IN THE HIGH COURT OF NEW ZEALAND
WELLINGTON REGISTRY

CIV-2010-485-2122

UNDER	the Arbitration Act 1996
IN THE MATTER OF	an arbitration
BETWEEN	TODD PETROLEUM MINING COMPANY LIMITED Plaintiff
AND	SHELL (PETROLEUM MINING) COMPANY LIMITED Defendant

CIV-2010-485-2126

AND UNDER	the Arbitration Act 1996
IN THE MATTER OF	an arbitration before the Honourable B J Paterson QC
BETWEEN	SHELL (PETROLEUM MINING) COMPANY LIMITED Plaintiff
AND	TODD PETROLEUM MINING COMPANY LIMITED Defendant

Hearing: 18 and 24 May 2011

Counsel: H N McIntosh and M F Mabbett for Todd
J E Hodder SC and T D Smith for Shell

Judgment: 30 June 2011

RESERVED JUDGMENT OF DOBSON J

Contents

Background

[1] These two proceedings constitute originating applications by each party to an arbitration, for leave to appeal from aspects of an arbitral award dated 28 July 2010.

[2] The dispute being arbitrated arises out of the management of the Kapuni gas and condensate field which is operated by the parties as joint venturers. It is sufficient to identify the parties to the arbitral proceedings simply as "Todd" and "Shell".

[3] As joint venturers in a number of ventures to produce petroleum in the Taranaki area, Todd and Shell are committed to using an operating company, Shell Todd Oil Services Limited (STOS) to undertake on their behalves the management of physical works. Within the governance of STOS, Shell has a casting vote. In circumstances where Shell has the right to resource STOS with Shell personnel, and to use Shell systems, STOS's operations are described as "Shellcentric".

[4] The terms for employment of STOS at Kapuni contemplate that it will propose work to be done for the venture, essentially of two types, at a cost that is categorised as either operating costs, or capital costs.[1]

[5] The present dispute arises out of decisions by STOS to include in the 2007 work programme and budget (WP&B) for Kapuni a series of expenses which STOS purported to treat as operating costs of the Kapuni venture. These can summarily be characterised as:

- sub-surface costs (incurred in appraising the prospects of further production, or possibly maximising production from Kapuni); and

- disputed allocated costs (relating to expenditure not specifically incurred just for work at Kapuni, but which STOS committed the Kapuni venture to pay as a contribution to costs for systems that were to be used at other fields where STOS was also the operator, in particular at another major Taranaki offshore field, Maui).

[6] The parties' dispute was first submitted to arbitration before the Honourable B J Paterson QC in the course of 2007. The first hearing occurred over nine days in February 2008, leading to an award described as interim by Mr Paterson on 10 October 2008.

[7] Both Todd and Shell sought to challenge elements of that first award, and the matter came before me in May 2009 as applications by both parties to set aside parts of the arbitrator's award. I upheld aspects of both applications on grounds that the arbitrator had exceeded his jurisdiction and had made a determination in breach of natural justice.[2] Those are among the grounds for setting aside an award provided for in Article 34 to Schedule 1 of the Arbitration Act 1996 (the Act). In that judgment, whilst recognising I may not have jurisdiction to do so, I invited the parties to resolve a set of issues to be determined in order to guide themselves and

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1 These are provided for respectively in clauses 13 and 6 of a 1955 agreement between the parties, and are set out in [15] below.

2 *Todd Petroleum Mining Company Ltd v Shell (Petroleum Mining) Company Ltd* HC Wellington CIV-2008-485-2816 , 17 July 2009.

the arbitrator. I recorded my contemplation that the re-hearing would be on the basis of evidence previously heard so that the leave of the arbitrator would be required before a party could adduce further evidence.[3]

[8] Within approximately the same timeframe, Todd and Shell were also in dispute as to the scope of STOS's control over assets associated with the Kapuni venture. Whereas the parties had previously jointly supplied gas to a co-generation plant at Whareroa, in 2006 Todd contracted to separately supply gas to that plant from Kapuni. The core of this second dispute related to Todd's entitlement to separately use the Whareroa pipeline from Kapuni to the co-generation plant, and the basis on which it ought to be charged for doing so. That dispute was also referred to arbitration before Mr Paterson, who convened a hearing over some 18 days and delivered an award on 10 July 2009. Again, both parties were unhappy with different aspects of that award, and both sought leave to appeal it. In March 2010, I delivered judgment on those applications, partially granting each of them.[4] The scope of the questions on which leave to appeal ought to be granted in relation to that arbitration still awaits a substantive hearing in the Court of Appeal, of an appeal from my March 2010 judgment.

[9] More of the background to the Todd/Shell relationship is reviewed in my earlier judgments, and I will not repeat it here.[5]

[10] Returning to the present dispute about the scope of operating costs for Kapuni, subsequent to my judgment dealing with the first award, the parties did exchange views about the list of issues in a series of memoranda between 28 August and 28 October 2009. A telephone conference was held with the arbitrator on 3 November 2009 and his Minute of it recorded:

> **ISSUES**
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> 3. As the pleadings stand at present, the matters for determination will be those which arise from the claims in the pleadings and the evidence which has already been adduced. In this respect Todd has acknowledged that no contractual duty of good faith was pleaded

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3 At [86].

4 *Shell (Petroleum Mining) Company Ltd v Todd Petroleum Mining Company Ltd* HC Wellington CIV-2009-485-2024, 5 March 2010.

5 17 July 2009 judgment at [5]-[11]; 5 March 2010 judgment at [2]-[8].

> and Shell has acknowledged that it will be necessary to determine whether there is a casting vote at the KMCs'[6] level regardless of whether or not damages are payable.

[11] The arbitrator convened a hearing on the second argument of the present dispute between 10 and 13 May 2010, and produced his interim award dated 28 July 2010. The essence of the interim award was that STOS was not entitled to call for the disputed sub-surface costs to be paid as operating costs. Rather, they were in the nature of capital expenses. The consequence of this categorisation is that a venturer could elect not to pay its proportionate part of such costs, but instead accept a proportionate diminution in its share in the venture, relative to the expenses not contributed to.

[12] As to the disputed allocated costs, the arbitrator determined that STOS could properly charge those, notwithstanding that they had been incurred by virtue of a decision in relation to the Maui venture rather than Kapuni.

[13] In his interim award, the arbitrator declined to decide the issue of whether Shell had a casting vote at a meeting of the KMCs. He invited an application if either party sought such a ruling, and subsequently on 13 October 2010 issued a separate ruling (the casting vote or CV ruling) in which he again declined to determine the issue.

Contractual framework

[14] As to the contractual framework, Todd and Shell first committed themselves to a joint venture agreement in 1955 (JV55). The two organisations agreed to pool their Crown petroleum prospecting licences, and to form a services company to be employed by both of them to do the prospecting and mining on behalf of their joint venture. The third schedule to JV55 set out terms on which STOS would be employed to do the prospecting and mining for petroleum on behalf of Shell and Todd. The terms of that schedule are variously referred to by Todd as the STOS Employment Agreement (SEA), and by Shell as the Contract of Employment.

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[6] The acronym "KMCs", as an abbreviation for "Kapuni Mining Companies" is used by the parties to refer to both Todd and Shell when they are interacting in their capacity as the venturers at Kapuni.

[15] JV55 made provision for finance for ventures and for operating costs in the following terms:

> PROVISION OF FINANCE
>
> 6. (1) All funds required from time to time for the joint venture (including excess costs as referred to in Clause 13 but not including operating costs to be paid under that Clause) shall, subject to the provisions of this Clause, be provided by the contributory companies, in proportion to their respective percentage interests, and such funds so provided are herein referred to as "capital contributions".
>
> OPERATING COSTS
>
> 13. (1) In this Clause the expression "operating costs" for any quarter means the cost incurred on behalf of the contributory companies by the Services Company in that quarter in the production of petroleum including a proper allocation of administrative and overhead expenses, rents, royalties and depreciation of tangible fixed assets, including movable plant and equipment, mechanical transport and drilling plant and tools. Such depreciation shall be at rates to be agreed upon by the contributory companies based on the expected useful life of such items and their residual value. Operating costs shall be computed in a consistent manner on the basis of generally accepted principles of accounting.

[16] On 1 March 2002, Todd and Shell concluded a Heads of Agreement (HoA) that was intended to record a restructuring of the arrangements between them, including the termination of JV55. In relation to STOS, the HoA provided:

> 5 **STOS**
>
> ***Documentation***
>
> 5.1 On or before 31 July 2002, the parties will enter into an agreement governing the relationship of Shell and Todd concerning, and the role and operations of, STOS. The agreement will contain and expand on the core terms set out in, or agreed under, schedule 3. Until such agreement is entered into, those core terms will govern that relationship, that role and those operations.

[17] Schedule 3 to the HoA was described as "STOS core terms". Those terms provided that Shell and Todd were to determine to carry on the business of providing services through one of two alternate ways. First, through an unincorporated joint venture between Shell and Todd, with STOS acting as nominee and/or bare trustee for Shell and Todd as joint venturers. Second, through STOS as a full operating company acting in its own right. The core terms also provided for a Shell

representative to have a second or casting vote in the case of an equality of votes cast at a meeting of the governance body, whether it be the board of directors of STOS or at an operating committee for a venture.

[18] Clause 2.1 of the HoA provided for the termination of JV55. However, the HoA separately addressed arrangements for Kapuni in the following terms:

> ***Kapuni***
>
> 2.3 Notwithstanding clause 2.1, the parties confirm that the provisions of JV55 listed in schedule 1 (or any other provisions as may be agreed by them) will continue to apply to the operation of the Kapuni field (which includes any further exploration, appraisal or other activities within the area of the Kapuni mining licence (PML 38839)) to the extent to which they relate to the operation of the Kapuni field, as if the parties were parties to and bound by JV55, until a new Kapuni joint venture agreement is entered into. Likewise, the parties confirm that the STOS employment agreement dated 5 December 1955 will remain in full force and effect insofar as it is currently applicable to the operation of the Kapuni field until superseded by a new employment agreement.

[19] No new Kapuni joint venture agreement has been concluded, nor is there any new STOS employment agreement.

The questions

[20] Todd seeks leave to argue nine questions of law. They are as follows:

> 1. If declarations and/or rulings as to relief in an arbitral award are set aside under Article 34 of the Arbitration Act 1996, what is the effect of that on findings of primary fact made in that arbitral award; and in any event what is the position in respect of findings of primary fact made in the interim award dated 10 October 2008? (Award [17])
>
> 2. Was the new STOS employment agreement to contain the Core Terms (Award [58])?
>
> 3. Does clause 5.1 of the Heads of Agreement ("**HOA**") mean that the Core Terms govern the relationship of the KMCs (Award [60])?
>
> 4. What are the constraints on the exercise of the vote of a member of the Shell Todd Oil Services Ltd ("**STOS**") Board at a meeting of such Board? (Award [93])
>
> 5. What is the relevance and scope of the obligation on STOS under clause 6(1) of its Employment Agreement ("**SEA**"), as operator of

the Kapuni oil and gas field, to carry out the work of prospecting, mining and development for which it is employed in accord with recognised good oilfield practice and with reasonable care as a prudent operator ("**RPO obligation**"):

(a) In respect of costs that are called for by STOS as operating costs under clause 13 of JV 55? (Award [95])

(b) In respect of costs that are proposed by STOS under clause 6 of JV 55? (Award [105] and [116])

(c) In respect of costs that are incurred by STOS on behalf of the KMCs and one or more other field joint ventures ("**multi-venture costs**")? (Award [183-190])

6. If STOS is instructed, by another venture to which it is contracted as operator, to purchase a system or other assets for use by that venture; and the system or asset could also be used by other ventures (and, if it is so used, the costs of the system or asset could be shared between the ventures pursuant to the Maui Cost Allocation Methodology ("**CAM**")):

(a) does STOS have the power to decide to use that system or asset on behalf of the Kapuni Joint Venture ("**KJV**"); and

(b) if so, what are STOS' obligations to the KMCs when making that decision?

7. Is STOS "for all practical purposes the operating committee" of the KJV (Award [107(d)]); and/or does STOS as operator also perform the function of a "management or operating committee"? (Award [113])

8. If STOS calls for costs under clause 13 that are ineligible to be called for under that clause, is STOS in breach of the SEA? And if STOS does so because Shell procures it to, is Shell in breach of JV 55? (Award [157])

9. Does Shell's right under the Core Terms to have its "standard accounting procedures" adopted by STOS extend to business management software systems used by STOS? (Award [181])

[21] Shell opposed leave being granted on all of the questions posed on behalf of Todd. For its own part, Shell sought leave for the following three questions:

(A) Was the Arbitrator correct to interpret the words "incurred … in the production of petroleum" in the definition of "operating costs" in clause 13(1) of the joint venture agreement between the parties dated 13 September 1955 (**JV55**), as continued in force by a heads of agreement dated 1 March 2002, as excluding costs, although incurred in good faith and rationally and with a view to facilitating future production of petroleum, where those costs are not certain to lead to further production of petroleum?

(B) Did the arbitrator have jurisdiction to, and was the arbitrator required to, deliver an additional award determining whether Shell has a casting vote at a meeting of the Kapuni Mining Companies (**KMCs**)?

[22] Because the arbitrator had subsequently addressed this issue in the CV ruling, question B was repeated in respect of that ruling, to cover the circumstances of both refusals to deal with it:

(C) Did the arbitrator have jurisdiction to, and was the arbitrator required to, deliver an additional award determining whether Shell has a casting vote at a meeting of the Kapuni Mining Companies (**KMCs**)?

[23] Todd opposed Shell's application in relation to all three questions.

The approach to granting leave

[24] As they have done in previous arguments before me, the parties were agreed that all of the questions were ones in respect of which the Court needed to be satisfied that there was a strongly arguable case. That standard derives from the Court of Appeal's analysis of the approach to granting leave in such applications in *Gold & Resource Developments (NZ) Ltd v Doug Hood Ltd*.[7] That unanimous decision of a Full Court of the Court of Appeal, delivered by Blanchard J, reviewed the relatively confined circumstances in which it would be appropriate to grant leave to appeal on questions of law in relation to arbitral proceedings under the Act. As summarised in the headnote to the report, leave to appeal would only be granted where the determination of the question of law concerned could substantially affect the rights of one or more of the parties to the arbitration agreement. That pre-condition to the granting of leave was not contested in relation to numerous of the questions on both applications, and I will address it separately on those where it was.

[25] On the analysis in *Doug Hood*, once that condition is met, the Court could exercise a discretion to grant leave, with the Court recognising eight factors as relevant in deciding whether or not to exercise the discretion. The first such factor

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7 *Gold & Resource Developments (NZ) Ltd v Doug Hood Ltd* [2000] 3 NZLR 318 (CA).

distinguishes, on one hand, questions arising which were one off points and of little precedent value. In such cases, the Court would not grant leave unless there were very strong indications of an error. On the other hand, where the question was of precedent value, then the somewhat lower standard of a strongly arguable case that an error existed would be sufficient. The questions on which leave is sought fall into the second category. I will first consider in respect of all of the questions on which leave is sought, whether they are strongly arguable. In relation to those that are strongly arguable, I will then revert to additional considerations from *Doug Hood* that may influence the discretion on granting leave.

Todd's application – questions strongly arguable?

[26] In advancing argument in support of leave for Todd's questions, Mr McIntosh addressed them in three groups. The first group, questions 2, 3 and 9, he described as raising misinterpretations of the HoA.

Question 2

[27] The interim award stated:[8]

> The new employment agreement was to contain the core terms set out in or agreed under Schedule 3 of HoA. Until the new agreement was entered into "*those core terms will govern that relationship, that role and those operations*". (italics included in the award)

[28] It is strongly arguable that the analysis in those sentences contains an error in interpreting the application of the HoA to current operations at Kapuni. The italicised words at the end of [58] of the interim award come from clause 5.1 of the HoA and it is strongly arguable that that provision does not apply to Kapuni because the contractual situation at Kapuni was separately addressed under clause 2.3 of HoA, the last sentence of which confirmed that the SEA was to remain in full force and effect insofar as it was currently applicable to the operation of the Kapuni field until superseded by a new employment agreement. Arguably therefore, [58] of the

[8] At [58].

interim award wrongly treats the core terms specified in Schedule 3 to the HoA as currently applying to Kapuni.

[29] However, that is not the precise point of concern to Todd, in posing question 2 in the terms it has. Rather, Todd's concern is that the core terms were intended to regulate the relationship inter se between Shell and Todd as the owners of STOS, and were not intended as a template for the terms that would apply between Shell and Todd on the one hand as the KMCs, and STOS as operator on their behalf, on the other hand. This concern also reflects the consistent observation by the arbitrator two paragraphs later in the interim award, as quoted in [31] below. Todd argues that the HoA contemplated that a draft technical services agreement that was contained in Schedule 2 to the HoA was what was intended as the source of terms to apply to a new employment agreement between Todd and Shell as the KMCs, and STOS as operator at Kapuni.

[30] Shell argued that no error is apparent because in the context of other paragraphs in the interim award, it was clear that the arbitrator treated the 1955 SEA (as annexed as a schedule to JV55) as still in force. I am not persuaded that that approach to [58] and those surrounding it deprives Todd of the point that there is a strongly arguable case for error in the terms of [58] itself.

Question 3

[31] The second of the first group of Todd's questions is number 3, which challenged the statement in [60] of the interim award, which was as follows:

> Clause 5.1 of the HoA states that the core terms will govern the relationship of the KMCs and the role and operation of STOS. However, the HoA also stated that the employment contract remained in full force and effect.

Todd seeks to argue that the core terms govern the relationship between Shell and Todd in respect of their participation in the unincorporated joint venture of STOS as it operates across all of the fields where it is employed, but that it does not govern the relationship between Todd and Shell in their capacity as the KMCs.

[32] Shell argued that the analysis of clause 5.1 of the HoA in [60] of the interim award does not give rise to any strongly arguable case of error. Shell suggests it is evident that the arbitrator simply used the acronym "KMCs" as a convenient shorthand reference for Shell and Todd in whatever capacity was relevant to the context in which it was used, and that it is an accurate observation that, in general terms, the core terms will govern the relationship between Shell and Todd (the KMCs) in relation to STOS, and on STOS's role and operation. Because [60] immediately acknowledged that the 1955 SEA remained in full force and effect, the arbitrator was correctly acknowledging the point that that original contract ought now to be interpreted in the context of the broader contractual structure and factual matrix, which included the HoA and the core terms.

[33] Clause 5.1 of the HoA[9] provided that before the end of July 2002 the parties were to enter into an agreement, which would govern the relationship of Shell and Todd concerning STOS, and also govern the role and operations of STOS. The terms of such an agreement were to expand on the core terms set out in Schedule 3 to the HoA and until that agreement was entered into, those core terms would govern the relationship between Shell and Todd, and STOS, and the role and operations of STOS.

[34] The heading to clause 5 of the HoA is "STOS" and the subheading before clause 5.1 is "Documentation". As a matter of contractual interpretation, it seems likely in that context that this part of the HoA recorded a commitment by Shell and Todd to negotiate a new agreement to govern their relationship concerning STOS, and to provide for the role and operations of STOS. It also seems likely that the last sentence of clause 5.1 was committing Shell and Todd to having their relationship vis-à-vis STOS governed by the core terms, pending completion of the new agreement. However, on the basis that specific provisions are treated as exceptions to the general, it is strongly arguable that the continued application of specified provisions from JV55 in relation to Kapuni, and the continuation in full force and effect of the 1955 SEA for Kapuni (provided for in clause 2.3 of the HoA), means that whilst the core terms applied in whatever different terms they specified to

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9 Quoted at [16] above.

regulate the relationship between Shell and Todd concerning STOS in general terms, in relation to Kapuni the specified existing provisions continued to apply.

[35] I accept that it is strongly arguable that [60] of the interim award attributes a different meaning to clause 5.1 of the HoA, namely that the core terms "will" govern the relationship of the KMCs – ie will regulate the relationship between Shell and Todd in their capacity as the Kapuni Mining Companies - and further that the core terms will govern the role and operation of STOS, implicitly at Kapuni. The arbitrator's analysis of clause 5.1 is open to two alternatives as to the temporal effect of clause 5.1. The expression "will govern" could mean that it will do so, prospectively, at some unspecified point in the future. Alternatively, because it is commenting on the effect that the HoA attributes to the core terms, it could mean that the core terms are to apply, for instance from execution of the HoA.

[36] In either temporal sense, it is strongly arguable that the core terms do not govern the relationship between Shell and Todd as the KMCs.

[37] Further, it is also strongly arguable that the core terms would not govern the role and operation of STOS in relation to its operatorship at Kapuni, which could reasonably be interpreted as the context in which the statement in [60] of the interim award is made.

[38] Accordingly, I accept on question 3 that there is a strongly arguable question that an interpretation that the core terms govern the relationship of the KMCs is wrong.

Question 9

[39] The last of the questions in the first group addressed for Todd was question 9. It was posed in terms of whether Shell's rights under the core terms to have its "standard accounting procedures" adopted by STOS extended to the business management software systems (SAP systems) acquired by STOS. This question sought to challenge the reasoning in [181] of the interim award, which provided:

> Shell has certain rights under the core terms to have its standard accounting procedures adopted and implemented. These rights would, in my view, extend to the systems used. If Shell deemed it advisable, because of STOS's multi-operator role, to change its systems then on the face of it it has the right to do so. This could involve adopting a system which is required for a venture and using it in another venture, albeit at a higher cost than the previous system for that other venture.

[40] The narrow point pursued by Todd is that the scope of rights recognised for Shell in the core terms did not extend to the SAP software that had been adopted by STOS to suit Maui, and because of that, was also being deployed by STOS in other ventures including Kapuni.

[41] Todd would seek to argue that business management software systems are distinguishable from "standard accounting procedures", and that in the absence of any evidence on the boundaries of the two concepts, the arbitrator's conclusion can only have been a matter of contractual interpretation. Todd cited dictionary definitions said to illustrate the extent of difference between the two concepts. It also argued that it was commercially unsound to interpret the provisions broadly enough to treat Todd as having signed on for any systems Shell wanted.

[42] For its part, Shell argued that any question defined as narrowly as Todd proposed was meaningless, and that the essence of Todd's complaint was the arbitrator's recognition two paragraphs earlier in his award, to the effect that as a multi-venture operator, STOS was entitled to choose its own systems. It followed from this point that if STOS changed its systems for a valid reason, then under a separate contractual arrangement, the Maui Cost Allocation Model (CAM), STOS was entitled to recover the cost of the system from the venturers in other ventures where STOS was the operator. That was a model to which Todd had agreed, and the consequence of doing so was that costs for Kapuni were likely to increase if it became appropriate to adopt another system for all the ventures where STOS was the operator.

[43] Shell also argued that the question involved mixed questions of fact and law, of a type that could not qualify for leave.

[44] There is a discrete issue of interpretation as contemplated by Todd's question 9. The arbitrator arguably may have erred if he has incorrectly treated the SAP software systems, which appear to be generically described as "business management systems" as falling within the scope of Shell's "standard accounting procedures" as that expression is used in the core terms.

[45] The relevant provision in the core terms annexed as schedule 3 to the HoA is as follows:

> **7 Accounting procedures**
>
> 7.1 The Venture will endeavour to ensure that Shell's standard accounting procedures are adopted and implemented for each venture or project to which it provides Services. In this regard, the parties acknowledge that those standard accounting procedures will be incorporated into the technical services agreement for each project or venture.

[46] There is no other provision in the core terms dealing with the source of procedures that are to be adopted by STOS in its role as operator of a field. Given the context of clause 7 in the STOS core terms, a purposive approach would suggest that the parties intended to give a relatively liberal interpretation to the scope of what was covered by "standard accounting procedures". Given that, at least when it is operator for a venture in which Shell and Todd are the parties, STOS is not intended to be a profit-making entity, but merely providing operatorship services at cost to the venturers, "accounting procedures" could reasonably be interpreted as extending to the procedures by which the operator accounted to the venturers for all the activities undertaken in the course of STOS's operatorship. Viewed in that sense, the concepts of "accounting procedures" and "business management software systems" are substantially closer than if STOS was a stand-alone business in its own right, operating to produce a profit and to pursue its own business interests.

[47] Because this contextual approach to interpretation is at least tenable, and because of STOS's entitlement to choose systems as discussed in [42] above, I am not persuaded that there is a strongly arguable case that the arbitrator erred in treating the two concepts as sufficiently similar to justify STOS's charging of SAP costs.

[48] I now turn to Todd's second grouping: questions 5 and 6.

Question 5

[49] Todd's analysis of STOS's contractual obligations attributed to it an obligation to act in accordance with recognised good oilfield practice and with reasonable care as a prudent operator (RPO obligation). The determinations by the arbitrator sought to be challenged by Todd in its question 5(a), (b) and (c) all reflect the arbitrator's rejection of any such contractual obligation.

[50] Todd would argue that the RPO obligation derives from clause 6(1) of the third schedule to JV55. That constituted an undertaking by STOS:

> …to carry out the work of prospecting, mining and development for which it is employed in accord with recognised good oilfield practice and with reasonable care as a prudent operator and in particular to comply with any legal requirements relating to the licences…

[51] Todd treats that undertaking by STOS as an important constraint on the manner in which STOS can conduct operations for the joint venture. In circumstances where STOS's "Shellcentric" operations are seen by Todd as conflicting with the best interests of the Kapuni venture, and given Shell's effective control of STOS, Todd treats the RPO obligation as its principal protection against being forced to meet costs that Todd considers would not be incurred by an RPO.

[52] The three parts of question 5 would seek to challenge the arbitrator's rejection of any RPO obligation as constraining what STOS can call for as operating costs, what STOS could propose as capital costs under clause 6 of JV55, and STOS's ability to incur multi-venture costs.

[53] The arbitrator rejected the status Todd wishes to attribute to the RPO obligation in the following terms:[10]

> The RPO requirement is not an express term of JV55. It is a term of the employment contract under which STOS undertook to carry out its services in accord with recognised good oilfield practise. In my view, this does not

[10] Interim award at [91].

> make the term a factor in defining operating costs. It is an express statement of a duty owed by STOS to the KMCs. They may have a claim against STOS if it does not operate in this manner but it is not an element in determining whether a cost is an operating cost.

[54] Todd would have to overcome a number of hurdles in establishing that the RPO obligation operates as an on-going constraint on the scope of costs STOS can propose under either or both of clauses 13 and 6 of JV55. So, too, as a constraint on the circumstances in which it can allocate to its operations at Kapuni a portion of multi-venture costs that are initially incurred on behalf of STOS as operator at other fields.

[55] Shell would argue that the expressions "recognised good oilfield practice" and "reasonable care as a prudent operator" are technical terms in this industry, which are used in standard form petroleum mining joint venture agreements, and which relate largely to technical matters. There is some support for that from the opening words of clause 6(1) of JV55 which relate STOS's undertaking to its carrying out of the work "…of prospecting, mining and development…".

[56] Further, Shell argues that if, as a matter of law, the RPO obligation does apply to constrain STOS, then the finding is pointless without revisiting factual matters as to what indeed constitutes compliance by STOS with the RPO obligation.

[57] Shell also opposes an RPO obligation of the type Todd contends for on the ground that it would enable one party to the venture to unreasonably disrupt the legitimate business of the operator by pursuing legal challenges to what should be left as purely operational matters. That would be inconsistent with well-understood limits of judicial review of commercial decision-making.[11]

[58] The absence of an RPO obligation from the terms of JV55 itself can hardly be decisive in resolving its status in the relationship between STOS as an operator at a particular field, and the venturers employing STOS. The third schedule to JV55 is arguably the appropriate place to define such an obligation, if indeed it exists. Within that deed, clause 6(1) defines the standards to which STOS had to perform so that whatever it does provide for can be enforced by Shell and Todd as the

[11] Shell cited *Latimer Holdings Ltd v SEA Holdings NZ Ltd* [2005] 2 NZLR 328 (CA) at [70]-]72].

employers. STOS undertook to carry out its work with reasonable care as a prudent operator, and it seems likely that some contrary provision would have to negate that obligation before it could reasonably be relegated as not meaning what it says.

[59] The arbitrator's reasoning was that STOS's status as a multi-venture operator altered what its employers could expect of it at any one field.[12] That does not address why Todd and Shell cannot require STOS to meet the standard of an RPO at each field.

[60] There may be some validity in Shell's criticism that Todd sought to rely on the RPO obligation to confine what STOS could do in wider circumstances than could be warranted. However, the core of this question is whether STOS's undertaking to carry out its work with reasonable care as a prudent operator has any contractual effect at all when STOS is working on the costs that it will propose for an ensuing period. In [91], the arbitrator acknowledged that it was an express statement of a duty owed by STOS to the KMCs, but the subsequent reasoning in the award strongly arguably relegated such a duty to one without any impact in this context. Accordingly, I accept that it is strongly arguable that the arbitrator's approach to interpretation in [91] is in error. Question 5 is appropriately worded to challenge that finding.

Question 6

[61] Todd's question 6 seeks to challenge the relevance attributed by the arbitrator to STOS's position as an operator for other ventures, and the entitlement of STOS to commit the Kapuni venture to costs on a basis that shares costs across ventures, when the initiative for incurring the cost has arisen in the course of STOS's operatorship at another field.

[62] Todd submitted that its question 6 contains a strongly arguable question that the arbitrator attributed unwarranted significance to the recognition of STOS as a multi-venture operator, and to a provision for allocation of part of the costs to other

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12 Interim award at [185].

ventures in the Maui CAM.[13] Todd argued that this reasoning incorrectly influenced the interpretation of the obligations STOS had to the KMCs in relation to Kapuni, which Todd argued should continue to be regulated by the SEA. Todd treats the arbitrator's interpretation as overriding any RPO obligation by recognising the status of STOS as a multi-venture operator, and relying on the Maui CAM to validate decisions by STOS in relation to assets originally acquired for other ventures (principally Maui), which on Todd's view are then foist on Kapuni without STOS having to separately consider whether such assets are appropriate for Kapuni.

[63] The arbitrator's reasoning included the following points:

> 179. There is substance in Shell's submission that STOS as a multi-operator was entitled to choose its own systems, and if it changed its systems for a valid reason it was entitled to recover the cost of the system from other joint venturers under the Maui CAM. Todd had agreed to this model and it follows that from time to time costs charged to one venture were likely to increase if it became appropriate to adopt another system for all the venturers serviced by STOS.
>
> …
>
> 181. …If Shell deemed it advisable, because of STOS's multi-operator role, to change its systems then on the face of it, it has the right to do so. This could involve adopting a system which is required for a venture and using it in another venture, albeit at a higher cost than the previous system for that other venture.
>
> …
>
> 185. If STOS had not been a multi-venture operator, the fit for purpose test may have had application. The contractual matrix associated with STOS, in which Todd was a party to many contracts, tells against the "*fit for purpose*" interpretation. If this were to be the case, it would be necessary in some situations for there to be several separate systems for separate ventures to undertake the same basic task. The overall cost to all ventures could be considerable if several different systems were to be used for the same basic function in several ventures.

[64] It is strongly arguable that recognition by the parties of STOS's position as a multi-field operator was subject to its on-going obligations to the parties interested in each of the fields where it was contracted as operator, to continue with the standards of performance that applied before that time. The prospect could well arise, at least

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[13] Defined at [42] above.

in relation to Kapuni, given the parties' agreement in the 2002 HoA to treat regulation of their relationship at Kapuni, and STOS's participation in it, discretely.

[65] This form of argument could assume greater relevance if Todd were to succeed on questions 2 and 3, which challenge the relative importance attributed by the arbitrator's interpretation to the 1955 and 2002 contractual documents, so far as they relate to operations at Kapuni.

[66] The issue has obvious precedential significance for the parties. In the present context, Shell argues that any question of law Todd can formulate could not substantially affect Todd's rights because of factual findings by the arbitrator that it would in any event have been inefficient to continue running the previous systems for Kapuni, once new systems had been introduced at Maui. Further, that the arbitrator was not satisfied that retention of the previous systems at Kapuni would have led to the KMCs paying a lesser amount than they are now being asked to pay, on an allocated basis, for the new system introduced initially for Maui.[14] I do not accept that these particular circumstances remove the prospect of the question substantially affecting a party's rights, in terms of clause 5(2) of the second schedule to the Act.

[67] I consider that it is strongly arguable that STOS's obligations to Todd and Shell in relation to its operatorship at Kapuni are not to be varied in the material way accepted by the arbitrator, by virtue of decisions STOS makes in the course of providing services as operator for other ventures, to an extent that STOS may disregard what would be in the interests of the KMCs.

[68] Todd, in its third grouping, addressed questions 4, 7 and 8 as challenging:

- in whose interests members of the STOS board, or other governance body of STOS, are entitled to vote;

- whether STOS is de facto an operating committee for the Kapuni joint venture; and

[14] Interim award at [178], [182].

- whether STOS can be liable for breach of its obligations under the SEA, including, where Shell has procured the breach, the prospect of attributing liability additionally to Shell.

Question 4

[69] This sought to raise as a strongly arguable question what the extent of constraints are on the exercise of votes by those contributing to decisions by STOS in respect of Kapuni.

[70] The question is intended to challenge the arbitrator's reasoning in [93] of the award, which found as follows:

> Further, I do not accept that a decision by STOS as to the incurring of an expense must not have the purpose or effect of preferring or allowing to be preferred the interests of either KMC over the other. There is a difference between voting for an outcome which may favour the voting party and harming the other KMC. Provided a KMC's representative on the STOS board of governance acts honestly, in good faith and genuinely, without arbitrariness, capriciousness, perversity or irrationality, that member can vote in the interests of that party. This matter is addressed below.

[71] Todd now wishes to argue that those participating in STOS governance decisions are to be treated as directors of STOS, and because of that are required by s 131 of the Companies Act 1993 to comply with a duty to STOS to act in its best interests. That requirement can only be abrogated with express authorisation of a company's constitution, and there is no such provision in the constitution of STOS.

[72] Mr McIntosh did not make clear in his argument whether the representatives of Shell and Todd who contribute to the governance decisions of STOS in relation to Kapuni are formally appointed as directors of STOS, or whether Todd's analysis simply imputes that position to them by virtue of the functions they discharge. Presumably, decisions for STOS in relation to its responsibilities as operator at various fields are likely to be made by different personnel, depending on which operatorship is being considered. It may be that the decision-makers for STOS in relation to its work at Kapuni do not constitute all of the same group as those who

make equivalent decisions in respect of its operatorship at Maui, or other Taranaki fields.

[73] Shell opposed this question on grounds including that the point was a new one, not previously argued at earlier stages of the dispute. On Shell's analysis, Todd's question 4 raises a different issue from that which was being addressed by the arbitrator in his [93]. That point was that STOS could not incur expenses in a way that preferred the interests of one KMC over the other. In that context, the very limited constraint on freedom to vote in the interests of the appointing party reflected the decision in *Socimer International Bank Ltd (in liquidation) v Standard Bank London Ltd* on joint venturers[15] (hence the arbitrator's reference to "…the STOS board of governance…") and does not distinctly address any different constraints if those participating in such decisions are to be treated as directors of STOS.

[74] The arbitrator's reasoning on the extent of constraints on those contributing to governance decisions for STOS follows his rejection of any obligation on STOS to discharge its operatorship responsibilities at Kapuni by complying with an RPO obligation owed just to that venture. However, the tenability of this question is not necessarily tied to those earlier ones challenging the status of an RPO obligation as referred to in clause 6(1) of the third schedule to JV55.

[75] Further, the capacity in which the arbitrator treated KMC representatives contributing to decisions of "the STOS board of governance" does appear to draw a distinction between their participation in relation to the conduct of an unincorporated joint venture, as distinct from participating as directors of a limited liability company. STOS is operating as a bare nominee and there is no suggestion in the reasoning in the award that the arbitrator considered and rejected the notion that in that governance forum all representatives have to treat themselves as directors of STOS, with consequences for their freedom to act independently in the interests of the appointing party. The types of decision Todd is concerned about relate far more to STOS's operatorship at Kapuni (ie the work it was doing for others) rather than in

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[15] *Socimer International Bank Ltd (in liquidation) v Standard Bank London Ltd* [2008] EWCA CIV116.

relation to its own governance as a company. That tells against the point having any substantial effect on the parties' position, as does the point that it is a new argument.

[76] Accordingly, I am satisfied that Todd's question 4 does not pose a strongly arguable question arising out of the award.

Question 7

[77] Question 7 raises an issue closely linked to question 4, namely the scope of STOS's status in relation to the operation at Kapuni. Todd seeks to draw a distinction between STOS, being limited to its role as operator, and Shell and Todd as separately comprising an operating committee for their underlying joint venture at Kapuni.

[78] The findings which Todd treat as being to the contrary are in [107] and [113] of the award. Those paragraphs relevantly provide as follows:

> 107. The combined effect of clauses 13 and 6 of JV55 is:
>
> …
>
> (d) For all practical purposes, these rights under the standing authority given to it make STOS the operating committee of the joint venture.
>
> 113. The Merralls' article[16] notes that the context of petroleum mining joint ventures usually conform to a standard contractual structure which is well developed and understood. That structure generally involves:
>
> (a) a management or operating committee, at which the participants in the venture are represented; and
>
> (b) an operator which is appointed to conduct the activities of the venture.
>
> It follows from the previous findings that STOS performs both these roles at Kapuni.

[16] J D Merralls "Mining and Petroleum Joint Ventures in Australia: Some Basic Legal Concepts" (1988) 62 ALJ 907.

[79] Shell points out that the Merralls article assumes that one of the venturers usually undertakes the role of operator, whereas here the different structure is that the venturers have created a bare nominee to fill that role on both their behalves.

[80] Todd's challenge on this question is to the arbitrator's failure to acknowledge the different legal entities involved and their respective roles. In other words, STOS is operator and the KMCs are the joint venturers who, on Todd's analysis of JV55, have reserved to them certain powers of decision-making, and ultimate control.

[81] Shell argues that there is no question of law contained in the passages of the interim award that Todd seeks to challenge in its question 7. The arbitrator's reference to an "operating committee" is not a legal term of art, but rather a shorthand description the arbitrator adopted to reflect the practical reality of how Kapuni operates. As a matter of fact, Shell makes the point that Shell and Todd, in respect of their Kapuni interests, have never met in a forum other than for the governance of STOS. On Shell's analysis, the reasoning objected to is no more than observations of the commercial reality as to how the venture has been operating.

[82] Shell argued that Todd's proposed argument follows on from its challenge to the arbitrator's interpretation that any RPO obligation does not impact on STOS's task when proposing operating and capital costs. If that interpretation were reversed, then a context may well arise in which the venturers may need to meet other than as the governance body for STOS in relation to its operatorship at Kapuni. That point cuts both ways in the sense that if there is a strongly arguable question about the current application of an RPO obligation, and Todd were to succeed on that, then as a consequence any division of responsibilities between STOS and the KMCs would take on a different complexion.

[83] From Todd's perspective, recognition of the RPO obligation point as strongly arguable should carry with it the consequential point that the arbitrator erred in the scope of powers he attributed to STOS in relation to decision-making for Kapuni. On the other hand, if Todd is successful in imputing an RPO obligation to STOS, then that outcome is likely to cause a re-evaluation of the division of

decision-making between STOS and the KMCs. That suggests that leave would not be separately required on this point, to the extent that it is a consequential issue.

[84] In the end, I am not persuaded that standing on its own, question 7 constitutes a strongly arguable question.

Question 8

[85] On this question, Todd seeks to argue that if STOS calls for costs to be paid by the venturers under clause 13 (ie as operating expenses) that are in fact ineligible to be called for under clause 13, then STOS is in breach of the SEA. Further, that if STOS acts in breach in that way because Shell has procured it to do so, then Shell is also in breach of JV55.

[86] Todd asserts that conclusions having the contrary effect to these two propositions can be distilled from [157] of the interim award. That specifies as follows:

> It was also Todd's position that, by exercising its casting vote to approve the 2007 WP&B, Shell was causing STOS to breach a term of the employment contract. It was suggested that both clause 3(12) of JV55 and clause 2.3 in Schedule 3 clause 9.1 of the HoA were breached. I do not accept that there was any specific breach of the employment contract in determining to proceed with the sub-surface activities.

[87] That paragraph appears in a section of the award under the heading "Good Faith". The section did not deal specifically with the questions that Todd now poses in question 8. Rather, it considered the scope of the constraint on a joint venturer's ability to act in its own interests, to the extent that obligations of good faith might so constrain a party. The adverse consequences that Todd perceives as arising from [157] have to be seen in the context in which that reasoning was expressed. Shortly after [157], in [159] the arbitrator points out that the context of the reasoning in this section drew on two findings made earlier in the interim award. First, the scope of STOS's appointment, on terms where Shell has a casting vote, and secondly that he had found, as a matter of law, that Shell was entitled to vote in its own interests as long as it acted honestly and genuinely and not arbitrarily, capriciously, perversely or irrationally.

[88] Then in [160], the arbitrator made a factual finding that the dispute over the sub-surface costs is merely one of timing, and that Todd had accepted that they will need to be incurred sooner or later. The arbitrator commented:

> Both parties have different reasons for their timing differences and it is not for an arbitration such as this to determine which party is correct.

[89] Within the context of that analysis, I do not accept that the reasoning in [157] constitutes a finding of law that is to the contrary of the propositions Todd now wishes to argue as question 8.

[90] Shell's opposition to this question also took the point that [157] of the interim award made no finding at all in respect of Shell's secondary liability for a breach of contract by STOS. In addition, Shell denied any materiality to this proposition in light of the further factual finding by the arbitrator (at [198] of the interim award) that Todd had suffered no loss from STOS calling for the sub-surface disputed costs under clause 13.

[91] Todd's rejoinder to this last point was that it is an important point governing the future relationship of the venturers with STOS. Todd's concern is that if the operator is not bound to the terms of JV55 and its third schedule in the way Todd contends, then Todd is deprived of any material control over the extent of costs it is required to contribute. This point would not necessarily be correct if Todd is successful in establishing that an RPO obligation does constrain STOS's conduct when it is proposing operating and capital costs.

[92] Todd would argue that a proposal by STOS to call for operating costs under clause 13 in respect of expenditure that did not qualify as such would be contrary to a "key term" of the SEA, namely:

> No expenditure shall be undertaken by [STOS] beyond the limits from time to time prescribed by the employer.

However, that provision seems most likely to constrain what STOS can actually spend – ie it cannot commit to expenditure which it does not have sign off from the KMCs to incur. That is an entirely different point from treating STOS as having a contractual obligation to propose as operating costs under clause 13 only costs that

inarguably qualify as such. Indeed, where a proposed cost lies on the margin of "operating costs", STOS might well be expected to propose the cost, to enable debate to be had between the KMCs as to which side of the line that cost falls. The fact that one party has a casting vote cannot detract from the appropriateness of that common sense interpretation of clause 13. For all these reasons, I am not satisfied that Todd's question 8 would be strongly arguable.

Question 1

[93] Todd's first question (but the last which it addressed in argument) related to the effect of the terms on which my 17 July 2009 judgment directed that questions were to be re-argued. Because as a matter of form I arguably did not set aside the whole award, but rather each of the conclusory findings at the end of the first award, Todd wishes to argue that relevant findings that had not specifically been set aside by my judgment have survived.

[94] Todd's concern is that potentially favourable factual findings made in the first award, and not specifically addressed in my first judgment, ought still to bind the arbitrator and the parties.

[95] In contrast, in his interim award, the arbitrator has reconsidered findings of that type. So, the arbitrator's revised approach to the factual matters, in light of re-argued questions of law, has produced findings that are not consistent with those made in Todd's favour in the first award.

[96] Regrettably for Todd, I have a clear view on what was intended by the form of orders made at the conclusion of my first judgment. I did not set aside the first award in its entirety because neither party sought that. Each of Todd and Shell had sought leave to re-argue questions of law on which the arbitrator had not found in their favour in the first award. Each side had sufficient success before me, in that questions of law to be re-argued were sufficiently broad, for any orders made by me to represent a requirement that the arbitrator, in effect, start again. I did not contemplate that the evidence would be re-heard, but was advised that both sides did call additional evidence.

[97] I do not understand either party to argue that the form in which I ordered relief on their application went beyond the Court's jurisdiction under Article 34. The substance, in the circumstances of this case, is that there was to be a re-argument of questions of law that would materially affect all aspects of the ultimate outcome. The substance was a "clearing of the slate".

[98] Accordingly, I am satisfied that question 1, as sought to be argued on behalf of Todd, is not strongly arguable.

Shell's application – questions strongly arguable?

[99] Shell's own originating application sought leave on the two questions set out at [21] above. From an apparent abundance of caution, Shell sought leave to argue the same question as raised in its (B), in (C), as arising out of both the interim award, and out of the subsequent determination by the arbitrator in his CV ruling.

[100] Adopting the same approach as I did in relation to each of Todd's questions, the first issue is whether these questions raise a strongly arguable case of error by the arbitrator.

Question A

[101] Costs proposed by STOS in the 2007 WP&B included some $1.37 million for "tight gas studies" and some $913,000 for "reservoir management and Kapuni base model maintenance and enhancement".

[102] STOS's proposals were on the basis that these constituted "operating costs" as that phrase was defined in clause 13(1) of JV55.[17]

[103] A majority of these disputed sub-surface costs were to be expended in appraising the prospects for optimum recovery of gas from the field, throughout its

[17] Quoted at [15] above.

future life. That was particularly the case with the "tight gas studies". On those, the arbitrator determined:[18]

> Whether a cost is an operating cost or a capital contribution is ultimately a matter of fact. On the evidence in this case, it is my view that it can not be said that the tight gas costs are incurred in the production of petroleum. While they may be operating expenses for the purposes of GAAP, and are incurred in the production stage, they do not come within the modified definition of operating costs in clause 13 of JV55 because they may never lead to the production of petroleum. They are, therefore, not operating costs under clause 13.

[104] Although Todd supported the expenditure on reservoir costs of some $913,000 and well maintenance of $95,000, it disputed its categorisation and for the same reasons given in relation to tight gas costs, the arbitrator concluded that these categories of costs were also not operating costs within the meaning of clause 13.[19]

[105] Shell now wishes to argue that this approach to the interpretation of the expression "incurred…in the production of petroleum…" in clause 13(1) of JV55 erred by requiring a direct connection between the expenditure proposed, and production of petroleum.

[106] Shell would argue that the concept of production reflects a phase in the life cycle of the whole field (ie distinguishing it from prospecting, exploration and development), so that expenditure would constitute an operating cost if it is incurred to facilitate production or better enable assessment of how, where and when to produce.

[107] Shell's approach would not require a direct link between the expenditure and particular production. It would argue that it is sufficient that the expenditure was intended to advance the prospects of greater production, or to facilitate production over the life of the field, and is incurred during the production phase of the life of the field.

[108] Shell invites an analogy between costs of appraisal during the production phase, and the inclusion of an allocation of administrative and overhead expenses.

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18 Interim award at [149].
19 Interim award at [152].

Arguably, because the latter are included when they do not contribute directly to production, then so too should appraisal costs which are expended to optimise production.

[109] Todd denies that an interpretation different from the arbitrator's could be strongly arguable. It categorises the arbitrator's approach as consistent with that adopted by the industry, and reflects the ordinary meaning of the words used.

[110] Todd argued that the arbitrator was right in excluding the cost of tight gas studies because they may never lead to the production of petroleum.[20] Todd urged that this approach reflects common sense in that expenditure that may lead to a decision not to produce petroleum cannot sensibly be included within expenditure incurred in the production of petroleum.

[111] On the comparison Shell suggests between overhead expenses and costs of appraisal, Todd would argue that items specified in a list of what is "included" may well appear because they do not naturally fall within the classification as described. In other words, the drafters of JV55 recognised that an allocation of overhead might not fall within the defined scope of operating costs and was therefore specified as such to clarify the point.

[112] A wider approach to the relevant interpretation is certainly tenable. On Shell's approach, the scope of operating costs may reflect more the phase of production at the field, rather than incurring the expenditure because it will lead to production of particular petroleum. A more liberal view would suggest that work done to optimise overall production, whether in a particular instance leading to production of particular petroleum now, later or not at all is all related to production from the field in an overall sense. Todd would respond that Shell's expansive interpretation of clause 13 would rob the provisions of meaningful distinction between operating costs, and those to be treated as capital costs under clause 6.

[113] Whilst Shell's approach to the scope of "incurred…in the production of petroleum" is tenable, I am far from satisfied that it is strongly arguable. The

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[20] Interim award at [149].

arguability of Shell's contention is dented by the arbitrator's interpretation adhering to the natural meaning of the words as used in clause 13.

Questions B and C

[114] These questions seek to challenge the arbitrator's decisions in the interim award and the subsequent CV ruling not to address the issue of whether Shell would have a casting vote at a meeting of the KMCs, in the same way as it does in decisions by STOS's governance board in relation to operations at Kapuni.

[115] The issue is dealt with more thoroughly by the arbitrator in his CV ruling and it is convenient to analyse the prospect of granting leave on Shell's questions B and C in the context of that ruling. Having declined to provide a ruling in the interim award, the arbitrator invited either party to seek a separate ruling. He received Shell's application, together with Todd's opposition to it, leading to the whole issue being thoroughly considered in the CV ruling.

[116] In the first award, the arbitrator had considered this issue in the context of whether Todd could make out damages if relevant decisions had been made in the wrong forum, namely by STOS instead of at a meeting of the KMCs. In that context, the arbitrator found that Todd could not make out any loss suffered because the same outcome would inevitably pertain, whether the issue was decided by STOS or by a meeting of the KMCs.

[117] In my 17 July 2009 judgment, I held that the circumstances in which that finding had been made were in breach of the rules of natural justice because Todd was not sufficiently on notice that a finding adverse to its interests of this type might ensue.[21]

[118] The relevance of whether Shell has a casting vote at a meeting of the KMCs was thoroughly aired by the time of my first judgment, as was a reasonable outline of possible arguments for and against the proposition. Thereafter, the parties repeatedly acknowledged the relevance of the issue. In his CV ruling, the arbitrator

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[21] At [47]-[60].

summarised the matters that Shell relied on in order to attribute to Todd a commitment to have the question argued in the following terms:

> 14. Shell says there was such an agreement because:
>
> (a) Todd's counsel in a memorandum dated 28 August 2009 noted that "the existence of such a vote will need to be substantively argued in the rehearing";
>
> (b) Todd in memoranda listing the issues to be determined at the rehearing listed the casting vote issue as a distinct issue for determination;
>
> (c) Todd's counsel in a memorandum of 5 May 2010 asserted that the casting vote issue was "squarely within the ambit of the rehearing, including as to what impact it could have on remedies available";
>
> (d) Todd did not challenge the position set out in memoranda from Shell which listed as a substantive issue "does a Shell representative have a casting vote at a meeting of the KMCs held under clause 2(12) of JV55";
>
> (e) both parties argued the case for a substantive KMC casting vote in closing submissions;
>
> (f) in a memorandum which I issued on 3 November 2009, I recorded that "Shell has acknowledged that it will be necessary to determine whether there is a casting vote of the KMCs level regardless of whether or not damages are payable".

[119] Todd's rejoinder to the arbitrator was to take the formal points that:

- the issue of a casting vote at a meeting of KMCs had not been pleaded;
- on the findings in the second award the issue was not relevant to a determination of any of the matters resolved;
- its previous relevance arose from the analysis of Shell's grounds for resisting an award of damages; and
- at no stage had Todd explicitly agreed to have the matter determined irrespective of other findings relating to remedies.

[120] Having reviewed the competing positions, the arbitrator observed:[22]

> Against this background, the question is whether the actions of Todd's counsel, summarised above, amounted to conveying on behalf of Todd an agreement that the casting vote issue needed to be determined irrespective of whether or not there was to be a finding of a breach by Shell of its obligations and thus the possibility of damages.

[121] The arbitrator's conclusion on the numerous exchanges in memoranda subsequent to my first judgment was that he did not read into Todd's memoranda that it was "expressly agreeing to have the matter determined irrespective of the damages position".[23] I accept that it is strongly arguable that the arbitrator erred in that finding. Were it necessary to do so, I would be prepared to find that there was a very strong indication of an error on the point, so as to meet the higher threshold proposed in *Doug Hood*. However, a number of issues need to be addressed before it can assume status as a question of law arising out of an award, in respect of which leave to appeal can be granted.

[122] First, Todd argued that the essence of Shell's complaint is a finding of fact by the arbitrator. Shell responded to this argument by suggesting that the arbitrator's reasoning process required a standard of proof of Shell that was wrong as a matter of law, such as by requiring an "express" agreement on behalf of Todd. Further, that the arbitrator failed to have regard to the complete absence of any evidence that was inconsistent with there having been a requisite agreement.

[123] Those criticisms go to the approach adopted by the arbitrator, but they cannot transform his analysis on a question of fact, into an error of law.

[124] Shell further argued that for the purposes of clause 5 of the second schedule to the Act, rights of appeal may arise in respect of errors of jurisdictional fact because they constitute errors of law. This argument depended on an analogy with the administrative law context where, in certain circumstances, what appears to be an error of fact by the exerciser of a statutory power as to the scope of his or her jurisdiction may be reviewable.

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22 CV ruling at [20].

23 CV ruling at [22] (error in original corrected).

[125] Care would be needed in the arbitral context, in defining the scope of what may constitute a "jurisdictional fact" for the purposes of treating it as an error of law. The arbitral process is undertaken as a result of contractual commitments, and if an arbitrator incorrectly interpreted the scope of his or her jurisdiction, that could give rise to a question of law.

[126] Here, the alleged error is in the arbitrator accepting that Todd relevantly qualified the terms of an agreement to submit an additional question to arbitration, where the parties had committed themselves to arbitrating issues arising on pleadings and the additional question fell outside those pleadings. I am not inclined to treat that as an error as to the scope of jurisdiction of the arbitrator, so this alternative is not a viable means of avoiding its classification as a question of fact.

[127] Todd took an additional point that the CV ruling, in which the arbitrator reconsidered his decision not to provide a determination on the casting vote issue, was not "in an award". It is unnecessary to deal with that. The analysis of whether the question Shell wishes to pursue can constitute one of law is essentially the same, in both contexts.

[128] Shell sought to support the merits of its position in seeking to argue this question on appeal by reference to the efficiency of doing so. The issue has been traversed already by the arbitrator. On Shell's view, it is bound to arise sooner or later in the parties' on-going relationship. Determination by the same arbitrator who has dealt with the disputes over definition of costs, and assets disputes in relation to Kapuni, all support the logic of granting leave.

[129] However, none of those points can transform the character of the issue on which the question is formulated. Accordingly, I am not satisfied that questions B and C raise a question of law on which it is strongly arguable that there was an error.

Summary on strongly arguable questions and other considerations

[130] Accordingly, on the first consideration from *Doug Hood*, I find that Todd's questions 2, 3, 5 and 6 are strongly arguable. I find that Todd's questions 1, 4, 7, 8

and 9 are not. I also find that none of Shell's questions contain a question of law that is strongly arguable. Although its question A is certainly arguable, it clearly falls on the other side of the "strongly arguable" line from Todd's questions 2, 3, 5 and 6.

[131] If I were to grant leave on those four of Todd's questions, then there would be a challenge to questions of law about the application of core terms appended to the 2002 HoA in two ways. First, as those core terms impacted on the terms of STOS's employment at Kapuni. Secondly, the relevance of those core terms to the relationship inter se between Shell and Todd as the KMCs. In addition, there would be a question of law as to the application of an RPO obligation imposed on STOS in carrying out its operatorship duties at Kapuni, and whether STOS's work at Kapuni can validly be influenced by the scope of, or manner in which it conducts, work as operator for other ventures.

[132] The questions which I have found not to be strongly arguable mean that the parties must accept:

- the outcome of the award in relation to its approach to remaking findings of primary fact;

- the extent of constraints on the exercise of votes by members of the STOS board;

- the practical extent of STOS's role at Kapuni as either an operating committee or a management committee;

- the legal consequences of STOS calling for costs under clause 13 that are not eligible to come within that clause; and

- the scope to be attributed to the concept of "standard accounting procedures" that STOS may apply, as used by Shell.

[133] From Shell's perspective, finding its proposed questions not to be strongly arguable means that it would have to accept the arbitrator's interpretation of what

constitute "operating costs", for the purpose of clause 13(1) of JV55, and also accept the arbitrator's decision not to determine in this arbitration whether Shell would also have a casting vote at a meeting of the KMCs.

[134] I do not treat that division of issues (between those potentially arguable on appeal and those which would not be) as creating any asymmetry in the arguments, such that reconsideration of the first *Doug Hood* factor is warranted.

[135] Of the remaining discretionary factors listed in *Doug Hood*, the second factor invites an assessment of relatively how central to the reason for the arbitration the issue in question was. If the question of law was the very reason for the arbitration, then this might tend against exercising the discretion, whereas if the question of law emerged incidentally during the process, leave might more readily be granted.

[136] Here, the inter-relationship of the original SEA and the core terms attached to the 2002 HoA are central to the arbitration. So, too, is the scope of any RPO obligation sought to be enforced by Todd on its interpretation of the SEA. The entitlement for STOS to be influenced in the mode of its work at Kapuni by its work at other ventures is also important, although somewhat less central to the issues that have been determined.

[137] Given the scope of this arbitration and relative complexity of the potential inter-relationship between different contracts influencing STOS's work, I am not inclined to treat the relative centrality of these questions as a factor disentitling Todd to pursue an appeal in respect of them.

[138] The third factor under *Doug Hood* is whether the arbitrator was legally qualified. Mr Paterson is not only legally qualified, but a well-respected commercial arbitrator and a retired High Court judge. That counts against granting leave, particularly as the award is the result of a re-argument of the issues, very thoroughly aired by competent counsel with substantial resources available to them.

[139] The fourth and fifth factors in *Doug Hood* are whether the dispute is of great significance to the parties and whether a substantial amount of money is involved.

The second of these factors is certainly readily claimed by both parties in relation to all aspects of their on-going disputes. Similarly, on the four questions I have found to be strongly arguable, Todd can credibly claim that the outcome is of great significance to the parties.

[140] These fourth and fifth factors from *Doug Hood* overlap to an extent with the statutory pre-condition that the question of law concerned has to be one that could substantially affect the rights of one or more of the parties.[24] On the present argument, Shell did argue in respect of some of the questions which I have held to be strongly arguable, that the issue addressed by them could not substantially affect the rights of parties.

[141] For instance, on Todd's question 2, Shell suggested that Todd was jumping at shadows in the sense that the finding in [58] of the interim award complained about (ie that the core terms from a schedule in the HoA would govern STOS's employment arrangements at Kapuni) did not dictate subsequent outcomes in the award which are adverse to Todd. Shell analysed subsequent findings relevant to the scope of STOS's powers as appropriately reflecting the provisions of the 1955 SEA.

[142] The outcome which Todd treats as adverse to its interests does depend on a view of the inter-relationship between the 1955 and 2002 contractual provisions that would likely be revisited if Todd succeeded on its question 2. It is therefore impossible to relegate the outcome as one that could not substantially affect the rights of the parties.

[143] As to question 6, I have already addressed Shell's argument that factual findings to the effect that the new systems introduced by STOS were economically justified, would render the question of law irrelevant in any event.[25] As a subset of these fourth and fifth factors therefore, I am satisfied that the outcomes sought by Todd on the questions of law could substantially affect the rights of one or more of the parties.

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[24] Arbitration Act 1996, Second Schedule, cl 5(2).

[25] See [66] above.

[144] More generally on the significance of protracting this dispute, I have now spent part or all of nine days hearing arguments which sought to challenge various aspects of this experienced arbitrator's determinations in relation to the conduct of the joint venture at Kapuni.[26] In attempting to cursorily do justice to the extensive arguments advanced, I have struggled to provide anything in the nature of a "short judgment" on any of the applications. The processes followed by the parties are in stark contrast to that which the Court of Appeal directed should occur in *Doug Hood*.[27]

[145] Perhaps unfortunately for the parties, I have also learned a substantial amount about the strains in their commercial relationship as two of the three joint venturers at the Pohokura field. At the conclusion of my judgment in that litigation, I expressed the naïve hope (subsequently shown to be futile in light of Todd's appeal from that judgment) that the parties might draw breath on their serial disputes, and seek to re-establish the common commercial ground that ought to exist.[28]

[146] In all of these disputes, the amounts of money are readily classified as "very substantial", but on some issues the consequences of the different outcomes may only produce differences at the margins in what are financially very significant businesses. I am accordingly cautious of simply treating the amounts of money at stake as adding materially to the weight of the factors in favour of granting leave.

[147] I consider that weight in favour of granting leave to be diminished by the stage that this particular contractual relationship has reached overall. It has now been thoroughly aired before the well-respected commercial arbitrator chosen by the parties. Mr Paterson has taken a view of the way through the relatively complex inter-relationship of contracts, the structure of which is such that however strongly it is arguable that their combined effect is different, there also remains a prospect that the arbitrator's overall analysis is not materially in error. These considerations suggest a downplaying of the weight to be given to the discretionary factors in

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[26] 29 April, 11, 12 and 14 May, 16 November and 15 December 2009, 25 May 2010, 18 and 24 May 2011.

[27] See [56]-[59].

[28] *Todd Pohokura Ltd v Shell Exploration NZ Ltd* HC Wellington CIV-2006-485-1600, 13 July 2010 at [526].

favour of leave. However, it would be mischaracterising the nature of the issues to have such considerations dictate the outcome.

[148] The remaining discretionary considerations from *Doug Hood* are the impact of delay, and whether the parties had agreed that the arbitral award would be final. Delay here is not of great significance, given the scale and timing of other disputes in the on-going relationship between Todd and Shell and the inevitability that their joint venture will be on-going for many years, virtually irrespective of the timing of a final outcome and which party's position is finally vindicated on each of the disputed issues. This was not a submission to arbitration agreed to be final and so that factor, for what it is worth, does not weigh against the exercise of the discretion.

[149] Standing back and reflecting on all of these considerations, I am satisfied that leave should be granted on the four questions on which I have recognised a strongly arguable issue.

[150] There will be no order as to costs.

Dobson J

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