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39 Pages

FERMENTATION INDUSTRIES (AUST) PTY LTD and ANOR v BURNS PHILP & CO LTD - BC9800135

SUPREME COURT OF NEW SOUTH WALES COMMERCIAL DIVISION
ROLFE J

50210/1997

5 February 1998, 12 February 1998

A matter remitted for determination by an expert.

Circumstances in which the expert's approach can be reviewed by the Court.

Legal & General Life of Australia Ltd v A Hutson Pty Ltd (1985) 1 NSWLR 314; Strang Patrick Stevedoring Pty Ltd v James Patrick & Co Pty Ltd (1993) 32 NSWLR 583; Holt & Ors v Cox (1994-1995) 15 ACSR 330 and on appeal (1997) 23 ACSR considered.

Held that on a proper construction of the agreement the expert proposed to act outside its terms such that his decision was amenable to correction.

I N D E X

Rolfe J

Introduction

On 1 March 1978 Mauri Brothers & Thomson (Aust) Pty Ltd, ("MBT"), and Fermentation Pty Ltd, ("FI"), entered into a Supply Agreement, ("the agreement"), which recited:-

"WHEREAS

A. FI has requested MBT to manufacture the requirements of yeast of FI for supply to its Australian domestic markets and for export and MBT has agreed to do so on the conditions set out in this agreement.

B. As a consequence FI has this day offered to sell to MBT and MBT has agreed to purchase the manufacturing assets of FI upon the conditions more particularly described in the agreement entered into between FI, MBT and one Cedric Axelsen for that purpose."

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Cl1(1) and cl1(2) provided:-

"(1) On the date of completion of the sale and purchase of the manufacturing assets of FI (hereinafter called 'the commencement date') MBT shall commence the manufacture of yeast for and shall supply FI in such quantities and at such of MBT's plants in New South Wales, Queensland or Victoria as [I shall specify and thereafter FI shall subject to this agreement purchase from MBT its requirements of yeast for supply to its Australian domestic markets and for export.

(2) In the event that at any time or from time to time MBT shall choose to do so it may manufacture the whole or any part of the yeast requirements of FI as confirmed to MBT by FI pursuant to cl3 hereof at any one or more of its plants in New South Wales, Queensland or Victoria in which event the price payable by FI for yeast shall be determined ex the plant of MBT in such of the said States of New South Wales, Queensland or Victoria specified by FI as aforesaid and as hereinafter provided."

Cl8(1) provided:-

"The price to be paid by FI to MBT for yeast manufactured under this agreement shall be as follows:-

As to so much of FI's requirements of yeast as do not exceed 3,400,000 kilograms in any year the prices shall be as calculated from time to time according to the principles set out in the Schedule hereto and upon the basis that such prices shall operate ex the factory door of MBT at the plant in New South Wales or Victoria specified by FI in its firm orders placed with MBT pursuant to cl7(1) hereof or if the plant of MBT in Queensland be so specified upon the basis that such prices shall operate at the rail head nearest that plant or free on the truck of FI ex the door of that plant as stipulated by FI in its order. To the extent that

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the prices payable according to the said principles appear in the Schedule hereto it is acknowledged

(i) that they illustrate the application of those principles as at the date of this agreement;

(ii) that the same shall be recalculated so as to reflect the prices to be paid by FI as at the commencement date;

(iii) that the same may be revised from time to time during the currency of this agreement as a result of the application of the said principles and of variances in the cost to MBT of the manufactured yeast;

(iv) that MBT shall give to FI not less than twenty one (21) days notice in writing of any variations in such prices other than variations caused by fluctuations in the cost of labour and molasses which variations shall become effective on notification of which variations MBT shall give as much notice as is reasonable and practicable.

(b) As to any requirements of FI for yeast over and above the quantity of 3,400,000 kilograms per annum the prices to be paid therefor by FI to MBT shall be:-

(i) as to such requirements of yeast as are for the Australian domestic market at prices not exceeding those at which MBT supplies yeast products to any purchaser, user or wholesaler or to any MBT selling division or branch;

(ii) as to such of those requirements as are for export at prices not exceeding those at which MBT supplies yeast products to any other purchaser or to any MBT selling branch or division."

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Cl8(1) drew a clear distinction between the calculation of the price to be paid for up to 3,400,000 kilograms per annum and of the price to be paid for amounts in excess thereof. In the former case the price is to be calculated in accordance with cl8(1), which incorporates the requirements of the Schedule. In the latter case, depending upon where the product was to be sold, the price was to be related to one not exceeding the price charged to specified users. This distinction becomes significant in my opinion.

Cl8 set out further provisions for price adjustments, cl8(2) providing that "MBT shall invoice FI at the price of 38.51 cents per kilogram for compressed yeast or 36.51 cents for cream yeast (as adjusted from time to time pursuant to cl8(1)(a) hereof) for the standard amount and at the price calculated pursuant to cl8(1)(b) hereof for the excess". This reinforced the difference between the two price fixing regimes. Subcl(3), provided that in certain circumstances MBT was to pay FI a rebate on its purchases. In submissions it was accepted that FI's requirements did not exceed 3,400,000 kilograms per annum, so that the price to be paid was governed by cl8(1)(a).

Cl9 provided:-

"In the event that at any time any dispute or difference of opinion arises between MBT and FI as to the correctness of the calculations of the prices as hereinbefore provided such dispute or difference of opinion shall in the first instance be discussed with a view to settlement between nominated representatives of

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MBT and FI and in the event that such representatives are unable to agree shall be settled by the joint decision of the Auditors of MBT and FI who shall act as experts and not as arbitrators and whose decision shall be final and accepted by the parties as such. In the event that such Auditors are unable to reach a decision the matter shall be decided by a Chartered Accountant to be nominated by the President for the time being of the Institute of Chartered Accountants in Australia acting as an expert and not as an arbitrator and the decision of that Chartered Accountant shall be final and accepted by the parties as such."

Cl10 provided:-

"The Auditors of FI shall be entitled at any time and from time to time to have reasonable access to the basic records of MBT from which the prices hereinbefore provided are being calculated and in the event that it shall become necessary for the respective Auditors of MBT and FI to adjudicate upon a dispute or difference of opinion as hereinbefore mentioned such Auditors shall if they consider it reasonably necessary have access to all production costs and calculations in connection therewith."

It was conceded in submissions that if a Chartered Accountant was appointed pursuant to cl9, he or she had the same rights as the Auditors to the records and information specified in cl10. Mr J S Hilton of Senior Counsel, who appeared for the defendant, said that his client had not furnished the information to Mr Warwick Finney, who was the Chartered Accountant appointed in the circumstances contemplated by and pursuant to cl9, because it took the view that the matters he proposed to investigate went beyond those he was entitled to consider under the agreement.

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The Schedule provided a price escalation formula in respect of compressed yeast in one kilogram packs whereby the price to FI, which was stated to be the selling price to it for the base quantity of 3,400,000 kilograms, was agreed to be 38.51 cents per kilogram as at 13 February 1978. This was calculated by deducting from MBT's selling price of 49.6 cents per kilogram as at 13 February 1978 to "largest users", which were defined as parties buying over 50,000 kilograms of compressed yeast per month, an amount derived by deducting from 49.6 cents the total MBT manufactured cost as defined in the Schedule, which was 25.65 cents per kilogram as at 13 October 1977 and was

agreed to be the same as at 13 February 1978, which resultant figure was multiplied by .463. The price, accordingly, was determined by deducting from 49.6 cents per kilogram an amount produced by deducting from that figure 25.65 cents per kilogram multiplied by .463, which produced 38.51 cents per kilogram. That was the initial amount to be invoiced pursuant to cl8(1)(a). Accordingly FI's purchase price was 11.09 cents per kilogram less than the purchase price of MBT to its "largest users".

The manufactured cost comprised components for molasses, electricity and "others" giving a total raw materials component of 14.90 cents per kilogram. To this was added the total direct labour costs of 3.79 cents per kilogram and "other manufacturing expenses" of 6.96 cents per kilogram

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giving the total manufactured cost of 25.65 cents per kilogram. The following four notes appeared:-

"1. Costs and product usages shown are weighted averages of MBT costs (and Product Usages) calculated for MBT's factories in Queensland, New South Wales and Victoria.

The weighted average is based on the previous three (3) months actual volume of production of the product at MBT factories in Queensland, New South Wales and Victoria.

2. Prices of all raw materials used will be those on suppliers' invoices on the date of the Cost Schedule.

3. The labour cost rate ($/Man hour) includes all 'on' costs associated with the direct labour man hours such as pay roll tax, workers compensation, superannuation etc

4. Other manufacturing expenses contain all manufacturing overhead expenses incurred in the manufacture of yeast with the exception of Bank interest, Head Office charges, Research & Development costs, Freight, Distribution costs, Marketing costs and Sales expenses."

The Schedule also provided for the cream yeast price, which was stated to be:-

".. equal to the compressed yeast price minus the cost of packaging materials and raw materials used in Filtration together with the direct labour saving effected as a result of supplying cream yeast rather than compressed yeast. Such adjustment is illustrated as follows:"

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This disclosed that there should be a deduction of two cents per kilogram in respect of cream yeast from the price of 38.51 cents per kilogram, thus producing the figure to be invoiced as provided in cl8.2.

The agreement was for a twenty five year period and, on 26 February 1979, the first plaintiff, for which Mr DJ Hammerschlag of Counsel, appeared, took an assignment of all the rights and benefits of FI under the agreement and, on 28 October 1983, the defendant assumed all of the rights, benefits and obligations of MBT in respect of or arising from or imposed by the agreement. I shall, however, continue to refer to the parties as they are designated in the agreement.

On 7 June 1985 FI and MBT entered into a Deed whereby the pricing provisions of the agreement were varied as set out in the Schedule to that Deed. These variations ceased to be effective as from 30 June 1994 whereupon the parties reverted to the calculation of prices under the agreement.

Until 27 January 1995 the yeast supplied by MBT to FI was compressed and cream yeast, but after that date FI only purchased cream yeast and, on 31 March 1996, it ceased to purchase cream yeast and it has made no purchases since.

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The matters to which I have just referred are taken from the Statement of Agreed Facts and Issues, which was filed on 5

December 1997 and to which the parties adhered at the hearing. That Statement continued:-

"13. The defendant manufactures and supplies bakers' yeast to bakers throughout Australia and has installed certain equipment on the premises of the larger of its baker customers consisting of tanks in which cream yeast is stored with piping and pumps through which cream yeast is conveyed to the bakery houses of those customers. Such equipment is owned or leased by the defendant and no charge is made in respect thereof to the relevant customers.

14. Except in respect of supplies of compressed yeast in certain parts of Queensland the defendant has at all times since 30 June 1994 supplied yeast to its baker customers free into their stores. For deliveries of compressed yeast prices from the defendant's plant in Brisbane to the North Queensland towns of Rockhampton, Townsville and Cairns, a charge additional to the price prevailing in Brisbane and environs is made.

15. On 14 March 1996, pursuant to the terms of the Supply Agreement, Warwick Finney (the 'Expert') was appointed by the Institute of Chartered Accountants in Australia, as an expert to determine a dispute between the First Plaintiff and the Defendant. The terms of the Expert's engagement are set out in a letter dated 14 March 1996, a copy of which is annexed and marked 'B'.

16. The issues referred to the Expert for determination are set out in the Agenda dated 20 December 1994, a copy of which is attached and marked 'C'."

The parties made submissions to Mr Finney and MBT disputes, and has disputed at all relevant times, that he is entitled to determine Items 5, 6 and 7

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in the Agenda, although his decision on Item 7 is not presently relevant. On 9 April 1997 Mr Finney made a determination in respect of Items 1 to 4 and 7, but not in respect of Items 5 and 6. In that determination he referred to the successors of FI and MBT as FIA and BPC respectively.

Items 5 and 6 provided:-

"5. Provision of Capital Equipment.

The selling price as set out in the formula does not elaborate on how this is calculated, however, disagreement between the parties has already led to one settlement between them and generally in commercial dealings one would not expect to see large items of equipment being supplied without some recognition as to the benefit given to the customer. The benefits are quantifiable and substantial. An adjustment is required.

6. Freight Costs

The price payable under cl8(1)(a) p5 is 'ex the factory floor' and as such this charge is made to FI, however, the MBT other Large Users receive their deliveries to their door without charge (excepting one smaller country user (from memory)). It is contended that the FI price should reflect such advantage considering, para8(1)(a)(i) (p8). A similar conflict was settled by MBT in favour of FI.

An adjustment is required."

In his determination Mr Finney considered Item 5 and noted, in para4.8, that the agreement provided that the price of yeast was to be calculated according to the principles set out in the Schedule and upon the basis that the prices operated "ex the factory door" in New South Wales and Victoria and that there was a different requirement in Queensland. He noted

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that the difficulty concerned the price charged to "largest users" and continued:-

"4.11 BPC has made sales to its other 'large users' on a different basis by providing equipment free of charge to such customers and, from FIA's viewpoint, BPC has provided the benefit, interpreted by FIA as a price benefit to those other customers of BPC, which has not been made available to FIA. FIA claims it has consequently been disadvantaged as the terms of the Agreement between BPC and FIA provide that the price chargeable by BPC to FIA be a price determined by the formula set out in the Agreement which has regard to the ex factory door selling price by BPC to its 'largest users'.

4.12 The issue therefore is whether the benefits made available by BPC to its other customers should be recognised in determining the ex factory door large user price for the purposes of determining the price charge to FIA.

4.13 In my opinion, where two or more parties are supplied with goods at a uniform price but one (or more) of them has received a benefit not available to one (or other) of them then the prices, in effect, cease to be uniform. Further, in my opinion whether a benefit is a monetary price adjustment or a non-monetary benefit is not of relevance.

4.14 As the Agreement provides that the price payable by FAI shall have regard, by application of the formula, to the large user price for sales of cream yeast to other large users, in my opinion that large user price chargeable to other users should have regard to the benefits they receive by the provision of equipment by BPC."

In para4.15 Mr Finney set out a calculation by FI and, in para4.16, he said that he accepted its methodology to determine the

adjustment required to the large user price applicable for sales of cream yeast.

He continued:-

"However BPC has rejected the values and the depreciation rate used, without supplying details of the actual costs and depreciation rate applicable. I therefore now request BPC to provide me with the cost of equipment made available free of charge to customers, the date such equipment was provided, the depreciation rate they believe should be used and the interest cost applicable to the investment in such equipment. I will then be in a position to use such information to determine the appropriate adjustment for the provision of capital equipment to large users."

Mr Finney nextly considered Item 6, namely Freight Costs, and continued:-

"4.18 FIA has presented a case for an adjustment to be made to the large user price for any freight costs incurred by BPC in delivering to large users. FIA has referred to cl8.1(a)(i) of the Agreement claiming that the price to FIA 'shall operate ex the factory door of MBT' and noting that FIA accordingly pays the freight for delivery to its customers or to itself.

4.19 It is further pointed out by FIA, inter alia, that large users supplied by BPC receive their deliveries free of any freight charge and that an adjustment should be made in favour of FIA for freight costs incurred by BPC in delivering to large users in order to establish an ex factory door selling price.

4.20 BPC has, in its submissions, rejected the arguments put forward by FIA. Included in its reasons for rejecting FIA's claim, BPC points out that no freight rebates are granted to its customers and accordingly the prices charged to those customers cannot be reduced artificially by a deemed rebate in the manner FIA contends.

However based on the submission made by BPT it would appear that rather than give rebates to its large users, BPC has simply provided freight at its own cost.

4.21 The Agreement provides for the price to be 'ex the factory door of MBT'. I understand FIA is required to incur

freight on yeast from BPC's premises whereas other large users have delivery costs included in their selling price. BPC has not denied or rejected this understanding. I am therefore of the opinion that the price to FIA has ceased to represent the price charged to BPC's large users. Accordingly, I now request BPC provide me with details of the freight costs incurred in delivering to large users where no charge has been made to such users. I will then be in a position to use such information to determine the appropriate freight adjustment."

In his consideration of Items 5 and 6 Mr Finney referred in para4.11 and para4.21 to "other large users". It appears, therefore, that he has taken the view that FI and MBT's "largest users" are to be equated so far as their business dealings with MBT are concerned. The same suggestion appears in para4.13, the assumption being that the parties were to be supplied goods at a uniform price. The agreement was not seeking to establish any equivalence between FI, on the one hand, and "largest users" on the other. It was recognised that FI and MBT would be in competition for the custom of "largest users". Hence a price was struck whereby FI would purchase at a lesser pace than "largest users", thus allowing it to onsell to its customers, including "largest users" at a profit. Different considerations, which are more consistent with the matters to which Mr Finney was referring in considering

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sales to 3,400,000 kilograms, applied to sales over that amount. In the latter case there was a direct equation of the price payable by FI and by other purchasers.

Put shortly Mr Finney concluded that the price to "largest users", which was set forth in the Schedule and was to be the initial invoice price pursuant to cl8.2, had to be adjusted downwards to take into account the benefits to them of the supply of capital equipment free of charge and of the delivery costs, which they were not charged. Thus, when one returns to the initial figure as the selling price to the largest users in the Schedule of 49.6 cents per kilogram it was the view of Mr Finney that that should be, or may have to be, reduced by the value of capital equipment and the freight cost. Another way of achieving the same result would be by increasing the total MBT manufactured cost by adding those amounts. In either event the result would be that the cost to FI would be reduced. There are, if I may respectfully say so, many potential difficulties with this approach, which spring from a proper interpretation of the agreement.

The Proceedings

The proceedings were commenced by a Summons filed on 31 October 1997. The parties filed a Statement of Issues on 30 December 1997, which they agreed stated the issues, viz:-

"1. Whether the Appointed Expert, Warwick Finney is entitled to determine the following matters:

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(a) Whether an adjustment is required in the selling price between the defendant and the first and/or second plaintiff, pursuant to the Supply Agreement, to recognise and take into account the benefits received by other customers of the defendant pursuant to the provision, by the defendant to other customers of capital equipment.

(b) Whether an adjustment should be made to the large user price for the freight costs incurred by the first and/or second plaintiff to take into account inclusion of delivery costs to other customers in the Defendant's Current Large User Price.

2. Whether in the events that have occurred and on the proper construction of the Supply Agreement, the defendant is obliged to furnish to the Appointed Expert such information as is necessary and required by the Appointed Expert to make a decision pursuant to cl9 of the Supply Agreement.

3. Whether the defendant is obliged to provide to the first and/or second plaintiff details of the Current Large User Price.

4. Whether the defendant is obliged to do all things necessary to enable the first and/or second plaintiff to have the benefit of the Supply Agreement."

Those questions all relate to supplies not exceeding 3,400,000 kilograms per annum.

The matter proceeded on the basis of the Statement of Agreed Facts and Issues filed on 5 December 1997 and the Statement of Issues filed on 30 December 1997. No reliance was placed on another document entitled

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"Statement of Issues" filed on 24 December 1997, and no evidence was led apart from the material contained in and appended to the Statement of Agreed Facts and Issues filed on 5 December 1997.

An Initial Point

The matter has come before the Court before Mr Finney has concluded his consideration of Items and 5 and 6, because Mr Finney cannot finish what he perceives to be his task without MBT's records. MBT has refused to deliver up the records because of its view that a consideration of them by Mr Finney goes beyond that which the agreement permits. In these circumstances it has submitted it is not obliged to divulge its confidential business information to him when, as it has submitted, he is acting beyond the terms of the agreement.

In my opinion it is appropriate for the Court to resolve this impasse by considering whether the exercises upon which Mr Finney proposes to embark in relation to Items 5 and 6, as appearing from his initial report, are committed to him by the agreement in his role as an expert. If they are Mr Finney is entitled, at least prima facie, to the documents he is seeking, so that he can complete his task. If they are not he is not entitled to them. So much was not in issue, Mr Hammerschlag submitting that Mr Finney was deciding the matters committed to him by the agreement, and Mr Hilton submitting that he

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was not. I think it an appropriate exercise of discretion that I should decide that issue and the contrary was barely argued.

The Extent To Which The Expert's Duties Can Be Supervised By The Court

By their agreement the parties have provided a dispute resolution procedure in so far as there is a dispute or difference of opinion between them "as to the correctness of the calculations of the prices as hereinbefore provided". The decision of the auditors and, in the event of their being unable to reach a decision the decision of the Expert, "shall be final and accepted by the parties as such". The question arises therefore as to the circumstances in which a Court can interfere with the decision of the Expert. In the word "decision" I include his stated intention to investigate and rule upon a matter in circumstances where he must have access to confidential material to which he would not be entitled if such an investigation is not warranted.

It is convenient to commence a consideration of this question by reference to the decision of McHugh JA in Legal & General Life of Australia Ltd v A Hudson Pty Ltd (1985) 1 NSWLR 314, in which the Court of Appeal was considering a rent review clause, which provided that if the lessor and the lessee were unable to agree on the amount of the current annual open market rental value that question was to be referred for the decision of a qualified valuer acting as an expert and not an arbitrator whose decision "shall accordingly be final and binding on the parties to this

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lease". His Honour was of the view that the valuer was mistaken in assessing the area of a void at the same rate as the rest of the ground floor and that, accordingly, he erred in principle in determining the rent of the demised premises. The question then became whether that error in principle invalidated the valuation.

After a consideration of the relevant authorities to that time his Honour said, at p335:-

"In my opinion the question whether a valuation is*binding* upon the parties depends in the first instance upon the terms

of the contract, express or implied. This was pointed out by Sir David Cairns in the Court of Appeal in Baber v Renwood Manufacturing Co Ltd (at 181). A valuation obtained by fraud or collusion can usually be disregarded even in an action at law. For in a case of fraud or collusion the correct conclusion to be drawn will almost certainly be that there has been no valuation in accordance with the terms of the contract. As Sir David Cairns pointed out, it is easy to imply a term that a valuation must be made honestly and impartially. It will be difficult, and usually impossible, however, to imply a term that a valuation can be set aside on the ground of a valuer's mistake or because the valuation is unreasonable. The terms of the contract usually provide, as the lease in the present case does, that the decision of the valuer is 'final and binding on the parties'. By referring the decision to a valuer, the parties agree to accept his honest and impartial decision as to the appropriate amount of the valuation. They rely on his skill and judgment and agree to be bound by his decision. ... *While mistake or error on the part of the valuer is not by itself sufficient to invalidate the decision or the certificate of valuation, nevertheless, the mistake may be of a kind which shows that the valuation is not in accordance with the contract*. A mistake concerning the identity of the premises to be valued could seldom, if ever, comply with the terms of the agreement between the parties. But a valuation which is the result of the

mistaken application of the principles of valuation may still be made in accordance with the terms of the agreement. *In each case the critical question must always be: Was the valuation made in accordance with the terms of the contract?* If it is, it is nothing to the point that the valuation may have proceeded on the basis of error or that it constitutes a gross over or under value. Nor is it relevant that the valuer has taken into consideration matters which he should not have taken into account or has failed to take into account matters which he should have taken into account. *The question is not whether there is an error in the discretionary judgment of the valuer. It is whether the valuation complies with the terms of the contract."* (My emphasis.)

This posed the question as to what is meant by the failure to comply with the terms of the contract. In that case the valuer was required to determine the current annual open market rental value. Because of the error he had not done this. It may be thought that he had determined another value different from that for which the contract called. Therefore, one may ask: How could it be said that he was complying with the contract? The answer seems to be that his Honour considered that the mistake occurred in carrying out the task committed to the expert by the contract. Thus the expert was trying to find the contractually stipulated value, but in doing so he made a mistake in valuation principle. The mistake was made honestly; In these circumstances his Honour considered that it was not a vitiating mistake, saying at p336:-

"There is also nothing in the nature of the mistake which indicates a departure from the terms of the contract. The mistake was one made in the process of valuation. But it was not a departure from the terms of the contract."

Thus even though error leads to a result, which does not accord with that for which the parties contracted, ie a valuation on a different basis, the fact that it occurred in attempting to perform the task they contractually submitted to the expert means that it does not invalidate the conclusion to which he came. However, if it is said that by committing that error the expert arrived at a value that was not the current annual open market rental value I have difficulty, if I may say so with respect, in concluding that such a mistake was one performed in carrying out the contractual requirement. If on the other hand it is said that the decision was one in the exercise of discretion on which minds could legitimately differ as to the methodology to be applied, provided one reached the contractually stipulated for result, I do not have that difficulty.

In Strang Patrick Stevedoring Pty Ltd v James Patrick & Co Pty Ltd (1993) 32 NSWLR 583 Giles J was concerned with whether a crane had been valued correctly by an expert in circumstances where it was not stated that the valuation was to be binding on the parties. His Honour was of the view that the parties had agreed to accept the valuer's determination as final, provided he acted honestly and impartially and complied with the terms of the contract, even though their agreement did not expressly state that his determination should be final and binding: p588. Subsequently on the same page he said:-

"But even when the valuer's determination is binding provided his valuation was made in accordance with the terms of the contract, as I consider is the position in the present case, that is only the beginning of the inquiry. What does the contract - here, the sale agreement - require of the valuer?"

For present purposes it is not necessary for me to be concerned, as Olsson J was in Bank of South Australia v S A Health Commission (1996) 65 SASR 409, with whether Giles J was correct in his view that the determination in Strang Patrick should be regarded as final and binding. I should also note that in Holt & Ors v Cox (1994-1995) 15 ACSR Santow J followed the decision in Strang Patrick on this point: p333 and I do not discern any statement in the judgment of Mason P on appeal, (sub nom Holt & Anor v Cox (1997) 23 ACSR 590), which casts any doubt on the conclusions of Giles and Santow JJ on this point. Priestley JA agreed with Mason P and, Cole JA dissented, although his Honour did not deal with the point to which I am presently referring.

For present purposes it is appropriate to note that in Strang Patrick Giles J, at p592, said:-

"Once again the first question must be what the asset sale agreement required of the valuer. What is meant by valuing in accordance with proper valuation principles is not as clear as might first appear. McHugh JA, in Legal & General Life .., considered that a valuation would be binding although the valuer had taken into consideration matters which he should not have taken into account or failed to take into account matters which he should have taken into account (at 336), had erroneously taken into account as comparable

rents, rents which were not in fact comparable (at 331), or had mistakenly applied the principles of valuation (at 335). On one view valuation in accordance with proper valuation principles would not permit any of those matters. I consider it is better to ask, in the present case, whether the asset sale agreement required that the valuer use a discounted replacement cost method rather than a comparable sales method, and if so whether it required that there be taken into account hypothetical purchasers in the international market.

I do not think it did. It seems to me that the method to be used, and if the discounted replacement cost method was used the extent of the market considered, were matters left for the judgment of the valuer. His discretion was to determine the value of the crane, and provided he honestly and impartially did so it does not matter that he made a mistake in seeing available comparable sales and using a comparable sales method, or in failing to take account in the admittedly judgmental phase of striking a value of a class of hypothetical purchasers. If there were mistakes, they were mistakes in the course of doing what the asset sale agreements required. As McHugh JA observed in the second of the passages from Legal & General .., set out above, it will be difficult and usually impossible to imply a term that a valuation can be set aside on the ground of the valuer's mistake. The parties have committed themselves to the valuer's honest and impartial, albeit mistaken, exercise of his skills. In my view that is so in the present case."

If I may respectfully say so I discern a difference in approach between McHugh JA and Giles J. When Giles J said:-

"On one view valuation in accordance with proper valuation principles would not permit any of those matters"

he was, in my opinion, saying that the consequence would be that there was not a valuation made conformably with valuation principles and, hence, not a

valuation of the type for which the parties contracted. His Honour differentiated that from the situation before him where he concluded that the methodology to be adopted was within the discretion of the expert. The adoption of that process still produced a valuation, which was not outside the contractual terms.

In Holt the issue was whether an expert valued shares at a "fair price" as he was required to do by the Articles of Association of a company. In carrying out that task the auditor was acting as an expert rather than as an arbitrator. In a detailed judgment Santow J said, at p333:-

"2. Where a valuation is made as an expert, the issue of whether it is binding on the parties, depends on the terms of the contract. If the contract expressly or impliedly, provides that the decision of the valuer is 'final and binding on the parties', a valuation made in accordance with the terms of the contract will be binding as between the parties, even if made negligently, or in mistaken application of the principles of valuation including failing to consider relevant matters or misvaluing the asset."

If I may say so with respect this method of stating the matter causes me some difficulty in the sense that it may pre-suppose that notwithstanding that a valuation was made negligently, or in mistaken application of principles of valuation, it will none-the-less be made in accordance with the terms of the contract. I have sought to explain why, in my view, that will not necessarily be the case: if the valuation is made contrary to principles of valuation it may not produce that which is contractually demanded, viz a "fair value".

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His Honour continued that the question was whether the valuation was made in accordance with the terms of the contract and, subsequently, at p333, he said that it is necessary to determine what the contract required of the valuer. He continued:-

"Where the direction is simply to determine the value of the asset, the inference is that the method to be used was left for the judgment of the valuer, and if so, any mistakes of methodology are mistakes in the course of doing what the contract required .."

His Honour was of the view that there was a non-compliance with the contract created by the Articles of Association in two respects and that, accordingly, the valuation had not been carried out conformably with the contract and was thus susceptible to interference by the Court. He said:-

"First, as I have said, the winding up right is a right attaching to the shares by virtue of the articles. Thus the prospect of its future fructification, stemming from that right, requires to be valued under the contract. Second, the contract requires a fair price, that is to say, a price which is not unfair. To fail to take account of this chance or prospect and of the other matters set out in 9 and 15 above, or to discount that price rather than give it a liberal estimate having regard to the element of expropriation, would not be fair and thus contrary to the contract."

In essence his Honour held that the valuation, by error, failed to meet the contractual requirement. As I have said the decision was upheld by Mason P, with whom Priestley JA agreed. Cole JA dissented. At p597 Mason P said:-

"A close reading of McHugh JA's judgment in Legal & General indicates that his Honour was not propounding the view that a valuation will stand regardless of error.

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Rather he was making the point that mistake is not itself a ground of vitiation: see also Wamo Pty Ltd v Jewel Food Stores Pty Ltd [1983] ANZ Conv R50. A valuation may contain a factual error or embody consideration of matters which should have been taken into account, but it does not follow that the result is outside that which the contract contemplated would be made within the realm of determination by the valuer. As McHugh JA makes plain, 'in each case the critical question must always be: Was the valuation made in accordance with the terms of (the) contract? If it is, it is nothing to the point that a valuation may have proceeded on the basis of error or that it constitutes a gross over or under value' (emphasis added). The statement in the next sentence ('Nor is it relevant that valuer has taken into consideration matters which he should not have not taken into account') must be read in the same context. His Honour is not saying that these matters are never relevant. Rather he is saying that they are not relevant *if* the valuation was in accordance with the terms of the contract."

I have already suggested how the mistake in Legal and General, on this approach, could have led to the conclusion that the contractually stipulated for valuation was not reached. Mason P continued:-

"I have already mentioned Sir Frederick Jordan's apophthegm about 'mistakes and mistakes'. It was uttered in a mandamus case. It seems to me that administrative law provides a useful analogy in the present context. There, the decision maker has an area in which he or she may make mistakes, even mistakes of relevance or law, without failure to exercise the jurisdiction conferred, or exposing the decision to quashing. It is only those mistakes which involve a failure to address something which the statute requires to be taken into account that will expose the decision to judicial review on jurisdictional grounds."

This approach seems to me consistent with finding the contractually stipulated for value. But if the error precludes that there has not been an

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answer to the question the contract propounds. On the other hand if the error simply means that a different answer to the contractually posed question was thrown up, not that the error led to a failure to answer that question, the error does not invalidate the result.

Cole JA considered that the approach of the majority involved the Court's substituting its view as to a "fair" price for that of the duly appointed expert, notwithstanding that he had carried out the task honestly and impartially. His Honour said, p608:-

"To do so is in truth to substitute the valuation of the Court for the impartial valuation of the person to whom the parties have, by their contract, entrusted the valuation task. The contract between the parties was not that the auditor should determine a price for the shares which a Court must be satisfied was fair. The contract was that the auditor should, impartially and honestly, determine what in his opinion was a fair price, and the parties agreed to accept that valuation."

The difference between the majority and his Honour, as I would understand it, is that the majority, upholding the decision of Santow J, were of the view that notwithstanding that the auditor had acted impartially and honestly he had failed to carry out his valuation in a manner which would give a "fair value" because the errors precluded his reaching such a value. Therefore, the errors, which were exposed, showed that the value was not "fair" and, hence the contractual requirement had not been satisfied. Thus, if he had had regard to the matters to which he had not had regard, but come to a

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conclusion which the majority found to be unacceptable, the result would, I infer, have been different, because he would have made a mistake in the course of carrying out the task committed to him by the contract. The mistake discerned by the learned trial Judge and the majority of the Court of Appeal was that the errors precluded him performing the contractual obligations imposed on him ie the error precluded him from reaching a "fair" value and, accordingly, he was not acting conformably with the contract.

In these circumstances it becomes necessary to consider with care the contractual obligations imposed on Mr Finney and whether what he proposes to do goes beyond them. That requires a careful analysis of the agreement.

The Contractual Obligations Imposed Upon Mr Finney

The agreement, of course, does not require Mr Finney to carry out a valuation exercise. It required him to make a determination "as to the correctness of the calculations of the prices as hereinbefore provided".

The "prices" to which reference is being made are:-

(a) "The price to be paid by FI to MBT for yeast manufactured under this agreement .....": cl8(1)(a); and

(b) "... the price to be paid therefor by FI to MBT ...": cl8(1)(b). Those "prices" are to be calculated from time to time:-

(a) according to the principles set out in the Schedule; and

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(b) at the factory door of MBT at the plant in New South Wales or Victoria specified by FI in its firm orders placed with MBT, or if the plant of MBT in Queensland be so specified upon the basis that such prices shall operate at the railhead nearest that plant or free on the truck of FI at the door of that plant as stipulated by FI.

The agreement contemplated that the prices payable initially appear in the Schedule, but that "the same", ie the prices, may be revised from time to time to take account of stated variations. If, which is not relevant in the instant case but is of assistance in construing the agreement, the requirements of FI exceeded 3,400,000 kilograms per annum the prices to be paid were equated to prices not exceeding certain specified prices payable by specified others: cl8(l)(b).

Cl8(2) provided for the invoicing of FI at 38.51 cents per kilogram for compressed yeast and 36.51 cents per kilogram for cream yeast "(as adjusted from time to time pursuant to cl8(1)(a) hereof) for the standard amount and at the price calculated pursuant to cl8(1)(b) hereof for the excess". These are the amounts specified in the Schedule and they were reached by commencing with the "selling price" to "largest users" of 49.6 cents per kilogram.

I have referred to the provisions of the Schedule and to the fact that the starting point for the calculation is 49.6 cents per kilogram as the selling price.

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The formula is tied to that amount and on the basis of it various other calculations are carried out, which produced the amounts referred to in cl8.2 of 38.51 and 36.51 cents per kilogram for which FI is to be invoiced. It is those figures to which, in accordance with the agreement, adjustments are to be made. But those figures cease to be of relevance or contractual significance if 49.6 cents per kilogram is subjected to further modification by taking into account the value or cost of capital equipment and/or the freight costs. The effect of taking into account either or both of those matters would be to alter the price, which the parties have agreed should be the selling price from MBT to FI, and to do so, in my respectful opinion, in circumstances not permitted by a proper construction of the agreement. There is no suggestion in it that there should be parity between the price paid by FI and "largest users" in relation to prices for up to 3,4000,000 kilograms. Indeed that would be contrary to the competition between MBT and FI for, inter alios, those purchasers. The purpose of taking the selling price to the "largest users", which it may be permissible to infer is the most favourable selling price, is to provide a price certain from which the calculations commence and which, in the first instance, give the price at which MBT is to invoice FI as provided in cl8.2. That contractual result could not follow if the agreement permitted adjustments to the 49.6 cents before the 38.51 cents and the 36.51 cents were reached.

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The task committed to Mr Finney does not appear difficult in the sense that the words "selling price", where used as the selling price "to F1" and "to 'largest users' ", appears to have the same meaning, namely the amount paid by the purchaser to the vendor per kilogram. The problem has arisen, if I may say so with respect, because Mr Finney has sought to intrude further considerations into the selling price by MBT to its "largest users". He has suggested that by providing equipment free of charge to "largest users" MBT has provided a benefit, which has not been made available to FI, which sounds in money terms, and that by paying freight costs to such users MBT has provided a further monetary benefit to "largest users", which also sounds in money terms. He proposed to evaluate the amount per kilogram, which those benefits are worth to those users, to arrive at the selling price, notwithstanding that the agreement provided for a specified initial selling price, which is only amenable to change in the manner provided in the agreement. Not only does the agreement not provide in terms for those matters to be taken into account, but there are, in my opinion, positive indications, on a proper construction of it, that they should not be when considering a quantity up to 3,400,000 kilograms. The consequence of taking those matters into account would be that the selling price would be reduced and by the application of the formula in the Schedule the selling price to FI would be reduced.

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The question is whether the contract between the parties permits the MBT selling price to "largest users" to be adjusted in either or both of these ways. If it does then the further question arises as to whether the adjustments would constitute a consideration of "the correctness of the calculations of the prices". In my view that question should be answered in the affirmative. One then returns to the basic question as to whether the formula, read in the context of the agreement, allows for the deductions in the selling price in the manner contemplated by Mr Finney. I consider that it does not.

Firstly, in my opinion the words "selling price" should have a consistent meaning in the formula, and be consistent with the words in the agreement "the price to be paid" and invoiced. When used in determining the price to FI they clearly mean the price per kilogram to be paid by FI to MBT. The contrary was not suggested. Consistency would demand that when used in the context of the selling price to "largest users" they should have the same meaning, ie the monetary amount paid per kilogram by the "largest users" to MBT. The view for which Mr Finney contends would mean that the words have a different meaning in the two parts of the formula which, in itself, would seem to be a strange result.

Secondly, the formula demands consistency. If one is to consider the cost of providing equipment free of charge to the largest users and freight costs to the largest users a problem arises as to what figure one adopts. It seems to

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be a reasonable inference that each of these cost components will differ, at least to some extent, between various "largest users". There is no way of determining whether one takes the highest, the average or the lowest of such costs for the purpose of the exercise to be undertaken. One answer to that may be that that is a matter for the expert judgment of Mr Finney. But the problem with it is that as the agreement states a price certain per kilogram as the selling price to the "largest users" one would anticipate that if the agreement contemplated any reduction in that price the method of bringing about that reduction would have been specified. In the absence of specification the formula, as stated in the agreement, cannot work, or at least is difficult of implementation.

Thirdly, the parties obviously directed their attention to the basis upon which sales were to be made by MBT to FI in relation to delivery costs. Cl1(2) provided that the price shall be determined "ex the plant of MBT". Cl8(1)(a) provided "that such prices shall operate ex the factory door of MBT .." in New South Wales and Victoria, with some variation in Queensland. Accordingly FI is required by the agreement to bear the cost of freight. It would be an extraordinary result, in my opinion, if in the face of those contractual provisions FI was to obtain the benefit of freight costs to others, which are met by MBT, such benefit arising from the reduction in the price per kilogram specified as the selling price to "largest users".

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Fourthly, I do not think it can be overlooked that the parties, in preparing the formula, directed their attention to the amount which should be deducted from the selling price to "largest users" by way of the total manufactured cost. Included in the total manufactured cost is an amount for "other manufacturing expenses". These are expressly defined in Note 4 in the terms to which I have referred, but do not include, inter alia, "Freight, Distribution costs, Market costs and Sales expenses". It may very well be that the reference to "Freight" is a reference to freight into MBT's premises of goods to be manufactured into yeast. However "Distribution costs" is clearly capable of including the cost of transporting the product to "largest users". It would be quite contrary, in my opinion, to the terms of the agreement, if those amounts, which have expressly been excluded from "other manufacturing expenses" and, therefore, in that way have not been deducted from MBT's selling price to "largest users" were to be taken into account by being deducted from that selling price.

Fifthly, "Marketing costs and Sales expenses" appear to relate, or arguably relate, to the provision to customers of capital equipment, which makes it more attractive for customers to purchase MBT's product. Therefore, for the reasons to which I have just referred, the deduction of those from the selling price would have the effect of altering the formula in the same way as "Distribution costs". Even if that not be so there is no suggestion that one

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takes an amount into account to determine the selling price on a proper construction of the agreement. The other difficulty, which is related to the second matter, is what amount should be deducted. Is it the cost to MBT or the benefit to the individual "largest users"? Prima facie it would seem that only the latter could be deducted to take into account the reduction in selling price: ie what constitutes the benefit to the purchaser, rather than the detriment to the vendor.

Sixthly, the formula has to be viewed in the light of the commercial realities confronting the parties. MBT and FI are competitors in the field of selling yeast. In these circumstances MBT has allowed FI a price reduction and FI is at liberty to sell to its customers and, if it can make the price sufficiently attractive, to those of MBT. There seems to be no reason flowing from the terms of the agreement or such a commercial relationship why MBT would have agreed to reduce its price to FI to give effect to trade inducing concessions it may make to its customers. FI is not in competition, as certain of Mr Finney's observations seem to imply, with the "largest users". It is in competition with MBT. However, the formula ceases to apply once the quantity of 3,400,000 kilograms per annum is reached.

The conclusion to which I have come is that the views expressed by Mr Finney in relation to Items 5 and 6 constitute, in my respectful opinion, a misinterpretation of the supply agreement. If he pursues a course of fixing the

price having regard to this misinterpretation then, in my view, he will not be acting conformably with the agreement between the parties for the determination of the selling price to FI. He will be imposing another pricing regime, which the agreement relevantly for present purposes (ie sales not exceeding 3.4m kilograms per annum) does not countenance, and, therefore, he will be going beyond considering the correctness of the calculations of the prices. This he is not permitted to do. If he fails to act in accordance with the agreement then, conformably with the authorities to which I have referred, he acts outside the charter conferred upon him by it and his determination is amenable to review by the Court.

The price is the sum of money or its equivalent for which property is bought, sold or offered for sale: Johnston Fear & Kingham and the Offset Printing Co Pty Ltd v The Commonwealth (1943) 67 CLR 314 at 327; Hooker Investments Pty Ltd v Baring Bros Halkerston & Partners Securities Ltd & Ors (1986) 5 NSWLR 157 at p163; s6(1) of the Sale of Goods Act 1923 and various dictionary definitions. Thus one must find the monetary consideration or some other consideration equal to the monetary amount. The question is whether that price can be subject to a notional discount by the imputed cost to MBT, as seller, of providing benefits to the purchaser. In the course of submissions it was pointed out on behalf of MBT that it would be strange if there was a discount for the cost to the seller,

rather than a discount for the benefit to the purchaser, because the reduction in the price, albeit made notionally, is the value to the purchaser of the benefits, not the cost to the seller.

In his written submissions Mr Hilton referred to cases where it has been held that the amount payable represents the price of the goods acquired, and that it is not permissible to dissect that amount, for the purpose of working out the cost of the goods by reference to the price paid, into various components, such as insurance and freight.

In Re Scremby Corn Rents ex parte Church Commissioners for England [1960] 1 WLR 1227 corn rents were to be determined by reference to the "average price of good marketable wheat in the County of Lincoln during the term of twenty one years ending at Michaelmas 1799". That price was ascertained by an award to be 57-tenths shillings per Winchester bushel. The legislation provided that the amount of the rent should be varied at twenty one year intervals if it appeared that the "average price" of a Winchester bushel of good marketable wheat in the County of Lincoln for the twenty one years then last past was more or less by threepence than the average price set out in the award. In 1959 three arbitrators found that such average price was ten shillings one penny and that in addition to that amount, which was received from the purchaser, the grower received deficiency payments under a certain order, which averaged eleven pence a Winchester bushel. In these

circumstances they awarded the average price to be eleven shillings. On appeal to Quarter Sessions the view was taken that the deficiency payment should not be included in the average price and, on a Case Stated as to whether they should be included as part of the average price, the decision of Quarter Sessions was upheld. It was held that the meaning of the word "price" was unambiguous:-

".. and denoted what a grower or seller could obtain for his wheat when he sold it independent of any additional benefit or subsidy; accordingly, the deficiency payments should not be included in the average price."

At p1234 Lord Morris said:-

"It seems to me that the word 'price' was a word which denoted what a grower or seller would obtain for his wheat when he sold it. I cannot think that if by some other later legislation he was to get from some other source than from his purchaser some additional benefit, that such benefit could properly be comprehended within the word 'price'. I think, furthermore, that there is nothing in the Act which suggests that the corn rents were to be related to nett profits made by owners of land. There is no such notion introduced by the words in question.

I think, therefore, that the word 'price' simply denotes what a grower of good marketable wheat would, on its sale within the County of Lincoln, realise for his wheat. There is, I think, no ambiguity, and, therefore, in agreement with the Court of Quarter Sessions, and with the Divisional Court, I think that the figure upon which to proceed should be that of ten shillings one pence and not eleven shillings."

I appreciate the distinction between the matters there under consideration and the provisions of the agreement in the present case.

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However, I consider that upon a proper construction of the agreement the "price" "selling price" was that specifically defined by the parties without any other deduction.

In Mutual Finance Ltd v Davidson & Anor [1962] 1 WLR 134 there was included in the price of a motor vehicle the cost of insurance, which raised the hire purchase price above £300, which had a relevant effect in relation to the provisions of the Hire Purchase Act 1938. The Court of Appeal held that the insurance was included in the price or, to put the matter in the way for which Mr Hilton contends, that the price should not be discounted by an amount referable to the cost to the dealer of insurance: per Ormerod LJ p139; per Donovan LJ p140-p141 and Pearson LJ at p144. Pearson LJ added:-

"I have considered only the present case, in which there is a single price stated covering the cost of the car and the insurance. I have not considered what the position would be if in the agreement the cost of the car and the cost of the insurance provided by the dealer for the benefit of the hirer were stated separately in the composition of the hire-purchase price."

Mr Hilton also relied on statements in Benjamin's Sale of Goods (4th Edition) at para19-050 and para19-052.

It seems to me that in each case one must look at the particular circumstances in which the word "price" is being considered. I have set out the circumstances in the present case and, for the reasons I have given, I have

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come to the view that the "selling price" of 49.6 cents must mean the invoice price and not a price adjusted in the manner to which Mr Finney has referred.

In my opinion the agreement does not, on its proper construction, require or permit the base selling price, on which the formula depends, to be changed in the way for which Mr Finney contends and, as I have said, if he pursues that approach he is not, in my respectful view, conforming with the requirements of the agreement.

Order

Conclusion

I would propose to answer the questions posed in the Statement of Issues filed on 30 December 1997 thus:-

1(a) and (b): No.

In the result I do not think it necessary to answer the remaining questions, although if the parties seek answers I shall consider the matter" further. The plaintiffs should pay the defendant's costs of the proceedings. The parties should bring in Short Minutes in order to give effect to these reasons.

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