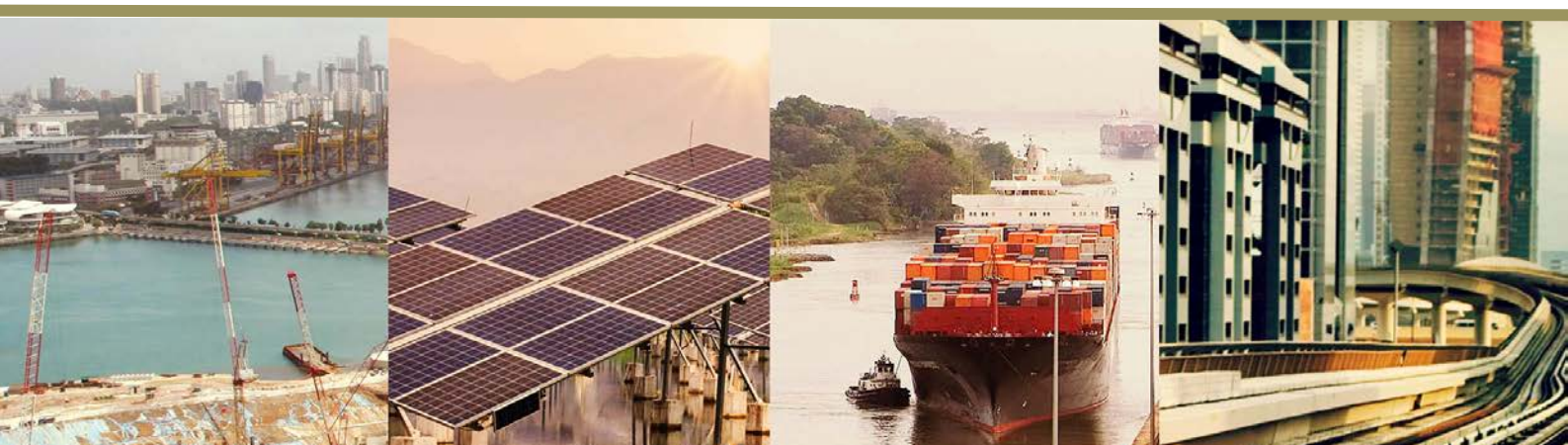


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Contractual Interpretation -  
The Retreat from Hoffman

Andrew Goddard QC  
David Johnson



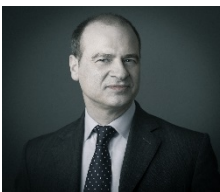
## Contractual Interpretation – The Retreat from Hoffman

Contractual interpretation is a key battleground in much commercial litigation. Recent decisions from the UK Supreme Court and the courts in Singapore and Hong Kong appear to show a shift in approach from Lord Hoffmann's well-known statement of principles in *Investors Compensation Scheme v. West Bromwich BS*. Andrew Goddard QC and David Johnson examine those recent decisions and consider whether they mark a fundamental change how courts are likely to approach such questions in the future, or whether they represent merely cosmetic updates to the philosophy put forward by Lord Hoffmann in *Investors Compensation Scheme* and subsequent judgments.

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Andrew Goddard QC specialises in international commercial arbitration, concentrating on complex construction, infrastructure and IT disputes. He believes that the intelligent use of IT to improve communication, collaboration and management in major projects has the potential to reduce the number and severity of disputes. He is passionate in his belief that when matters do become litigious, leveraging IT can increase the efficiency and reduce the costs of conducting and resolving complex disputes. He is an innovative problem solver committed to finding solutions which produce cheaper and better outcomes for his clients.

He has acted in numerous disputes referred to arbitration under the auspices of the ICC, the HKIAC, the LCIA and the LMAA and also has experience of Investor-State disputes proceeding before the International Centre for the Settlement of Investment Disputes (ICSID). He has been appointed as Arbitrator, Adjudicator and Legal Expert in various disputes in the UK and internationally. He is based in London but his work regularly takes him to the Far East, the Gulf and the Caribbean.

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David practises in the fields of construction, engineering, energy and information technology. David has been involved in numerous transport and infrastructure disputes, including several UK and international railway and urban railway projects and multiple disputes in relation to the CAPEX expansion programme at an international airport.

In addition to these specialist areas he also advises and appears in respect of a range of other general commercial matters. David has experience of both project and pre-action work as well as all other stages of the litigation, arbitration and adjudication processes. He is instructed either as junior counsel or as sole acting counsel and is a TECBAR accredited adjudicator. David has also worked on-site with numerous clients where extensive on-the-ground support has been required. David is experienced in dealing with all major standard form building contracts (JCT, FIDIC, NEC3, ICE) and has appeared in numerous interim and final hearings. David has recently acted as Junior Counsel in arbitration proceedings in the Middle East and as sole Counsel in an arbitration involving a Singaporean client.

## Introduction

1. Questions of contractual interpretation arise in almost every construction or infrastructure dispute, whether in the context of the principal conditions of contract, the technical specifications, or even the contract drawings. The question for the tribunal seized of the issue is, obviously, to determine what the particular document means.
2. English law has, over the centuries, developed various rules and principles to guide the interpretive exercise. The starting point (which is not shared by numerous other jurisdictions) is that the determination of meaning is an *objective* exercise; and that there is only one correct meaning to an instrument in law. English law has, therefore, in the context of the interpretive exercise, no interest in the subjective intentions of the parties, whether demonstrated through their pre-contractual negotiations or their post-contractual conduct.
3. Alongside these fundamental tenets, English law developed various canons of construction to be applied to assist courts and tribunals in working out what the documents before them meant. These were guidelines, largely demonstrative of common sense, and included 'rules' such as that words should normally be given their ordinary meaning, or that a word used more than once in a document should usually be given the same meaning in each place.

## Interpretation of express terms and the search for meaning

4. It is generally recognised that English law took something of a modernising step in its approach to contractual interpretation in Lord Hoffman's well-known speech in *ICS v. West Bromwich*<sup>1</sup>. In declaring the previous 'intellectual baggage' and specific rules of interpretation largely a dead letter, Lord Hoffman set out five principles of construction of express terms. They are as follows:
  - (1) The court must consider the meaning a document would convey to a reasonable person having all the background knowledge that would reasonably have been available to the parties at the time the document was made.
  - (2) This background knowledge includes all relevant factual information that was available to the parties, and which would have affected the way in which the language used in the document would have been understood by a reasonable person.
  - (3) Pre-contractual negotiations, however, are excluded from this background information.

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<sup>1</sup> *Investors Compensation Scheme v. West Bromwich Building Society* [1998] 1 WLR 896 (HL)

- (4) The meaning of a document may not be the same as the meaning of the words used. The court can and should attempt to ascertain what the words were intended to convey as opposed to their literal meaning.
  - (5) Whilst parties must be taken to have used the words they did for a reason, it may be possible to conclude that something has gone wrong with that language, and the court must attempt to give effect to what the parties meant to say.
5. *ICS* was decided in 1997 and involved a claim based on the assignment of claims arising out of negligent financial advice. The case turned on the meaning of a clause that purported to exclude the assignment of “*any claim (whether sounding in rescission for undue influence or otherwise)*” and the issue was whether or not this excluded claims for damages as well as for rescission. The House of Lords held that, despite the wording, the clause did not exclude claims for damages, and did so effectively by concluding that, when executing the contract of assignment, there was, objectively, no apparent intention to exclude damages claims. Lord Hoffmann explained that<sup>2</sup>:

*“The exercise of interpretation is therefore to identify what a reasonable individual would have understood the parties to have meant by the language used. Crucially, this is not the same as identifying what the parties themselves understood, or intended: subjective intent is irrelevant to the process of interpretation and evidence of such should not be relied upon as an aid to construction. The only relevant evidence is therefore that which was known or reasonably available to both parties at the time of contracting<sup>3</sup>.”*

6. *ICS* can be seen as ushering in a move away from a ‘literalist’ to a more ‘purposive’ approach to construction of express terms, taking note of background information reasonably available to the parties at the time of contracting. The scope of admissible background information includes anything which would have affected the way in which the language of the document would have been understood by the reasonable man, save for previous negotiations and declarations of subjective intent. *ICS* itself is largely uncontroversial, and has generally been accepted as such in common law jurisdictions, notwithstanding its significant downgrading of the old established canons of construction.
7. However, what made the approach of the House of Lords in *ICS* noteworthy was Lord Hoffmann’s express acknowledgment that the court should be open to the possibility that the drafted words may not reflect the objectively ascertained intention of the parties - and that the parties may therefore have

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<sup>2</sup> [1996] 1 W.L.R. 896 at 912-913

<sup>3</sup> As stated at [18] of *Sirius International Insurance Company v. FAI General Insurance Limited and Ors* [2004] 1 W.L.R. 3251 (HL), per Lord Steyn: “*The aim of the inquiry is not to probe the real intentions of the parties but to ascertain the contextual meaning of the relevant contractual language. The inquiry is objective: the question is what a reasonable person, circumstanced as the actual parties were, would have understood the parties to have meant by the use of specific language. The answer to that question is to be gathered from the text under consideration and its relevant contextual scene.*”

used the wrong words or syntax in their drafting. Whilst parties should be understood normally not to have made linguistic mistakes, it is nevertheless possible for something to have, as Lord Hoffmann noted, 'gone wrong with the language'.

8. It is worth pausing to consider the implications of this. It is one thing, where there is *ambiguity* in the language used, to reach a conclusion that, judged objectively, it is more probable that meaning X is the intended meaning, rather than meaning Y. But it is going a further distance to say that although *unambiguous* wording has been used, taking all other admissible information into account, the objectively intended meaning is the opposite of the words' objective meaning when interpreted without the benefit of the other background information.
9. It may be that this is an all but unavoidable consequence of the fact that language is open-textured; that it has a certain fluidity of meaning. But whilst one can readily accept that in everyday speech utterances are littered with ambiguities (often amplified or clarified by 'relevant background information') which provoke numerous requests for clarification from one's interlocutors, one tends to expect that legal instruments are, or at any rate should be, less open to interpretation. The approach of Lord Hoffman in *ICS* may suggest that this is an expectation with tenuous justification.
10. It is right to acknowledge that the acceptance that the wrong words may have been used is an approach that has its roots in earlier House of Lords decisions such as *Wickman Machine Tool Sales v. L Schuler AG*<sup>4</sup> where Lord Reid said<sup>5</sup>:

*"The fact that a particular construction leads to a very unreasonable result must be a relevant consideration. The more unreasonable the result, the more unlikely it is that the parties can have intended it, and if they do intend it the more necessary it is that they shall make that intention abundantly clear."*

11. In *The Antaios*<sup>6</sup> Lord Diplock arguably went further when saying:

*"If detailed and syntactical analysis of words in a commercial contract is going to lead to the conclusion that flouts business common sense it must yield to business common sense."*

12. This approach certainly provides the court with flexibility. However, the line, if there is one, between 'yielding to business common sense' and actively rewriting the parties' contractual bargain may at best be a fine one. For the interventionist court this may be unproblematic, but, as discussed below, such an attitude may no longer permeate the Supreme Court in England.

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<sup>4</sup> *Wickman Machine Tool Sales v L Schuler AG* [1974] AC 235 (HL)

<sup>5</sup> *ibid*, at 251

<sup>6</sup> *Antaios Compania Navera SA v. Salen Rederierna SA ('The Antaios')* [1985] AC 191

13. It is the view of the authors of this article that under the guidance of Lord Hoffman in the House of Lords and the Privy Council, *ICS* can best be seen as merely the first step in an attempt to introduce a new 'unified theory' of contract doctrine into English law, whereby the interpretation of express terms, questions as to the existence of implied terms of fact and issues as to remoteness of damage, are ultimately subsumed in an interpretive exercise posing the single question asked in *ICS v. West Bromwich*: what would the agreement, read against the admissible background information, reasonably be understood to mean?

## The implication of terms as an agreement-centred exercise

14. Turning from express terms to implied terms of fact, one needs to consider Lord Hoffman's approach as set out in the *Belize Telecom* case<sup>7</sup>. In *Belize*, the Government of Belize wanted to privatise telecommunications in Belize while still retaining a degree of control over the industry. To do this, a share scheme was established creating two classes of ordinary shares (B and C shares) and one special share. The special share was issued to the Government. There were to be eight directors: two appointed by the holder of the special share (i.e. the Government); two appointed by the B shareholders; and four appointed by the C shareholders. The company's articles of association provided that if the special shareholder owned 37.5% or more of the C shares, the owner of the special share could, in its discretion, appoint two of the four directors allocated to the C shareholders. After such appointments were made by the Government, it then sold some of the C shares so that it now owned less than 37.5% of them. There was nothing in the company's Articles of Association which provided for what was to happen to the already appointed directors in such a situation. Lord Hoffmann, giving the judgment of the Board, implied a term removing the specially appointed directors.
15. Although clearly in the territory of implied terms, Lord Hoffman did not approach the matter in the usual way of considering whether the various tests for the implication of a term premised on necessity had been overcome (namely that of business efficacy and the 'officious bystander'). Instead he downgraded the importance of these traditional tests, considering them to be merely different formulations of the ultimate question of: 'what the instrument, read against the relevant background, would be reasonably understood to mean.' As such, the approach promulgated in *ICS* to express terms was now applied to implied terms of fact.

## Recoverability of loss as an aspect of objective intention

16. The third in the trilogy of cases demonstrating the unified, agreement-centred approach to the law of contract is *The Achilles*<sup>8</sup>. The facts, slightly simplified,

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<sup>7</sup> *Attorney-General for Belize v. Belize Telecom* [2009] UKPC 10. This was a decision of the Law Lords sitting in the capacity of the Privy Council of the United Kingdom

<sup>8</sup> *Transfield Shipping Inc v. Mercator Shipping Inc* [2008] UKHL 48

can be stated as follows. Charterers were eight days late in redelivering a vessel. Such delay caused the owners (on pain of cancellation) to have to renegotiate a particularly profitable forward hire of the vessel for six months at a substantially reduced daily rate. The issue was whether the first charterers were liable for the difference between the originally negotiated hire and the reduced hire rate for just the eight days delay in redelivery, or for the six months of the renegotiated forward hire period.

17. Here, with the support of Lords Hope and Walker, Lord Hoffman introduced an objective agreement-centred approach to issues of remoteness of damage, concluding that a reasonable person in all the circumstances would have understood the charterparty to limit recovery for late redelivery to the difference between the market rate and the charter rate only for the overrun period of eight days.
18. For Lords Hoffmann, Hope and Walker, this was, among other things, because the losses incurred over the full length of a subsequent charter would be 'completely unquantifiable' and 'completely unpredictable' since 'the charterers had no knowledge of, or control over, the new fixture entered into by the owners.' Based on traditional authorities on remoteness of damage, this is a significant conclusion, since they contain no principle that denies recovery for losses on the basis that losses were unquantifiable or unpredictable. For their Lordships however, it appears that their conclusion as to recoverability/remoteness is the product of what the parties, judged objectively, would have intended.
19. The decision in the *Achilleas* can be contrasted with two of the traditional authorities on remoteness: *The Heron II*<sup>9</sup> and *Brown v. KMR Services*<sup>10</sup>. In *The Heron II*, the defendant shipowners were held liable for the profits that the claimant charterers would have made from the sugar market at Basrah had the defendant not deviated from its course and delayed the vessel's arrival. The rise and fall of the sugar market at Basrah was plainly unquantifiable and unpredictable, as were the profits that could be made. This was, however, no bar to recovery.
20. *Brown v. KMR Services Ltd* is perhaps an even more striking example. The case concerns the Lloyds Names – a famous London syndicate of investors who underwrote risks. In the 1980s and 1990s a long tail of asbestos-related claims, together with unexpectedly large 'punitive damages' awards in the US on various policies – some dating as far back to the 1940s – led to huge losses being faced by the syndicate – and by individual Names themselves. In *Brown*, however, the unpredictability or unquantifiability of losses arising from those unprecedented (and unforeseen) financial collapses was, for the Court of Appeal, no bar to a Lloyds Name recovering for his members' agents' breach of an implied obligation to warn of the high risks associated with loss syndicate investments.

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<sup>9</sup> *Koufos v C. Czarnikow Ltd (The Heron II)* [1969] 1 AC 350 (HL)

<sup>10</sup> *Brown v. KMR Services Ltd* [1995] 4 All ER 598 (CA)

## Consequences of the unified approach

21. The effect of bringing under the umbrella of the interpretive exercise the three issues of express terms, implied terms of fact, and remoteness of damage, and subjecting each to the same interpretive criterion, is potentially very significant. This is not least because the upshot may be that ultimately a contractual agreement would generally be held, as a matter of construction, to have the legal effect that a reasonable person in all the circumstances would have understood the parties to have agreed it would have.
22. This is a far cry from *The Moorcock*<sup>11</sup> approach to implied terms or the policy-driven dual test as to remoteness in *Hadley v. Baxendale*<sup>12</sup>.

## Resistance to the unified approach

23. As discussed below there has not been a universal acceptance of the unified approach. Certainly, the courts of Singapore have not shied away from criticising what has been characterised as a form of ‘one size fits all’ approach to issues (*viz.* implied terms of fact and remoteness) that are quite distinct from the interpretation of express terms.
24. Moreover, there is reason to query whether the Supreme Court of England and Wales is now also undergoing something of a ‘retreat’ from the principles espoused by Lord Hoffman, motivated in particular by the uncertainty and unpredictability that the unified agreement-centred approach gives rise to.
25. In this regard particular attention should be given to the Supreme Court decisions in *Arnold v Britton*<sup>13</sup>, *Marks & Spencer v BNP Paribas*<sup>14</sup> discussed below. There may be good reason to suppose that, amid some uncertainty, there is indeed a retreat from Hoffman and one which may gather momentum, such that the radicalism demonstrated in *Belize Telecom* and *The Achilleas* may soon be consigned to history.

## The Singaporean response

26. As discussed above, it could reasonably be said that by the end of the first decade of the 21<sup>st</sup> century, the doctrines of interpretation of express terms, the implication of terms in fact and remoteness of damage had, in England and Wales, all been subsumed within a unified ‘agreement-centred’ approach to contract law that focused on the parties’ intentions and could probably be described thus: **a contractual agreement will generally be held to have the legal effect that a reasonable person in all the circumstances would have understood the parties to have agreed it would have.**

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<sup>11</sup> *The Moorcock* (1889) LR 14 PD 64 (CA) 68

<sup>12</sup> *Hadley v. Baxendale* (1854) 9 Exch 850 (at 855)

<sup>13</sup> *Arnold v. Britton* [2015] UKSC 36

<sup>14</sup> *Marks and Spencer Plc v. BNP Paribas Securities Services Trust Company (Jersey) Ltd* [2015] UKSC 72



27. The same cannot, however, be said of Singapore, as a succession of decisions illustrates. The first of these is *MFM Restaurants v. Fish & Co*<sup>15</sup>. An employee changed job, causing losses to his former employer due to breach of a covenant not to compete. The only issue of remoteness was whether he was liable for its on-going effects after the breach had ceased. Why not? It was exactly the same kind of loss caused by the same kind of breach. It was only a question of its on-going effects. The Singapore Court of Appeal concluded that Lord Hoffmann's agreement-based rationale did not assist: it was uncertain, and it did not provide anything that *Hadley v. Baxendale* did not itself provide. At paragraph 98 the Court said:

*"It is interesting to note, at this juncture, that the broad underlying thread of interpretation which Lord Hoffmann utilises in advocating his approach centring on assumption of responsibility by the defendant has also been utilised by the learned law lord in the area of implied terms as well (in particular, to terms implied in fact) – hence, the analogy drawn by Lord Hoffmann between both these aforementioned areas. However, and with the greatest of respect, the uncertainty generated in the latter area would, in our view, apply equally to the former area. In the recent Privy Council decision (on appeal from the Court of Appeal of Belize) of Attorney General of Belize v Belize Telecom Limited [2009] 1 WLR 1988, for example, Lord Hoffmann, delivering the judgment of the Board, adopted an extremely broad approach towards the implication of terms in fact, effectively effacing the distinction between the time-honoured "business efficacy" and "officious bystander" tests."*

28. In *Foo Jong Peng v. Phua Kiah Mai*<sup>16</sup> [2012] SGCA 55, a number of individuals brought actions challenging resolutions that had removed them from their executive positions despite the fact that there was no term allowing their removal other than for misconduct or at the end of their two-year tenure. The appellants argued that there was an implied term allowing removal in other, wider circumstances. The Singapore High Court had declined to imply such a term and had declared the resolutions null and void.

29. The Court of Appeal agreed with this conclusion. At paragraph 36 it said, *"...although the process of the implication of terms does involve the concept of interpretation, it entails a specific form or conception of interpretation which is separate and distinct from the more general process of interpretation (in particular, interpretation of the express terms of a particular document). Indeed, the process of the implication of terms necessarily involves a situation where it is precisely because the express term(s) are missing that the court is compelled to ascertain the presumed intention of the parties via the "business efficacy" and the "officious bystander" tests (both of which are premised on the concept of necessity). In this context, terms will not be implied easily or lightly. Neither does the court imply terms based on its idea*

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<sup>15</sup> *MFM Restaurants Pte Ltd v. Fish & Co Restaurants Pte Ltd* [2011] 1 SLR 150

<sup>16</sup> *Foo Jong Peng v. Phua Kiah Mai* [2012] SGCA 55

*of what it thinks ought to be the contractual relationship between the contracting parties. The court is concerned only with the presumed intention of the contracting parties because it can ascertain the subjective intention of the contracting parties only through the objective evidence which is available before it in the case concerned. In our view, therefore, although the Belize test is helpful in reminding us of the importance of the general concept of interpretation (and its accompanying emphasis on the need for objective evidence), we would respectfully reject that test in so far as it suggests that the traditional “business efficacy” and “officious bystander” tests are not central to the implication of terms. On the contrary, both these tests (premised as they are on the concept of necessity) are an integral as well as indispensable part of the law relating to implied terms in Singapore (as noted above at [27]–[28]).*

30. In *Sembcorp v. PPL Holdings*<sup>17</sup>, the Singapore Court of Appeal considered that questions of admissibility of evidence had to be considered by reference to the existing law of evidence, which, in Singapore, is largely governed by the Evidence Act (Cap 97). The court noted the tendency of many parties to rely on the *ICS* line of authority and produce extensive evidence of little or no value in support of their contended-for construction. The court concluded that it was necessary for any background facts or matters, circumstances and other elements of the ‘matrix of fact’ to be specifically pleaded, with any evidence introduced to be limited to those pleaded matters.

31. In this respect the Court was alive to one of the other difficulties with Lord Hoffmann’s approach that has plagued the courts in England and Wales: the mass of evidence frequently adduced by parties to support their preferred construction. Very often that evidence is adduced in a somewhat unstructured and unfocused way and cases are tried on the basis of a chronological run through the documents in the hope that there is something the Court will seize upon as being persuasive. Not only is this unsatisfactory, it is also time-consuming and expensive.

32. It notable that the England and Wales Commercial Court Guide has adopted similar rules to those used in Singapore. Rule C1.2(g) states:

*“Where proceedings involve issues of construction of a document in relation to which a party wishes to contend that there is a relevant factual matrix that party should specifically set out in his pleading each feature of the matrix which is alleged to be of relevance. The “factual matrix” means the background knowledge which would reasonably have been available to the parties in the situation in which they found themselves at the time of the contract/document.”*

33. Equally notable is the fact that the Technology and Construction Court, by contrast, has not.

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<sup>17</sup> *Sembcorp Marine Limited v. PPE Holdings Pte Ltd* [2013] SGCA 43, 151 Con L.R. 170

34. Singapore has therefore, like England and Wales, adopted the contextual approach to interpretation as the bedrock of contract law. However, unlike England and Wales, attempts to subsume or combine separate doctrines under this agreement-centred focus have been met with considerable resistance and the courts have been particularly alive to the difficulties of doing so.

### The Supreme Court's retreat from Lord Hoffman's approach?

35. There is some evidence that the English courts are not as welcoming to Lord Hoffmann's approach as had previously been thought. *Arnold v. Britton*<sup>18</sup> was the first of the key decisions from the Supreme Court that indicated a potential retreat from the high point of the unified approach. That was, however, perhaps due as much as anything to the very particular facts of the case. The court was required to interpret a service charge provision in relation to a 99-year leasehold agreement from 1974. The agreement itself related to a holiday home in South Wales, which is a very beautiful part of the world – but not one affected by the problem of skyrocketing house prices that affects London. Pursuant to that agreement the lessee had promised:

*"To pay to the Lessor...as a proportionate part of the expenses and outgoings incurred by the Lessor in the repair maintenance renewal...and the provision of services...the yearly sum of Ninety Points...for the first Year of the term hereby granted increasing thereafter by Ten Pounds per hundred for every subsequent year or part thereof".*

(emphasis added)

36. The lessor argued that the underlined words stipulated that the annual service charge was a fixed £90 charge for the first year, increasing by 10% per year on a compound basis.
37. The lessee may or may not have had in mind the quote frequently attributed to Albert Einstein, namely, that, *"Compound interest is the eighth wonder of the world. He who understands it, earns it...He who doesn't...pays it"*. Based on the Bank of England's published inflation figures, it was calculated that by 2012 the annual service charge (on a chalet retailing for around £70,000) would be £3,366. By 2072, it was estimated that it would be some £1,025,004. Not surprisingly, and faced with South Wales looking like a rather expensive option after all, the lessee argued that this was not the intention of the lease, and that the words *"up to"* were required to be inserted prior to *"the yearly sum of Ninety Pounds"*. They argued that the clause had the effect of imposing a maximum on the annual service charge recoverable by the lessor, such that the lessor was entitled to an appropriate percentage of the annual cost of providing the contracted services, subject to a maximum of £90 that could rise by a maximum of 10% compound annually.

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<sup>18</sup> [2015] UKSC 36

38. The Supreme Court disagreed. Considering that there was, in fact, only one literal interpretation of the wording, it held that it was this that had to be given effect to. Lord Neuberger stated<sup>19</sup> that:

*“It is true that the first part of the clause refers to a lessee paying a ‘proportionate part’ of the cost of the services, and that, unless inflation increases significantly in the next 50 years it looks likely that the service charge payable under each of the 25 leases may exceed the cost of providing services to the whole of the Leisure Park. However, if, as I believe is clear, the purpose of the second part of the clause is to quantify the sum payable by way of service charge, then the fact that, in future, its quantum may substantially exceed the parties’ expectations at the time of the grant of the lease is not a reason for giving the clause a different meaning. As already explained, the mere fact that a court may be pretty confident that the subsequent effect or consequences of a particular interpretation was not intended by the parties does not justify rejecting that interpretation”.*

(emphasis added)

39. After referring to Lord Hoffman’s speech in *Chartbrook* for the general approach to the interpretation of a written contract, Lord Neuberger then went on to identify six general factors that were important in the *Arnold* case<sup>20</sup>, namely:

- (1) Reliance placed on commercial common sense and surrounding circumstances should not undermine the importance of the language and wording of the provision to be construed.
- (2) The less clear the centrally relevant words to be interpreted, the more ready the court can properly be to depart from their natural meaning.
- (3) Commercial common sense is not to be invoked retrospectively.
- (4) Whilst commercial common sense is an important factor to be considered, a court should be slow to reject the natural meaning of a provision simply because the consequences seem imprudent for a party. The purpose of interpretation is to identify what the parties have agreed, not what the court considers they should have agreed.
- (5) When interpreting a contractual provision, one can only take into account facts or circumstances that existed at the time the contract was made and were known or reasonably available to both parties.
- (6) In cases where an event subsequently incurred that was plainly not intended or contemplated by the parties on the basis of the wording, but it is clear what the parties would have intended, the court will give effect to that intention<sup>21</sup>.

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<sup>19</sup> *ibid.*, at [34]

<sup>20</sup> A seventh, more specific principle stated that there were no special or particular rules to be applied in relation to the interpretation of service charge clauses

<sup>21</sup> e.g. *Aberdeen City Council v. Stewart Milne Group Ltd* [2011] UKSC 56, where the court concluded that “any approach” other than that which was adopted “... would defeat the parties’ clear objectives”

40. The Court made clear that business common sense is therefore just one factor in the exercise of identifying how the words of the contract would be understood by a reasonable person with the background knowledge held by the parties. Moreover, the court cannot rely on what it perceives to be business common sense to find a different meaning where there is only one possible meaning.

## Analysis of *Arnold v. Britton*

41. *Arnold v. Britton* is arguably not of itself revolutionary in its approach: where a court or tribunal is faced with a dispute as to the meaning of particular wording in a provision or provisions of a contract, it must begin by considering the wording itself in its documentary, factual and commercial context, and, where that wording is, when placed in context, unambiguous, it must be applied<sup>22</sup>.

42. Other than the harsh result for the lessee<sup>23</sup>, there is one particular aspect of *Arnold v. Britton* that marks the case out as somewhat unusual. **There was, in fact, no background documentation against which the lease agreements could be construed by the court:** the lease documents themselves were the only evidence available. In such circumstances, it is perhaps unsurprising that the court considered it was unable to displace the wording of the agreement with business common sense: with no evidence, identifying such business common sense would have been nothing more than speculation on the part of the court. Even for Lord Hoffmann, that would have been quite a stretch. So the approach in *Arnold v. Britton* may be simply a consequence of the specific facts of the case.

43. By contrast, where such evidence is available, the court is in reality likely to take it into account, as Lord Neuberger's principles make clear. Indeed, the problem is arguably not one of legal principle but of language itself: given the open-textured nature of the words and phrases we use in everyday life, are there ever examples where the words used are truly unambiguous? To what extent are there situations where, although the literal meaning of certain wording is clear, surrounding circumstances or background information render the objectively intended meaning ambiguous? Moreover, can an otherwise unambiguous phrase be rendered ambiguous by certain background information that might be known to the parties, or indeed by the tribunal charged with ascertaining its meaning? We think instances of 'true' unambiguity are likely to be rare.

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<sup>22</sup> See *Rainy Sky SA and Ors v. Kookmin Bank* [2011] 1 WLR 2900 (SC) at [23]. Similar observations were made in *US Bank Trustees Ltd v. Titan Europe 2007-1 (NHP) Ltd* [2014] EWHC 1189 (Ch) (at [25]): "If...the court concludes that the language used is unambiguous, then the court must apply it, even though some other result might be thought more commercially reasonable, and even if it gives a result that is commercially disadvantageous to one of the parties. The court's function is to interpret the contract, not to rewrite it".

<sup>23</sup> Mitigated in reality by the fact that the lessor indicated, via her counsel in open court, that she was prepared to agree to the variation of the provision to tie the charge payable to consumer price index inflation

44. This may suggest that, no matter how tightly the courts attempt to draw the underlying legal principles, parties are likely to continue to fight extensive battles over problems of interpretation, and lawyers and judges alike are likely to expend considerable energy grappling with these issues.

## Further developments from the Supreme Court

45. Another recent decision from the Supreme Court also suggests a more restrictive approach may be adopted in future in relation to the implication of terms of fact. *Marks and Spencer Plc v. BNP Paribas Services Trust Company (Jersey) Ltd*<sup>24</sup>, turns on relatively simple facts. M&S was the tenant; BNP was its landlord. M&S had paid rent for the quarter year in advance before validly serving a break notice. M&S sought repayment of the rent relating to the post-break period, but did so in the absence of an express contractual term dealing with such a scenario. The Supreme Court found, echoing what might be regarded as the prevailing orthodoxy, that an express term would be needed in all but the most exceptional circumstances if such repayment were to be made. More significantly however, drawing on the previous criticisms made by the Singapore Court of Appeal in *Foo Jong Peng v. Phua Kiah Mai*<sup>25</sup>, it made clear that any approach to the implication of terms based on the presumed (yet objectively judged) intentions of the parties, following *Belize Telecom*, was too wide, and that *Belize Telecom* was not to be regarded as having changed the law in this respect.
46. The majority of the Supreme Court explained that construing express words and implying additional terms are different processes governed by different rules, and that Lord Hoffman's suggestion in the *Belize Telecom* case that the implication of terms forms part of the process of construction could obscure that fact. Whilst accepting that the factors taken into account when interpreting a contract are also taken into account on an issue of implication, that did not mean that the exercise of implication should be classified as part of the exercise of construction or that it should be carried out at the same time as interpretation.
47. In other words, parties should not and cannot assume that the court or tribunal will be as likely to step in and imply a term into a contract that is otherwise silent on a particular matter. The Supreme Court in *Arnold v. Britton* similarly made expressly clear it was not prepared to insert new words into a clause as part of the process of interpretation<sup>26</sup>. The precise consequences of this change in approach remain, of course, to be seen, and much will turn on the particular case or contract under consideration. The Supreme Court in *Marks and Spencer* were careful not to suggest that the result in *Belize Telecom* was incorrect, even if they did not approve the reasoning<sup>27</sup>.

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<sup>24</sup> [2015] UKSC 72

<sup>25</sup> [2012] SGCA 55

<sup>26</sup> [2015] UKSC 36 at [32] *per* Lord Neuberger

<sup>27</sup> [2015] UKSC 72 at [21] to [26] *per* Lord Neuberger; [58] to [73] *per* Lord Carnwath

48. Nevertheless, it needs to be recognised that the courts will be less likely to introduce implied terms where there is no express wording in the contract, so long as the contract can operate adequately without such. In such situations there is less prospect of the court determining questions of interpretation by reference to commercial expectation of a bargain under the guise of commercial common sense.
49. Moreover, it is arguable that the courts are trying to simplify the approach to be taken to questions of interpretation. This may be a laudable goal, but whether or not it will be achieved remains to be seen. A consequence of this more restrictive approach may be to reduce the amount of documents and evidence put before the court by parties in favour of their contended-for construction. In addition, the more literalist approach does suggest that the courts will be less likely to adopt special rules or principles when approaching certain types of provisions, such as penalty clauses or exclusion of loss clauses.
50. As to the development of a 'grand unified theory' based on interpretation and the ascertaining of the parties' (objective) intentions, this appears to have been stopped – for now. Some may lament this; but others applaud. As recognised by Andrew Phang Boon Leong JA, delivering the judgment of the Court of Appeal in *MFM v. Fish* (at paragraph 98), there are two sides to the debate:

*“Put simply, whilst it is desirable from a conceptual perspective to have umbrella doctrines that make for theoretical “neatness”, there is a limit to which one can have “one-size-fits-all” doctrines that will not ultimately become legal procrustean beds<sup>28</sup>. Indeed, the necessity for specific rules and principles has always been the hallmark of the development of the common law. Such specificity has, in fact, been (perhaps paradoxically) one of the key strengths of the common law itself, which is why Prof S F C Milsom perceptively observed that the common law system developed in a strikingly systematic fashion, notwithstanding the apparent absence of a clear blueprint as such.”*

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<sup>28</sup> Procrustes, whose name means “he who stretches”, was a host who adjusted his guests to their bed. He kept a house by the side of the road where he offered hospitality to passing strangers, who were invited in for a meal and a stay in the bed. Procrustes explained that its length exactly matched whoever lay upon it. What Procrustes did not volunteer was the method by which this “one-size-fits-all” was achieved: as soon as the guest lay down Procrustes went to work, either stretching him on the rack if he was too short for the bed and chopping off his legs if he was too long.