AUSPACIFIC CONSTRUCTION CO PTY LTD v THE ATTORNEY GENERAL ON BEHALF OF THE GOVERNMENT OF KIRIBATI

Unreported,
Court of Appeal, Kiribati,
Civ App no 1/1996, 25 March 1997

Court of Appeal, Kiribati

Facts:

The defendant invited tenders to design and build a prison in a document containing the words, 'This Expression of Intention and any Expression of Interest ... will become binding only on a bidder and the government after a formal Memorandum of Agreement has been agreed and executed by both the successful bidder and the Government'. On 26 May 1994, the plaintiff submitted a tender. On 29 July 1994 the Secretary for Finance and Economic Planning wrote to the plaintiff saying the tender had been accepted by the relevant committee and that a copy of the agreement would be sent for the plaintiff to sign, if the terms in it were agreed. The plaintiff's managing director received the agreement some time in October. The terms provided for progress payment and required the tender to contain an undertaking to obtain a performance bond from a bank for 10% of the contract price.

The agreement was not signed by either party and on 18 November 1994 the plaintiff wrote to the defendant saying that it was suspending work relating to the contract in Australia until the agreement was signed. The letter enclosed an invoice for preparatory work and associated fees. On 9 December 1994 the plaintiff's managing director signed the agreement. At about the same time, the defendant raised the question of the performance bond and the plaintiff indicated that it would be given within 30 days of the first progress payment. The defendant did not agree that this was the effect of the relevant clause. The plaintiff wrote to the defendant indicating that this insistence on the performance bond being given earlier was a change in the agreed terms and that unless the defendant confirmed its commitment to the agreement within two days legal proceedings would be commenced.

Claim:

The plaintiff sued the defendant for damages for breach of contract. On appeal an alternative claim for recovery of preparatory expenses was also made.

Outcome:

The defendant's appeal against the High Court decision that there was no concluded agreement was dismissed with costs.

Legal Principles:

Ratio Decidendi

A letter indicating acceptance of a tender, which contemplates the consideration of terms in and the signing of a further document cannot amount to acceptance, but is only a step in the negotiations.
• Where the intention of the parties is that they will not be bound until both sides have executed a formal agreement no concluded contract can arise until that has been done, as execution is a condition precedent to a concluded contract.
• Where execution of a formal document by both parties is a condition precedent to a binding agreement, the delivery of the unexecuted document does not amount to an offer, but is merely a step in the negotiations. Accordingly, a contract cannot result from unilateral assent to the terms in the document. Nor can it result from execution of the document by one party only.
• In order for estoppel to arise it must be shown that the party against whom it is alleged represented that a binding agreement existed.

Obiter Dicta

Words in an advertisement indicating that agreement is subject to execution of a formal document preclude the possibility that the advertisement may be construed as an offer.
• An invitation to tender which is not an offer and which indicates an intention by the advertiser not to be bound until a formal agreement has been executed does not preclude a binding agreement arising pursuant to subsequent negotiations, without execution of a formal document.
• A clause requiring an undertaking to be given to obtain a performance bond, which does not make it clear when the bond is to be given is probably meaningless.

Commentary:

Invitations to Treat

In this case the delivery of a standard form of agreement by the defendant to the plaintiff was alleged to be an offer. The court held that it was a statement of intention rather than an offer. A 'statement of intention' is known in law as an 'invitation to treat'. The court held that it would depart from commercial reality to regard the defendant's statement of intention as an offer. This is the very reason why advertisements are not generally regarded as offers, but as invitations to treat (see eg, *Partridge v Crittenden* [1968] 2 ALL ER 421). To hold otherwise would mean that every advertiser and catalogue publisher is obliged to sell to every person who responds, regardless of the level of supply. However, if the advertiser makes it clear that he or she is prepared to be bound in certain circumstances, an advertisement may be construed as an offer (see eg, *Carlill v Carbolic Smoke Ball Company* [1893] 1 QB 256). This rule applies equally to advertisements for tenders (*Spencer v Harding* (1870) LR 5 CP 561). Thus, an invitation to tender that indicates that the highest or lowest tender (as the case may be) will be accepted may be construed as an offer. One way of ensuring that an advertisement is not construed as an offer is to state in it that it is not intended to give rise to a binding relationship. In this case the words, '*This Expression of Intention and any Expression of Interest ... will become binding only on a bidder and the government after a formal Memorandum of Agreement has been agreed and executed by both the successful bidder and the Government'* were used. This precluded the possibility that the invitation to submit tenders could be construed as an offer, because the words showed that it was not the intention of the Government to be bound on acceptance.

Where the invitation to submit tenders is construed as an invitation to treat, a tender bid will normally constitute an offer, which may be accepted by the offeree. However, it is common practice for negotiations to take place after close of tenders. These negotiations may include a counter-offer by the original offeree or a fresh offer by the original offeror. This may lead to difficulties in identifying whether a binding

agreement has been concluded (see eg, *Sivans Transport Ltd v Nadi Town Council* (1981) 27 FLR 192; *Beti v Aufiu,* unreported, High Court, Solomon Islands, civ cas 170/1990, 9 May 1991) as it did in this case. The court then has to analyse the subsequent dealings between the party to see whether agreement was ever reached. In this case it was held that it had not been.

Conditional Acceptance and 'Subject to' Agreements

Parties to an agreement may use the words 'subject to' to indicate an intention not to be finally bound, as where an offer is accepted 'subject to the preparation of a formal contract', in which case there is no binding contract until the formal contract is executed. The words 'subject to contract' may also be used to indicate that the parties are still in the course of negotiation. If the words 'subject to contract' indicate that terms have yet to be settled by a future agreement between the parties, this is an agreement to agree. Because some of the terms have yet to be decided there is no final assent and the agreement is incomplete. The implication that the parties do not intend to be bound, arising from the words 'subject to contract' may be displaced by words or conduct of the parties suggesting the contrary.

A similar case, which arose in Fiji Islands is *Prasad v Hussein* ((1967) 13 FLR 98), where Hammett J held that the parties had been in negotiation and had reached agreement on some terms as to the sale and purchase of the plaintiff's property to the defendant. One term of the agreement was that the parties would enter into a formal contract. However, there were other necessary terms that had not been agreed upon at all, such as the date for completion of the sale and the date for possession of the property, which would also be dealt with in the formal contract. Accordingly, judgment was given for the defendant.

In this case the parties did not specifically use the words 'subject to' in respect of their intention to enter into a formal contract. However, it is clear that agreements may be held to be subject to execution of a formal contract by implication from the facts, even though the parties have not expressly stated this. In *Curran v Rankin* ((1964) FLR 212), a draft agreement for sale and purchase was agreed between the parties. On the evidence it was found that it was not their intention to be bound until a formal contract had been executed. As it never had been, an order for specific performance was refused.

In *Masters v Cameron* ((1954) 91 CLR 353 at 360) the High Court of Australia stated that 'subject to contract' agreements fall into three classes:

> The parties have reached agreement, intend to be bound immediately, but intend to have their agreement put into a formal document which may be fuller or more precise but no different in effect.
> • The parties have reached agreement on all terms, but nevertheless intend performance of one for more terms to be conditional upon entry into a formal agreement.
> • The parties do not intend to finalise their agreement until they execute a formal agreement.

The High Court stated that in the first two cases there was a binding contract, whereas in the last case there was not.

Courts in the South Pacific continue to demonstrate reluctance to enforce an agreement prior to execution of a formal written document. In *Prasad v Hussein* ((1967) 13 FLR 98 at 101) Hammett J expressed the view that the three categories set out in *Masters v Cameron* ((1954) 91 CLR 353) were not exhaustive and emphasised that if the parties were still negotiating any of the necessary terms of their bargain there would be no enforceable contract. Similarly, in *Curran v Rankin* ((1964) FLR 212 at 217 to 219) Mills-Owens CJ appears to suggest that Fiji Islands will follow the English common law approach of regarding a 'subject to contract' agreement as unenforceable unless there is cogent evidence of a contrary intention (see further Law Commission (Eng), '*Subject to Contract' Agreements*, No 65, 1975 and Working Paper No 51).

Estoppel

On appeal in this case, the plaintiff submitted an alternative claim for the cost of preparatory expenses. It was argued that the defendant was estopped from denying the existence of a contract as it led the plaintiff to believe that a binding contract exited and was thus estopped from denying the existence that contract. On the basis of that belief the plaintiff argued that it had carried out preparatory work in Australia and thereby incurred expenses.

Clearly, as the Court of Appeal pointed out, estoppel requires a promise to have been made by the person against whom estoppel is alleged. There must also be an existing relationship between the promisor and the promisee. Promissory estoppel cannot arise in a vacuum. It can only arise where there is an existing legal relationship between the parties (*Combe v Combe* [1951] 2 KB 215). In this case the parties were found not to have entered into any relationship and therefore estoppel was also prevented from applying for that reason.

Under the English common law estoppel cannot be used to found a course of action, but only as a defence. This restriction does not apply in Australia, where the common law has developed a more extensive role for estoppel. In *Waltons v Maher* ((1984) 164 CLR 387) and *Commonwealth of Australia v Verwayen* (1990) 170 CLR 394 the doctrine has been used to create new rights. These cases support a wide, general doctrine of estoppel preventing unconscionable conduct. The Australian common law has been followed elsewhere in the region, by the High Court of Fiji Islands (*Nair v Public Trustee of Fiji and the Attorney-General of Fiji* (unreported, High Court, Fiji, CAN 27/90, 8 March 1996). Lyons J considered the restrictions that had been put on the doctrine of estoppel by English courts and preferred the wider doctrine of unconscionable conduct, 'free from the fetters of the English Court's insistence on the analogy which waiver and estoppel imposed on it'. The Court of Appeal of Fiji Islands also followed the Australian approach to estoppel in *Attorney-General of Fiji v Pacoil Fiji Limited* (unreported, Court of Appeal, Fiji, cc496/1992, 29 November 1996).

Meaningless Clauses

Provided the rest of the contract forms a concluded agreement a meaningless clause can often be ignored. In *Nicolene Ltd v Simmonds* ([1953] 1 QB 543) the contractual documentation contained the statement 'we are in agreement that the usual conditions of acceptance apply'. Since there were no 'usual conditions', it was held that this was a meaningless phrase, which could be ignored. There was still a finalised agreement, which could be enforced. In this case, 4.1(c) required the plaintiff to undertake in the tender bid to obtain a bond or guarantee but failed to specify when this undertaking had to be fulfilled.

The Court of Appeal stated that it had no doubt the wording of the performance bond clause would not be used again. The defendant has presumably acted upon this by deleting the meaningless phrase from its standard form agreement and replacing it with a professionally drafted clause.

Performance Bonds

It is a common commercial practice for contractors assuming duties under a contract to be asked to provide a bank guarantee of performance. If the contractor does not fulfill its duties and the principal is obliged to employ a third party to complete the job, any additional cost involved in this may be claimed from the bank under the guarantee. The bank will provide the guarantee on behalf of its customer in return for a counter- guarantee or indemnity from the customer. Obviously, the bank will not be prepared to give a guarantee unless the customer provides it with sufficient security to cover its potential liability.

A performance guarantee is sometimes called a 'performance bond' or a 'standby letter of credit'. It is an unconditional obligation to pay the beneficiary upon demand and upon presentation of any documentation

specified in the guarantee agreement. Such guarantees have been said to be 'virtually promissory notes payable on demand' (per Denning LJ in *Edward Owen Engineering Ltd v Barclays Bank International Ltd* [1978] 1 All ER 976).

The Status of Australian precedents in Kiribati

Section 6(1) of the Laws of Kiribati Act 1989, which is still in force, states:

Subject to this section, the common law of Kiribati comprises the rules comprised in the common law, including the doctrines of equity, of England (in this section referred to as 'the inherited rules'), as applied in the circumstances pertaining, from time to time in Kiribati.

It is further provided that the common law of England will only have effect as part of the law of Kiribati if it is consistent with an enactment or an applied law and with customary law (s 6(3)). Although the common law is not subject to a 'cut-off date', that is a date after which it will cease to apply, this is arguably the effect of s 13(1) of the Laws of Kiribati Act 1989, which provides that decisions of foreign courts are no longer binding on courts in Kiribati (See further Corrin Care et al, 'Introduction to South Pacific Law', 1999, London: Cavendish, 73.

The reference in s 6(1) to the common law of 'England' makes it clear that it is the common law of England rather than the common law that has developed elsewhere in the Commonwealth that has been adopted. In this case the Court of Appeal followed Australian precedents. The case of *Waltons Stores (Interstate) Limited v Maher* ((1988) 164 CLR 387) departed from the English approach to estoppel, by allowing the doctrine to be used to found a cause of action. Similarly, *Masters v Cameron* (1954) 91 CLR 353 does not reflect the English common law relating to conditional contracts (see above). The court did not say why it was departing from the English common law, but it was no doubt influenced by its constitution by Australian judges.

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