafted from a neutral position. It states:

“Except as expressly provided in this [deed/agreement], a party may conditionally or unconditionally in its absolute discretion give or withhold any consent or approval under this [deed/agreement]”.

Consents and approvals – not unreasonably withheld

This clause is drafted in favour of the party likely to rely on / require the consent:

“Except as expressly provided in this [deed/agreement], a party may conditionally or unconditionally give or withhold any consent or approval under this [deed/agreement], but that consent is

not to be unreasonably delayed or withheld”.

For reasons discussed in item 1.1 above, it is prudent to include a consents and approvals clause in a contract. This ensures that the parties’ intentions about the process and standard of behaviour applicable to the decision to provide / withhold consent under the contract is clear.

3.2 How effective is it and when should I amend the sample clause?

A consents and approvals clause is effective from an evidentiary perspective. It demonstrates the parties’ intention about the process that should be applied when deciding whether consent or approval shall be provided under the contract.

As with all boilerplate clauses, the sample clauses should be amended to suit the particular needs and circumstances of your client. This may be done, for instance, by setting out specific grounds on which consent or approval may be withheld, or by setting out the circumstances in which consent or approval is not required.³³

ENDNOTES

¹See eg *United Group Rail Services Limited v Rail Corporation New South Wales* [2009] NSWCA 177 where Allsop P at [61, with whom Ipp and Macfarlan JJA agreed, said the issue was “not settled”; similarly in *Acton Real Estate Pty Ltd v Shemiran Pty Ltd* [2011] WASCA 33, Newnes JA, with whom Murphy JA agreed, said it was an “open question.... that... is still to be determined.” See also *CBA v Barker* (2014) 312 ALR 356 and *Royal Botanic Gardens v South Sydney* (2002) 240 CLR 45.

²See *Vodafone Pacific Ltd & v Mobile Innovations Ltd* [2004] NSWCA 15, [198]-[200]. See generally *Lewis v Bell* (1985) 1 NSWLR 731, where the NSW Court of Appeal stated that an implied term would not be found where the parties had directed their attention to the subject matter of the suggested implication and stipulated that no such implication was to be made. This is because the express stipulation meant the proposed implication would not be necessary to give business efficacy to the contract. Recently, in *CBA v Barker* (2014) 312 ALR 356 the High Court re-emphasised that the requirement that a term implied in fact be necessary to give business efficacy to the contract. As a general principle, parties are free to expressly agree that their contract will not include any terms implied by the common law. Further, terms implied by the common law may also be excluded if they are inconsistent with a term or the terms of the contract: *Castlemaine Tooheys v CUB* (1987) 10 NSWLR 468. The weight of authority supports the view that an implied term of good faith will be not be found where there is either an express or implied exclusion of the term.

³(1993) 6 BPR 13,209; [1994] ANZ ConvR 350; (1993) NSW ConvR 55-676; BC9301739.

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- ⁴ (1993) NSW ConvR 55-676; BC9301739 at 14 per Sheller JA.
- ⁵ See generally *Railways, Commissioner for v Avrom Investments Pty Ltd* [1959] 2 All ER 63.
- ⁶ [1959] 2 All ER 63.
- ⁷ *Ibid.*
- ⁸ *Burger King Corp v Hungry Jack's Pty Ltd* [2001] NSWCA 187 at [362].
- ⁹ [2010] NSWSC 1060; *Sundararajah v Teachers Federation Health Limited* [2011] FCA 1031 at [69]-[81] per Foster J. See also *Hampton v BHP Billiton Minerals Pty Ltd* [No 2] [2012] WASC 285.
- ¹⁰ *Solution 1 Pty Ltd v Optus Networks Pty Ltd* [2010] NSWSC 1060, at [61]. See also *Vodafone Pacific Ltd v Mobile Innovations Ltd* [2004] NSWCA 15, at [191].
- ¹¹ Hoffman B, *20 years on from Renard Constructions – is the contractual duty of good faith any clearer?*, Australian Construction Law Bulletin, April 2012, p 25.
- ¹² *Secured Income Real Estate (Australia) Ltd v St Martins Investments Pty Ltd* [1979] HCA 51; (1979) 144 CLR 596; 26 ALR 567 (**Secured Income**).
- ¹³ *Ibid.*, 578.
- ¹⁴ *Secured Income*, citing *Colvin v Bowen* (1958) 75 WN (NSW) 262, at [264].
- ¹⁵ [2003] VSC 385.
- ¹⁶ *Ibid.*, [18].
- ¹⁷ *Ibid.*, [25].
- ¹⁸ *EDWF Holdings 1 Pty Ltd v EDWF Holdings 2 Pty Ltd* [2010] WASC 78 (**EDWF**).
- ¹⁹ *Ibid.*, [113]. The distinction in this context is discussed at some length by Bryson J in *Noranda Australia Ltd v Lachlan Resources NL* (1988) 14 NSWLR 1, [21].
- ²⁰ *EDWF*, [115].
- ²¹ *Fulham Partners LLC v National Australia Bank Ltd* [2013] NSWCA 296.
- ²² *Ibid.*, [89], [96]-[97].
- ²³ *Re Idoport Pty Ltd (In Liquidation) (Receivers Appointed)* [2012] NSWSC 524 (*Re Idoport*), [50].
- ²⁴ *Ibid.*, [51].
- ²⁵ *Ibid.*, [53].
- ²⁶ [2013] WASC 358.
- ²⁷ *Ibid.*, [39].
- ²⁸ *Fulham Partners LLC v National Australia Bank Ltd* [2013] NSWCA 296, [59].
- ²⁹ *Secured Income*, [581-2].
- ³⁰ *St Barbara Ltd v Hockley* [No 2] [2013] WASC 358, at [158]-[182].
- ³¹ (2012) 84 NSWLR 114.
- ³² See also *Esso Australia Resources Pty Ltd v Southern Pacific Petroleum NL (Receivers and Managers Appointed)* [2004] VSC 477.
- ³³ *Esso Australia Resources Pty Ltd v Southern Pacific Petroleum NL (Receivers and Managers Appointed)* [2004] VSC 477, [43].