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p. 374

11. The Interpretation of Contracts

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Abstract

This chapter focuses on the principles applied by the courts when interpreting contracts. It examines the development of the modern law and focuses on three re-statements of the principles applied by the courts. The first is to be found in the judgment of Lord Hoffmann in *Investors Compensation Scheme Ltd* v. *West Bromwich Building Society*, the second is set out in the judgment of Lord Neuberger in *Arnold* v. *Britton*, and the third in the judgment of Lord Hodge in *Wood* v. *Capita Insurance Services Ltd*. The chapter discusses the scope of these principles (in particular, the 'factual matrix', the exclusion of pre-contractual negotiations, the meaning of words, 'corrective interpretation', and the balance to be struck between the natural and ordinary meaning of the words and giving to the words a commercial sensible construction).

Keywords: English contract law, contract interpretation, factual matrix, pre-contractual negotiations, natural and ordinary meaning of words, the role of commercial good sense, corrective interpretation

Central Issues

1. The principles applicable to the interpretation of contracts have been restated by the House of Lords and the Supreme Court in recent years. Three such restatements are the focus of this chapter. The first is to be found in the judgment of Lord Hoffmann in *Investors Compensation Scheme Ltd* v. *West Bromwich Building Society*, the second in the judgment of Lord Neuberger in

Arnold v. *Britton*, and the third in the judgment of Lord Hodge in *Wood* v. *Capita Insurance Services Ltd*. The significance of these principles should not be under-estimated. Many contract cases that come before the courts raise issues of interpretation.

2. In his speech in *Investors Compensation Scheme* Lord Hoffmann referred to the 'fundamental change' that has taken place in this area of contract law, the outcome of which has been generally to assimilate the way in which contractual documents are interpreted by judges to the common-sense principles by which any serious utterance would be interpreted in ordinary life.
3. Lord Hoffmann's restatement aroused a degree of controversy, principally because it was said to generate too much uncertainty and on the ground that it threatened to add to the cost and complexity of litigation. It was said to generate uncertainty because it appeared to widen the circumstances in which judges could depart from the 'natural and ordinary meaning' of the words used by the parties. But in *Arnold* v. *Britton* and *Wood* v. *Capita Insurance Services Ltd* the judicial pendulum appears to have swung back in favour of certainty and of giving to words their natural and ordinary meaning, at least in the case of a contract of some sophistication which has been drafted with the benefit of legal advice.

p. 375

11.1 Introduction

The principles applied by the courts when interpreting contracts are of enormous significance for contracting parties and their lawyers. This is so for a number of reasons. The first is that a significant number of the disputes that come before the courts raise issues of interpretation. The second is that many commercial parties make use of standard terms of business (or use industry-wide standard forms), and the precise meaning of these terms is a matter of considerable importance to them. The third is that many lawyers spend a considerable amount of time drafting contracts, and the drafting process must be carried out against the backdrop of the principles applied by the courts to the interpretation of contracts. So, for example, when drafting an exclusion or limitation clause the lawyer drafting the contract will be expected to be aware of the requirement that 'clear words' must be used if valuable rights are to be taken away (see *Triple Point Technology Inc* v. *PTT Public Co Ltd* [2021] UKSC 29, [2021] AC 1148, [107]–[111], see 13.2) and to draft the exclusion or limitation clause accordingly.

11.2 The Evolution of the Law

Traditionally, the English courts adopted a literal approach to the interpretation of contracts. In *Lovell and Christmas Ltd* v. *Wall* (1911) 104 LT 85 Cozens-Hardy MR stated (at p. 88):

> If there is one principle more clearly established than another in English law it is surely this: It is for the court to construe a written document. It is irrelevant and improper to ask what the parties, prior to the execution of the instrument, intended or understood. What is the meaning of the language that they have used therein? That is the problem, and the only problem. In saying that, I do not mean to assert that no evidence can be admitted. Indeed, the contrary is clear. If a deed relates to Black Acre, you may have evidence to show what are the parcels. If a document is in a foreign language, you may have an interpreter. If it contains technical terms, an expert may explain them. If, according to the custom of a trade or the usage of the market, a word has acquired a secondary meaning, evidence may be given to prove it. A well-known instance is where in a particular trade 1000 rabbits meant 1200. But unless the case can be brought within some or one of these exceptions, it is the duty of the court, which is presumed to understand the English language, to construe the document according to the ordinary grammatical meaning of the words used therein, and without reference to anything which has previously passed between the parties to it. When we come to the question of rectification,[1] wholly different considerations apply. The essence of rectification is to bring the document which was expressed and intended to be in pursuance of a prior agreement into harmony with that prior agreement.

p. 376 ↵ The meaning of a document was therefore to be found within its four corners. This approach was not without its merits. A court called upon to interpret a contract did not have to listen to evidence about the commercial purpose of the clause or the circumstances surrounding the conclusion of the contract. Its task was to rule on the meaning of the words used by the parties and it could do that on the basis of the documents alone. It was therefore possible for the parties to obtain a quick and relatively inexpensive ruling on the meaning of a disputed term in a contract. However, the drawbacks of this approach have been deemed to exceed its merits. In particular, it was argued that it was unrealistic to engage in a process of interpretation that was divorced from the context in which the parties found themselves. In other contexts, such as the interpretation of statutes, there has been a shift from ‘a literalist to a purposive approach’ to interpretation (see the dissenting speech of Lord Steyn in *Deutsche Genossenschaftsbank* v. *Burnhope* [1995] 1 WLR 1580, 1589) and this shift in emphasis has penetrated into the interpretation of contractual documents.

In retrospect the turning point can be seen to be the decision of the House of Lords in *Prenn* v. *Simmonds* [1971] 1 WLR 1381. The dispute between the parties related to the meaning of the word ‘profit’ in an agreement concluded under seal on 6 July 1960. Lord Wilberforce, giving the only reasoned judgment in the House of Lords, stated (at pp. 1383–1384):

> In order for the agreement of July 6, 1960, to be understood, it must be placed in its context. The time has long passed when agreements, even those under seal, were isolated from the matrix of facts in which they were set and interpreted purely on internal linguistic considerations. There is no need to appeal here to any modern, anti-literalist tendencies, for Lord Blackburn's well-known judgment in *River Wear Commissioners* v. *Adamson* (1877) 2 App Cas 743, 763 provides ample warrant for a liberal approach. We must, as he said, inquire beyond the language and see what the circumstances were with reference to which the words were used, and the object, appearing from those circumstances, which the person using them had in view. Moreover, at any rate since 1859 (*Macdonald* v. *Longbottom* 1 E & E 977) it has been clear enough that evidence of mutually known facts may be admitted to identify the meaning of a descriptive term.

The change in emphasis is clearly discernible. Contract documents are no longer to be interpreted 'purely' on internal linguistic considerations. Rather, they are to be placed in their 'context'. In other words, the court must have regard to the wider circumstances surrounding the conclusion of the contract. Lord Wilberforce returned to the issue in *Reardon Smith Line Ltd* v. *Yngvar Hansen-Tangen* [1976] 1 WLR 989, 995–997 when he said:

> No contracts are made in a vacuum: there is always a setting in which they have to be placed. The nature of what is legitimate to have regard to is usually described as 'the surrounding circumstances' but this phrase is imprecise: it can be illustrated but hardly defined. In a commercial contract it is certainly right that the court should know the commercial purpose of the contract and this in turn presupposes knowledge of the genesis of the transaction, the background, the context, the market in which the parties are operating. …
>
> It is often said that, in order to be admissible in aid of construction, these extrinsic facts must be within the knowledge of both parties to the contract, but this requirement should not be stated in too narrow a sense. When one speaks of the intention of the parties to the contract, one is speaking objectively—the parties cannot themselves give direct evidence of what their intention was—and
> p. 377 what must be ascertained is what is to be taken as the ↵ intention which reasonable people would have had if placed in the situation of the parties. Similarly when one is speaking of aim, or object, or commercial purpose, one is speaking objectively of what reasonable persons would have in mind in the situation of the parties … [w]hat the court must do must be to place itself in thought in the same factual matrix as that in which the parties were.

11.3 Restatements of the Applicable Principles

The shift from a narrow, literal approach to the interpretation of contracts, evident in the speeches of Lord Wilberforce in *Prenn* and *Reardon Smith*, led in time to the speech of Lord Hoffmann in *Investors Compensation Scheme Ltd* v. *West Bromwich Building Society* [1998] 1 WLR 896, in which he sought to restate the principles according to which contractual documents are to be interpreted. But Lord Hoffmann's restatement was not to be the last attempt at setting out the general principles to be applied by the courts when seeking to interpret a contract. In recent years the Supreme Court has had a regular flow of cases raising issues of contractual

interpretation, and in two of these cases, *Arnold* v. *Britton* [2015] UKSC 36, [2015] AC 1619 and *Wood* v. *Capita Insurance Services Ltd* [2017] UKSC 24, [2017] AC 1173, Lord Neuberger and Lord Hodge respectively sought to draw together the various threads and restate the principles which ought to guide the courts when seeking to interpret a contract. We shall examine the three judgments in turn before seeking to evaluate the approach which the courts currently take towards the interpretation of contracts.

Investors Compensation Scheme Ltd v. West Bromwich Building Society
[1998] 1 WLR 896, House of Lords

Lord Hoffmann

My Lords ... I should preface my explanation of my reasons with some general remarks about the principles by which contractual documents are nowadays construed. I do not think that the fundamental change which has overtaken this branch of the law, particularly as a result of the speeches of Lord Wilberforce in *Prenn* v. *Simmonds*, [1971] 1 WLR 1381 at 1384–1386 and *Reardon Smith Line Ltd* v. *Hansen-Tangen, Hansen-Tangen* v. *Sanko Steamship Co* [1976] 1 WLR 989, is always sufficiently appreciated. The result has been, subject to one important exception, to assimilate the way in which such documents are interpreted by judges to the common sense principles by which any serious utterance would be interpreted in ordinary life. Almost all the old intellectual baggage of 'legal' interpretation has been discarded. The principles may be summarised as follows:

(1) Interpretation is the ascertainment of the meaning which the document would convey to a reasonable person having all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract.

(2) The background was famously referred to by Lord Wilberforce as the 'matrix of fact', but this phrase is, if anything, an understated description of what the background may include. Subject to the requirement that it should have been reasonably available to the parties and to
p. 378 the exception to be mentioned next, it includes absolutely anything which would have affected the way in which the language of the document would have been understood by a reasonable man.

(3) The law excludes from the admissible background the previous negotiations of the parties and their declarations of subjective intent. They are admissible only in an action for rectification. The law makes this distinction for reasons of practical policy and, in this respect only, legal interpretation differs from the way we would interpret utterances in ordinary life. The boundaries of this exception are in some respects unclear. But this is not the occasion on which to explore them.

(4) The meaning which a document (or any other utterance) would convey to a reasonable man is not the same thing as the meaning of its words. The meaning of words is a matter of dictionaries and grammars; the meaning of the document is what the parties using those words against the relevant background would reasonably have been understood to mean. The background may not merely enable the reasonable man to choose between the possible meanings of words which are ambiguous but even (as occasionally happens in ordinary life) to conclude that the parties must, for whatever reason, have used the wrong words or syntax (see *Mannai Investment Co Ltd* v. *Eagle Star Life Assurance Co Ltd* [1997] 2 WLR 945).

(5) The 'rule' that words should be given their 'natural and ordinary meaning' reflects the commonsense proposition that we do not easily accept that people have made linguistic mistakes, particularly in formal documents. On the other hand, if one would nevertheless conclude from the background that something must have gone wrong with the language, the

law does not require judges to attribute to the parties an intention which they plainly could not have had. Lord Diplock made this point more vigorously when he said in *Antaios Cia Naviera SA* v. *Salen Rederierna AB, The Antaios* [1985] AC 191 at 201:

> '... if detailed semantic and syntactical analysis of words in a commercial contract is going to lead to a conclusion that flouts business common sense, it must be made to yield to business common sense.'

Arnold v. Britton
[2015] UKSC 36, [2015] AC 1619

Lord Neuberger

Interpretation of contractual provisions

14. Over the past 45 years, the House of Lords and Supreme Court have discussed the correct approach to be adopted to the interpretation, or construction, of contracts in a number of cases starting with *Prenn* v. *Simmonds* [1971] 1 WLR 1381 and culminating in *Rainy Sky SA* v. *Kookmin Bank* [2011] UKSC 50, [2011] 1 WLR 2900.

15. When interpreting a written contract, the court is concerned to identify the intention of the parties by reference to 'what a reasonable person having all the background knowledge which would have been available to the parties would have understood them to be using the language in the contract to mean', to quote Lord Hoffmann in *Chartbrook Ltd* v. *Persimmon Homes Ltd* [2009] UKHL 38, [2009] 1 AC 1101, para 14. And it does so by focussing on the meaning of the relevant words … in their documentary, factual and commercial context. That
p. 379 meaning has to be assessed in the light of (i) the natural and ordinary meaning of the clause, (ii) any other relevant provisions of the lease, (iii) the overall purpose of the clause and the lease, (iv) the facts and circumstances known or assumed by the parties at the time that the document was executed, and (v) commercial common sense, but (vi) disregarding subjective evidence of any party's intentions. In this connection, see *Prenn* at pp 1384–1386 and *Reardon Smith Line Ltd* v. *Yngvar Hansen-Tangen (trading as HE Hansen-Tangen)* [1976] 1 WLR 989, 995–997 per Lord Wilberforce, *Bank of Credit and Commerce International SA (in liquidation)* v. *Ali* [2002] 1 AC 251, para 8, per Lord Bingham, and the survey of more recent authorities in *Rainy Sky*, per Lord Clarke at paras 21–30.

16. For present purposes, I think it is important to emphasise seven factors.

17. First, the reliance placed in some cases on commercial common sense and surrounding circumstances … should not be invoked to undervalue the importance of the language of the provision which is to be construed. The exercise of interpreting a provision involves identifying what the parties meant through the eyes of a reasonable reader, and, save perhaps in a very unusual case, that meaning is most obviously to be gleaned from the language of the provision. Unlike commercial common sense and the surrounding circumstances, the parties have control over the language they use in a contract. And, again save perhaps in a very unusual case, the parties must have been specifically focussing on the issue covered by the provision when agreeing the wording of that provision.

18. Secondly, when it comes to considering the centrally relevant words to be interpreted, I accept that the less clear they are, or, to put it another way, the worse their drafting, the more ready the court can properly be to depart from their natural meaning. That is simply the obverse of the sensible proposition that the clearer the natural meaning the more difficult it is to justify departing from it. However, that does not justify the court embarking on an

exercise of searching for, let alone constructing, drafting infelicities in order to facilitate a departure from the natural meaning. If there is a specific error in the drafting, it may often have no relevance to the issue of interpretation which the court has to resolve.

19. The third point I should mention is that commercial common sense is not to be invoked retrospectively. The mere fact that a contractual arrangement, if interpreted according to its natural language, has worked out badly, or even disastrously, for one of the parties is not a reason for departing from the natural language. Commercial common sense is only relevant to the extent of how matters would or could have been perceived by the parties, or by reasonable people in the position of the parties, as at the date that the contract was made. Judicial observations such as those of … Lord Diplock in *Antaios Cia Naviera SA* v. *Salen Rederierna AB (The Antaios)* [1985] AC 191, 201 … have to be read and applied bearing that important point in mind.

20. Fourthly, while commercial common sense is a very important factor to take into account when interpreting a contract, a court should be very slow to reject the natural meaning of a provision as correct simply because it appears to be a very imprudent term for one of the parties to have agreed, even ignoring the benefit of wisdom of hindsight. The purpose of interpretation is to identify what the parties have agreed, not what the court thinks that they should have agreed. Experience shows that it is by no means unknown for people to enter into arrangements which are ill-advised, even ignoring the benefit of wisdom of hindsight, and it is not the function of a court when interpreting an agreement to relieve a party from the consequences of his imprudence or poor advice. Accordingly, when interpreting a contract a judge should avoid re-writing it in an attempt to assist an unwise party or to penalise an astute party.

21. The fifth point concerns the facts known to the parties. When interpreting a contractual
p. 380 provision, one can only take into account facts or circumstances which existed at the time that the contract was made, and which were known or reasonably available to both parties. Given that a contract is a bilateral, or synallagmatic, arrangement involving both parties, it cannot be right, when interpreting a contractual provision, to take into account a fact or circumstance known only to one of the parties.

22. Sixthly, in some cases, an event subsequently occurs which was plainly not intended or contemplated by the parties, judging from the language of their contract. In such a case, if it is clear what the parties would have intended, the court will give effect to that intention. An example of such a case is *Aberdeen City Council* v. *Stewart Milne Group Ltd* [2011] UKSC 56, 2012 SCLR 114, where the court concluded that 'any … approach' other than that which was adopted 'would defeat the parties' clear objectives', but the conclusion was based on what the parties 'had in mind when they entered into' the contract (see paras 17 and 22).

23. Seventhly [and a point which was of particular relevance to the facts of the case before the Supreme Court], reference was made in argument to service charge clauses being construed 'restrictively'. I am unconvinced by the notion that service charge clauses are to be subject to any special rule of interpretation. Even if (which it is unnecessary to decide) a landlord may have simpler remedies than a tenant to enforce service charge provisions, that is not relevant

> to the issue of how one interprets the contractual machinery for assessing the tenant's contribution. The origin of the adverb was in a judgment of Rix LJ in *McHale* v. *Earl Cadogan* [2010] EWCA Civ 14, [2010] 1 EGLR 51, para 17. What he was saying, quite correctly, was that the court should not 'bring within the general words of a service charge clause anything which does not clearly belong there'. However, that does not help resolve the sort of issue of interpretation raised in this case.

Wood v. Capita Insurance Services Ltd
[2017] UKSC 24, [2017] AC 1173

Lord Hodge

10. The court's task is to ascertain the objective meaning of the language which the parties have chosen to express their agreement. It has long been accepted that this is not a literalist exercise focused solely on a parsing of the wording of the particular clause but that the court must consider the contract as a whole and, depending on the nature, formality and quality of drafting of the contract, give more or less weight to elements of the wider context in reaching its view as to that objective meaning. In *Prenn* v. *Simmonds* [1971] 1 WLR 1381 (1383H–1385D) and in *Reardon Smith Line Ltd* v. *Yngvar Hansen-Tangen* [1976] 1 WLR 989 (997), Lord Wilberforce affirmed the potential relevance to the task of interpreting the parties' contract of the factual background known to the parties at or before the date of the contract, excluding evidence of the prior negotiations. When in his celebrated judgment in *Investors Compensation Scheme Ltd* v. *West Bromwich Building Society* [1998] 1 WLR 896 Lord Hoffmann (pp 912–913) reformulated the principles of contractual interpretation, some saw his second principle, which allowed consideration of the whole relevant factual background available to the parties at the time of the contract, as signalling a break with the past. But Lord Bingham
p. 381 in an extra-judicial writing, *A new thing under the sun? The interpretation of contracts and the ICS decision* Edin LR Vol 12, 374–390, persuasively demonstrated that the idea of the court putting itself in the shoes of the contracting parties had a long pedigree.

11. Lord Clarke elegantly summarised the approach to construction in *Rainy Sky* at para 21f. In *Arnold* all of the judgments confirmed the approach in *Rainy Sky* (Lord Neuberger paras 13–14; Lord Hodge para 76; and Lord Carnwath para 108). Interpretation is, as Lord Clarke stated in *Rainy Sky* (para 21), a unitary exercise; where there are rival meanings, the court can give weight to the implications of rival constructions by reaching a view as to which construction is more consistent with business common sense. But, in striking a balance between the indications given by the language and the implications of the competing constructions the court must consider the quality of drafting of the clause (*Rainy Sky* para 26, citing Mance LJ in *Gan Insurance Co Ltd* v. *Tai Ping Insurance Co Ltd (No 2)* [2001] 2 All ER (Comm) 299 paras 13 and 16); and it must also be alive to the possibility that one side may have agreed to something which with hindsight did not serve his interest: *Arnold* (paras 20 and 77). Similarly, the court must not lose sight of the possibility that a provision may be a negotiated compromise or that the negotiators were not able to agree more precise terms.

12. This unitary exercise involves an iterative process by which each suggested interpretation is checked against the provisions of the contract and its commercial consequences are investigated: *Arnold* para 77 citing *In re Sigma Finance Corpn* [2010] 1 All ER 571, para 10 per Lord Mance. To my mind once one has read the language in dispute and the relevant parts of the contract that provide its context, it does not matter whether the more detailed analysis

commences with the factual background and the implications of rival constructions or a close examination of the relevant language in the contract, so long as the court balances the indications given by each.

13. Textualism and contextualism are not conflicting paradigms in a battle for exclusive occupation of the field of contractual interpretation. Rather, the lawyer and the judge, when interpreting any contract, can use them as tools to ascertain the objective meaning of the language which the parties have chosen to express their agreement. The extent to which each tool will assist the court in its task will vary according to the circumstances of the particular agreement or agreements. Some agreements may be successfully interpreted principally by textual analysis, for example because of their sophistication and complexity and because they have been negotiated and prepared with the assistance of skilled professionals. The correct interpretation of other contracts may be achieved by a greater emphasis on the factual matrix, for example because of their informality, brevity or the absence of skilled professional assistance. But negotiators of complex formal contracts may often not achieve a logical and coherent text because of, for example, the conflicting aims of the parties, failures of communication, differing drafting practices, or deadlines which require the parties to compromise in order to reach agreement. There may often therefore be provisions in a detailed professionally drawn contract which lack clarity and the lawyer or judge in interpreting such provisions may be particularly helped by considering the factual matrix and the purpose of similar provisions in contracts of the same type. The iterative process, of which Lord Mance spoke in *Sigma Finance Corpn* (above), assists the lawyer or judge to ascertain the objective meaning of disputed provisions.
14. On the approach to contractual interpretation, *Rainy Sky* and *Arnold* were saying the same thing.
15. The recent history of the common law of contractual interpretation is one of continuity rather than change. One of the attractions of English law as a legal system of choice in commercial matters is its stability and continuity, particularly in contractual interpretation.

p. 382

11.4 The Scope of the Applicable Principles

These statements, or restatements, merit careful evaluation. They give rise to a number of issues to which we must now turn our attention.

11.4.1 The Importance of Principles

The judgments set out earlier attempt to distil the principles which the courts apply to the interpretation of contracts. They are not rules to be rigidly applied. Rather, they are principles to guide the court and they do so at a rather high level of generality. It is not uncommon for parties to litigation to be in agreement on the principles to be applied by the courts to the interpretation of the contract in dispute but to disagree on the application of these principles to the facts of the individual case (see, for example, *Quantum Advisory Ltd* v.

Quantum Actuarial LLP [2023] EWCA Civ 12, [9] and *Britvic plc* v. *Britvic Pensions Ltd* [2021] EWCA Civ 867, [16]). At this point it is important to note that the precedent value of a case concerned with the interpretation of a contract is generally low. Thus in *Surrey Heath Borough Council* v. *Lovell Construction Ltd* (1990) 48 Build LR 113 Dillon LJ stated (at p. 118) that 'a decision on a different clause in a different context is seldom of much help on a question of construction'. Further, in *Midland Bank plc* v. *Cox McQueen* [1999] 1 FLR 1002 Mummery LJ stated (at p. 1012):

> Detailed comparisons of one document with another and of one precedent with another do not usually help the court to reach a decision on construction. Indeed, that exercise occupies a disproportionate amount of valuable time which would be better spent on the arguments that really count: those which focus on the precise terms of the relevant documents and the illuminating environment of the transaction.

The authorities are, however, of greater importance in the situation where parties have chosen to use words that have acquired an established technical meaning. In such a case the courts are likely to give the words the meaning that they have been given in the case-law (*British Sugar plc* v. *NEI Power Projects Ltd* (1997) 87 BLR 42, 50).

11.4.2 The Objective Nature of the Test

Lord Hoffmann's statement that interpretation 'is the ascertainment of the meaning which the document would convey to a reasonable person having all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract' is, or appears to be, relatively uncontroversial and it is also adopted by Lord Neuberger (at [15]) and Lord Hodge (at [10]). It emphasizes the objective nature of the test applied by the courts. The 'methodology' of the common law is 'not to probe the real intentions of the parties but to ascertain the contextual meaning of the relevant contractual language. Intention is determined by reference to expressed rather than actual intention' (per Lord Steyn in *Deutsche Genossenschaftsbank* v. *Burnhope* [1995] 1 WLR 1580, 1587). Statements of subjective intent are therefore inadmissible so that where witnesses express views as to what they thought the provisions meant or were intended to mean, such evidence, being subjective in nature, is inadmissible (*BP Gas Marketing Ltd* v. *La Société Sonatrach* [2016] EWHC 2461 (Comm), [37]).

p. 383

11.4.3 The Importance of Textual Analysis

When seeking to ascertain the meaning of a disputed term in a written contract, particularly a written contract which has been drawn up with the benefit of professional legal advice, the task of the court is principally to engage in textual analysis (see *Wood* v. *Capita Insurance Services Ltd,* above, [15]). The words 'principally' and 'textual analysis' are important in this context. 'Principally' is important because it tells us that this is the most important task of the court, although it is not its only or its exclusive task. 'Textual analysis' is important because it reminds us that the focus should be upon the words to be found in the

written text. However, textual analysis should not be equated inevitably with a literal approach to interpretation (*Cantor Fitzgerald & Co* v. *YES Bank Ltd* [2023] EWHC 745 (Comm), [83]). It is possible to have a clear focus on the text but to interpret the text in a contextual or a purposive manner.

The focus on textual analysis is most apparent in the case of written contracts drawn up with the benefit of professional legal advice. Where the contract has been concluded rather more informally, the factual matrix (see 11.4.4) may play a greater role when seeking to resolve any dispute relating to the meaning of the contract. In such a case the parties may rely more on informal understandings than a carefully delineated text and that difference is reflected in the approach which a court is likely to adopt to the interpretation of such an informally created contract. The difference here is primarily one of emphasis. It is not the case that informal contracts are governed by a different set of principles from contracts drawn up with the benefit of professional legal advice. The framework which has been devised by the courts has to be sufficiently flexible to be able to accommodate many different types of contract within its scope. Thus, while the courts can be expected to go beyond textual analysis when seeking to interpret a contract which has been concluded informally, it is important to recall that 'informality is not a trump card that can overturn a text that carries an obvious and clear meaning' (*Contra Holdings Ltd* v. *Bamford* [2023] EWCA Civ 374,[25]).

11.4.4 The 'Factual Matrix'

The use of the language of 'matrix of fact' can be traced back to the speech of Lord Wilberforce in *Prenn* v. *Simmonds* [1971] 1 WLR 1381. However, its use has been attacked, in particular by Sir Christopher Staughton, a former judge in the Court of Appeal (see 'How Do the Courts Interpret Commercial Contracts?' [1999] *CLJ* 303, 306–308). He criticized the use of language such as 'the matrix of fact' on the ground that 'counsel have wildly different ideas as to what a matrix is and what it includes'. Particularly difficult was the use by Lord Hoffmann in his second principle in *Investors Compensation Scheme* of the words 'absolutely anything' which appeared to encourage lawyers to trawl through all the documentation relating to the transaction and then seek to introduce it all in evidence as part of the 'matrix of fact'. Lord Hoffmann sought to meet this criticism in *Bank of Credit and Commerce International* v. *Ali* [2001] UKHL 8, [2002] 1 AC 251 when he stated (at [39]):

> I did not think it necessary to emphasise that I meant anything which a reasonable man would have regarded as *relevant*. I was merely saying that there is no conceptual limit to what can be regarded as background. It is not, for example, confined to the factual background but can include the state of the law (as in cases in which one takes into account that the parties are unlikely to have intended to
> p. 384 agree to something unlawful or legally ineffective) or proved ↵ common assumptions which were in fact quite mistaken … I was certainly not encouraging a trawl through 'background' which could not have made a reasonable person think that the parties must have departed from conventional usage.

This qualification is, however, limited in its scope. It does not purport to fix a formal limit to the scope of the 'factual matrix'. That said, the significance of the factual matrix does vary from case to case. In particular, it is likely to play a lesser role in the case where the issue before the court is the interpretation of a document which is in standard use throughout a particular industry (*Re Sigma Finance Corp (in administrative receivership)* [2009] UKSC 2, [2010] 1 All ER 571) or the interpretation of a public document, such as a charge

registered in the land registry, which is available for inspection (*Cherry Tree Investments Ltd* v. *Landmain Ltd* [2012] EWCA Civ 736, [2013] Ch 305). It is, however, important not to push the latter point too far. It is not the case that the factual matrix is entirely irrelevant in the case of standard form contracts or public documents (*BNP Paribas Trust Corporation UK Ltd* v. *Uro Property Holdings, SA* [2022] EWHC 3251 (Comm), [105] and [115]). It remains relevant but has a more limited role to play (*In re LB Holdings Intermediate 2 Ltd (in administration) and In re Lehman Brothers Holdings plc (in administration)* [2021] EWCA Civ 1523, [2022] Bus LR 10, [28]) and, where relevant, it is more likely to take the form of evidence of the market or public understanding of the term rather than evidence that relates to the particular position of the parties to the individual contract (given that the aim of using a standard form or public document is likely to be that there should be a common interpretation of the term which holds good for all users of the contractual document).

The function of the matrix of fact is to 'elucidate the contract, and not contradict it' (*Contra Holdings Ltd* v. *Bamford* [2023] EWCA Civ 374, [31]). Thus it is not an alternative to textual analysis but it provides additional sources upon which a court can draw when seeking to ascertain the meaning of the disputed term. In order to fall within the matrix of fact the evidence relied upon must have been known to, or reasonably available to, both contracting parties. It does not suffice to prove that the evidence was available to, or known by, one contracting party. The scope of the matrix of fact is therefore broad.

There is, however, little evidence that judges have experienced difficulty in ascertaining what does and what does not fall within the matrix of fact or in restraining the excesses of counsel. The point was well put by Arden LJ in *Static Control Components (Europe) Ltd* v. *Egan* [2004] EWCA Civ 392, [2004] 2 Lloyd's Rep 429 when she stated:

> When the principles in the *ICS* case were first enunciated, there were fears that the courts would on simple questions of the construction of deeds and documents be inundated with background material. Lord Hoffmann recognised this risk by emphasising in *BCCI* v. *Ali* [2002] 1 AC 251 at 269 that his reference to 'absolutely anything' in his second proposition was to anything that a reasonable man would have regarded as relevant. Speaking for myself, I am not aware that the fears expressed as to the opening of floodgates have been realised. The powers of case management in the Civil Procedure Rules could obviously be used to keep evidence within its proper bounds. The important point is that the principles in the *ICS* case lead to a more principled and fairer result by focusing on the meaning which the relevant background objectively assessed indicates that the parties intended.

To the extent that uncertainty persists it would appear to relate to the weight to be given to the evidence once it has been admitted rather than to the decision whether to admit the evidence or not.

p. 385

11.4.5 The Exclusionary Rules

Lord Hoffmann's third principle in *Investors Compensation Scheme* is his exception to the rule that documents are to be interpreted in accordance with the common-sense principles by which any serious utterance would be interpreted in ordinary life. It is a principle that declares certain types of evidence to be inadmissible. In so far as it states that 'declarations of subjective intent' are inadmissible, it has not given rise to debate. The first

principle establishes that the test to be applied by the court is an objective one and so the exclusion of statements of subjective intent does not occasion surprise. More difficult is the exclusion of 'previous negotiations'. In *Investors Compensation Scheme* Lord Hoffmann acknowledged that the boundaries of this exclusion are 'in some respects unclear' and it was not until the decision of the House of Lords in *Chartbrook Ltd* v. *Persimmon Homes Ltd* [2009] UKHL 38, [2009] 1 AC 1101 that the issue was resolved.

In *Chartbrook* the House of Lords affirmed the existence of this general exclusionary rule. In declining to depart from the general rule, their Lordships attached importance to the need to uphold the value of certainty in the interpretation of contracts and to the imperative not to increase the costs of litigation by increasing still further the range of admissible evidence. As Lord Hoffmann observed (at [37]), the law of contract is 'designed to enforce promises with a high degree of predictability' and 'the more one allows conventional meanings or syntax to be displaced by inferences drawn from background, the less predictable the outcome is likely to be'. Lord Hoffmann summed up the reasoning of their Lordships in the following passage (at [41]):

> The conclusion I would reach is that there is no clearly established case for departing from the exclusionary rule. The rule may well mean … that parties are sometimes held bound by a contract in terms which, upon a full investigation of the course of negotiations, a reasonable observer would not have taken them to have intended. But a system which sometimes allows this to happen may be justified in the more general interest of economy and predictability in obtaining advice and adjudicating disputes. It is, after all, usually possible to avoid surprises by carefully reading the documents before signing them and there are the safety nets of rectification and estoppel by convention. Your Lordships do not have the material on which to form a view. It is possible that empirical study (for example, by the Law Commission) may show that the alleged disadvantages of admissibility are not in practice very significant or that they are outweighed by the advantages of doing more precise justice in exceptional cases or falling into line with international conventions. But the determination of where the balance of advantage lies is not in my opinion suitable for judicial decision.

It is, however, important to observe the scope of the rule which excludes evidence of pre-contractual negotiations. As Lord Hoffmann observed (at [47]):

> There are two legitimate safety devices which will in most cases prevent the exclusionary rule from causing injustice. But they have to be specifically pleaded and clearly established. One is rectification. The other is estoppel by convention … If the parties have negotiated an agreement upon some common assumption, which may include an assumption that certain words will bear a certain meaning, they may be estopped from contending that the words should be given a different meaning. Both of these remedies lie outside the exclusionary rule, since they start from the premise that, as a matter of construction, the agreement does not have the meaning for which the party seeking rectification or raising an estoppel contends.

p. 386 ↵ Lord Hoffmann's confidence in the ability of these 'safety devices' to prevent injustice may be questioned. Both rectification (see 16.7) and estoppel by convention (see 5.3.4) operate within narrow confines and so may provide little solace for the party seeking to rely on them in a particular case. More comfort may

be found in a broader exception subsequently recognized by the Supreme Court, namely that pre-contractual negotiations which are 'part of the factual matrix' may be admissible in evidence (*Oceanbulk Shipping and Trading SA* v. *TMT Asia Ltd* [2010] UKSC 44, [2011] 1 AC 662, [40]), although the 'facts' admissible in evidence are confined to those known to both parties and do not extend to 'a mere negotiating position taken by one of the parties' (*Northrop Grumman Missions Systems Europe Ltd* v. *BAE Systems (Al Diriyah C41) Ltd* [2015] EWCA Civ 844, [2015] BLR 657, [31]). The Court of Appeal in *Merthyr (South Wales) Ltd* v. *Merthyr Tydfil County Borough Council* [2019] EWCA Civ 526 recognized that it may not always be easy to distinguish between the case where previous negotiations are legitimately relied upon to identify the 'genesis and aim of the transaction' and the case where they are impermissibly relied upon for the purpose of showing what the parties intended a particular provision in a contract to mean (although on the facts of the case the Court of Appeal had no difficulty in concluding that the pre-contractual negotiations were not admissible because they were being relied upon to support the submission that a clause of the agreement should be interpreted in a particular way). The likelihood is that the decision in *Chartbrook* will give rise to the occasional injustice but, in the view of their Lordships, that injustice is outweighed by the certainty and predictability which the maintenance of the general exclusionary rule will provide (see also *Scottish Widows Fund and Life Assurance Society* v. *BGC International* [2012] EWCA Civ 607, (2012) 142 Con LR 27, [34]–[35] and [70]).

Lord Hoffmann made no express reference in his speech in *Investors Compensation Scheme* to the admissibility of evidence of conduct subsequent to the making of the contract. Pre-*Investors Compensation Scheme* authority establishes that such evidence is inadmissible (*Schuler AG* v. *Wickman Machine Tool Sales* [1974] AC 235), although it may be relevant to a plea of estoppel, including estoppel by convention (*James Miller & Partners Ltd* v. *Whitworth Street Estates (Manchester) Ltd* [1970] AC 583; *Mannai Investment Co Ltd* v. *Eagle Star Life Assurance Co Ltd* [1997] AC 749, 768 (Lord Steyn) and 779 (Lord Hoffmann)), to the question whether a contract has been subsequently varied (*Philip Collins Ltd* v. *Davis* [2000] 3 All ER 808, 822) and it does not apply to oral contracts (*Maggs (t/a BM Builders)* v. *Marsh* [2006] EWCA Civ 1058, [2006] BLR 395). The reason given for the exclusion of this evidence is that, were it admissible, the contract could mean one thing on the day on which it was signed but mean something completely different six weeks later by virtue of the subsequent conduct of the parties. This exclusionary rule has been affirmed in a number of cases post-*Investors Compensation Scheme* (see, for example, *The 'Tychy' (No 2)* [2001] EWCA Civ 1198, [2001] 2 Lloyd's Rep 403, [33]) but has been departed from in New Zealand (see *Wholesale Distributors Ltd* v. *Gibbons Holdings Ltd* [2007] NZSC 37, [2008] 1 NZLR 277, noted by Berg (2008) 124 *LQR* 6).

11.4.6 The Iterative Nature of the Process

In his judgment in *Wood* v. *Capita Insurance Services Ltd* Lord Hodge referred (at [12]) to the 'iterative' nature of the process by which each suggested interpretation is checked against the provisions of the contract and its commercial consequences are investigated. In this way the process of interpretation requires both a textual
p. 387 analysis of the language used against the ↵ background of facts reasonably available to the parties and consideration of the commercial consequences of the rival interpretations. A helpful indication of the range of materials to which the courts will have regard when carrying out this iterative process is provided in the judgment of Lord Neuberger in *Arnold* v. *Britton* (at [15]). It can be seen that the effect of the approach is gradually to expand the range of materials to be taken into account. Lord Neuberger commences with the natural and ordinary meaning of the clause that is in dispute. This is a good place to start but it is important to

state that this is the beginning and not the end of the inquiry. Then, secondly, he states that the court will have regard to any other relevant provisions of the contract. This is an important point. It is important to set the clause in dispute in the context of the contract as a whole and, when that exercise is conducted, it may be that the prima facie meaning of the disputed clause has to give way to an alternative possible meaning so that the disputed clause can then be reconciled with the other provisions of the contract. This is the essence of the iterative process. Beyond the express terms of the contract, Lord Neuberger states that the court should have regard to the overall purpose of the disputed clause, the facts and circumstances known or assumed by the parties at the time of entry into the contract, and commercial common sense.

The range of materials to which the courts can have regard can be identified with some precision. Much more difficult is the weight to be given to these factors. The courts have been less clear on this issue. It is suggested that much depends upon the clarity which is obtained by examining the words of the disputed clause in the context of the contract as a whole. Where the meaning of the disputed clause is clear and that meaning fits within the structure of the contract as a whole, the wider circumstances surrounding the contract and considerations of commercial common sense are unlikely to persuade a court to depart from the clear meaning of the term in dispute (see, for example, *Mutual Energy Ltd* v. *Starr Underwriting Agents Ltd* [2016] EWHC 590 (TCC), [2016] BLR 312). However, it is not impossible that a court may do so in an exceptional case. Thus in *DnaNudge Ltd v Ventura Capital GP Ltd* [2023] EWCA Civ 1142, [46] Snowden LJ observed that 'in a rare case, even where there is no ambiguity in the language, the iterative process may lead the court to conclude that something has gone wrong and that there has been a mistake in the drafting of the document.' Such a case is most likely to arise where there is an obvious error on the face of the document or, more controversially, in the case where 'when the other terms of the contract and the context is taken into account, it becomes apparent that the ordinary and natural meaning of the words used cannot have been what the drafter meant, because the outcome makes no rational sense.' A court is, however, likely to be slow to reach such a conclusion as evidenced by the fact that such a case is described as being 'rare'. The case in which a broader range of factors is mostly likely to be taken into account by a court is where the meaning of the disputed term is not clear. In such a case the court is much more likely to have regard to, and attach weight to, the surrounding circumstances and considerations of common sense when seeking to decide which of the possible competing meanings is the correct one.

11.4.7 Choosing Between Competing Possible Meanings

The iterative approach assumes particular significance in the case where the term in dispute is capable of being interpreted in different ways. In such a case, how does the court go about the task of choosing which of the possible meanings of the disputed term is the correct one? No single answer can be given to this question
p. 388 which holds good for all circumstances. ↵ The answer will inevitably depend, at least to some extent, upon the facts and circumstances of the particular case.

In the case where the contract has been drawn up with the benefit of professional advice, it is textual analysis which, for the reasons already given, is likely to weigh most heavily in the scales. On the other hand, in the case of an informal contract, a court may have more regard to the factual matrix. The commercial sense of the competing interpretations is also, as we shall see, likely to be an important factor (see 11.4.8) in the sense that,

where the terms of the contract are genuinely capable of two or more meanings, a court will often select the meaning that achieves a commercially sensible outcome (particularly in the case where one interpretation leads to a commercially sensible outcome and the other does not).

However, the court, when seeking to identify the true meaning of the disputed term. is not confined to the adoption of an interpretation which has been advanced by the parties to the litigation. Although it is rare for a court to do so, it can select a meaning for which neither party has contended. Such was the case in *Sara & Hossein Asset Holdings Ltd* v. *Blacks Outdoor Retail Ltd* [2003] UKSC 2, [2023] 1 WLR 575, [50]–[57] where Lord Hamblen, giving the majority judgment of the Supreme Court, adopted a construction of the lease for which neither party had contended but which he believed was an interpretation that gave effect to the contract as a whole and reached a commercially sensible conclusion (whereas on his view the approach adopted by one party was consistent with the meaning of the disputed words but did not fit the wider contractual context, while the approach of the other party did fit that contractual context but not the wording of the disputed provision). Lord Briggs, while not unsympathetic to the result reached by the majority, dissented on the ground that he could see no basis for the proposed interpretation in the wording of the lease ([62]) and he observed ([61]) that 'it is well-settled that the uncommerciality of the prima facie meaning of contractual words only yields to a more commercial alternative if there is some basis in the language of the contract as a peg upon which that alternative can properly be hung.' While *Sara & Hossein* is in many respects an unusual case, it does illustrate the scope which the principles applicable to the interpretation of contracts give to the courts when deciding which of the competing possible meanings is the correct one.

11.4.8 Something Has Gone Wrong with the Language

What are the courts to do when it is alleged that something has gone wrong in the drafting process and it is submitted by one of the parties that the natural and ordinary meaning of the disputed term does not give effect to the intention of the parties? Lord Hoffmann addressed this issue in his fifth principle in *Investors Compensation Scheme* where he referred to the case where 'something must have gone wrong with the language'. In such a case he stated that the law 'does not require the judges to attribute to the parties an intention which they plainly could not have had'. There is, however, an initial hurdle that must be overcome by a party who wishes to submit that something has 'gone wrong with the language'. That hurdle is that the courts 'do not easily accept that people have made linguistic mistakes'.

The importance of this hurdle was affirmed by the House of Lords in *Chartbrook Ltd* v. *Persimmon Homes Ltd* [2009] UKHL 38, [2009] 1 AC 1101, where Lord Hoffmann acknowledged (at [15]) that it 'requires a strong case to persuade the court that something must have gone wrong with the language'. In order to establish such a
p. 389 'strong case' it is necessary to do ↵ more than demonstrate that a particular interpretation results in an outcome which is especially favourable to one party. As Lord Hoffmann observed (at [20]):

> It is of course true that the fact that a contract may appear to be unduly favourable to one of the parties is not a sufficient reason for supposing that it does not mean what it says. The reasonable addressee of the instrument has not been privy to the negotiations and cannot tell whether a provision favourable to one side was not in exchange for some concession elsewhere or simply a bad bargain. But the striking feature of this case is not merely that the provisions as interpreted by the judge and the Court of Appeal are favourable to Chartbrook. It is that they make the structure and language of the various provisions of Schedule 6 appear arbitrary and irrational, when it is possible for the concepts employed by the parties … to be combined in a rational way.

Thus there comes a point (which is not easy to define) where the results are so startling that the court will conclude that the contract does not mean what it says and it will then look to adopt a construction of the contract which gives effect to the intention of the parties.

Once this point has been reached, the court's powers to adapt the language of the contract in order to give effect to the intention of the parties would seem to be broad. Lord Hoffmann in *Chartbrook* summarized these powers as follows (at [21]):

> I do not think that it is necessary to undertake the exercise of comparing this language with that of the definition in order to see how much use of red ink is involved. When the language used in an instrument gives rise to difficulties of construction, the process of interpretation does not require one to formulate some alternative form of words which approximates as closely as possible to that of the parties. It is to decide what a reasonable person would have understood the parties to have meant by using the language which they did. The fact that the court might have to express that meaning in language quite different from that used by the parties ('12th January' instead of '13th January' in *Mannai Investment Co Ltd* v. *Eagle Star Life Assurance Co Ltd* [1997] AC 749; 'any claim sounding in rescission (whether for undue influence or otherwise)' instead of 'any claim (whether sounding in rescission for undue influence or otherwise)' in *Investors Compensation Scheme Ltd* v. *West Bromwich Building Society*) … is no reason for not giving effect to what they appear to have meant.

He continued (at [25]):

> What is clear … is that there is not, so to speak, a limit to the amount of red ink or verbal rearrangement or correction which the court is allowed. All that is required is that it should be clear that something has gone wrong with the language and that it should be clear what a reasonable person would have understood the parties to have meant.

The importance of these statements lies in their willingness to engage in a measure of rewriting of the contract under the guise of interpretation (a process described as 'corrective interpretation' by Arden LJ in *Cherry Tree Investments Ltd* v. *Landmain Ltd* [2012] EWCA Civ 736, [2013] Ch 305, [62]). It is no longer necessary to resort to the remedy of rectification (see 16.7) in order to achieve this measure of rewriting. This change has not been to everyone's taste. Sir Richard Buxton, writing extrajudicially ('"Construction" and Rectification
p. 390 after *Chartbrook*' [2010] *CLJ* 253, 256), criticized Lord Hoffmann's fifth principle on the ground ↵ that it was 'revolutionary because it overrode the previous understanding that, rectification apart, the court could

not depart from the words of the document to find an agreement different from that stated in the document' and that it confused 'the meaning of what the parties said in the document with what they meant to say but did not say'. In *Oceanbulk Shipping and Trading SA* v. *TMT Asia Ltd* [2010] UKSC 44, [2011] 1 AC 662, [44] Lord Clarke accepted that there was a 'close relationship between interpretation and rectification' but did not otherwise endorse the criticism of Lord Hoffmann's fifth principle.

However, it is important to note the limits of Lord Hoffmann's principle, in particular the requirement that 'it should be clear what a reasonable person would have understood the parties to have meant'. In other words, both the mistake and the intended outcome must be clear. It does not suffice to establish that it is 'undoubtedly possible that something has gone wrong' It must be 'clear' that something has gone wrong (*Altera Voyageur Production Ltd* v. *Premier Oil E&P UK Ltd* [2020] EWHC 1891 (Comm), [2021] 1 Lloyd's Rep 451, [67]). As Rix LJ observed in *ING Bank NV* v. *Ros Roca SA* [2011] EWCA Civ 353, [2012] 1 WLR 472, [110], 'judges should not see in *Chartbrook* an open sesame for reconstructing the parties' contract, but an opportunity to remedy by construction a clear error of language which could not have been intended'. Further, construction cannot be 'pushed beyond its proper limits in pursuit of remedying what is perceived to be a flaw in the working of a contract'.

This concern to ensure that interpretation is not pushed beyond its proper limits is also apparent in the judgments of Lord Neuberger in *Arnold* v. *Britton* and Lord Hodge in *Wood* v. *Capita Insurance Services* (discussed earlier). In *Arnold* Lord Neuberger's warning (at [17]) that considerations of commercial common sense must 'not be invoked to undervalue the importance of the language of the provision which is to be construed' is clearly intended to provide a measure of certainty to contracting parties in cases where they have drafted a contract the meaning of which is clear. As Lord Clarke observed in *Rainy Sky SA* v. *Kookmin Bank* [2011] UKSC 50, [2011] 1 WLR 2900, [23], 'where the parties have used unambiguous language, the court must apply it'. In other words, where the meaning of the term is clear, it is not the function of the court to give it a different meaning in an attempt to render the term more reasonable or 'commercially sensible'. To similar effect is the judgment of Lord Hodge in *Wood,* to which reference has already been made, when he stated (at [13]) that 'some agreements may be successfully interpreted principally by textual analysis, for example because of their sophistication and complexity and because they have been negotiated and prepared with the assistance of skilled professionals'. As has been pointed out, the word 'principally' is important here. The point being made is not that there is an exclusive focus on the words used by the parties. Rather, it is that, at least in the case where the parties have access to legal advice and can be expected to use the English language properly, the courts will more likely give effect to the intention of the parties if they give primary weight to the text which the parties have agreed. However, it is here important to re-affirm that an emphasis on the meaning of the words used by the parties (and on giving the words their ordinary and natural meaning) is not to be equated with an over-literal interpretation of one provision without regard to the whole of the document, particularly in the case of complex documents which have been put into circulation in the market (*Metlife Seguros de Retiro SA* v. *JP Morgan Chase Bank, National Association* [2016] EWCA Civ 1248; *Re Sigma Finance Corp* [2009] UKSC 2, [2010] 1 All ER 571).

But this heavy emphasis on the importance of the words used by the parties does not hold true in all cases. Courts have greater flexibility where the disputed term is capable of more than one meaning, the contract is badly drafted (see *Arnold* at [18]), the parties' use of punctuation is erroneous or erratic (*Vitol E&P Ltd* v. *New*
p. 391 *Age (African Global Energy) Ltd* [2018] ↵ EWHC 1580 (Comm), [28]), or the parties are operating in an

informal context (see *Wood* at [13]). In these cases, when considering the alternative possible meanings of the term, the court should consider which interpretation is the more commercially sensible and in most cases can be expected to adopt the more, rather than the less, commercial construction (*Rainy Sky SA* v. *Kookmin Bank* [2011] UKSC 50, [2011] 1 WLR 2900, [30]). The court is not, however, obliged to adopt the more commercially sensible interpretation. There is no rule of law that requires the court to give effect to the interpretation which is most consistent with business common sense. It is entitled to prefer that interpretation and it may be generally appropriate to do so but it is not bound to do so. The more ambiguous the meaning of the term and the stronger the arguments based on business common sense, the more likely it is to be appropriate to adopt that interpretation. Or, to put the same point another way, 'the less the commercial sense of a construction of an agreement, the greater the need to scrutinise its literal wording and if possible to depart from it to give a commercially sensible interpretation' (*African Minerals Ltd* v. *Renaissance Capital Ltd* [2015] EWCA Civ 448, [40], *Fomento de Construcciones Y Contratas SA* v. *Black Diamond Offshore Ltd* [2016] EWCA Civ 1141, [12]).

In those cases where the courts do have regard to considerations of commercial common sense, it is important to note that these considerations are not to be viewed retrospectively (*Arnold* at [19]). Such considerations are not infrequently invoked by parties who have entered into a bad bargain. But the fact that the bargain has turned out to be a bad one is not a relevant consideration. The reason for this is that the consideration of the demands of commercial common sense is to be undertaken at the moment of entry into the contract, not the date of the breach or the date of the hearing before the court. As Lord Grabiner has observed ('The Iterative Process of Contractual Interpretation' (2012) 128 *LQR* 41, 46), it is 'critically important' that the commercial purpose of the disputed clause is 'derived from the contract as a whole and from an accurate understanding of the way in which the various provisions interact' and that it does not degenerate into 'little more than an appeal to the court for a more reasonable result' (p. 50).

Finally, in this context it is important to stress that it is not the task of the court to write or make the contract for the parties (see *Arnold* at [20]). As Arden LJ observed in *Credit Suisse Asset Management LLC* v. *Titan Europe 2006-1 plc* [2016] EWCA Civ 1293, [28], party autonomy is a fundamental principle of English contract law from which it follows that the court will not rewrite the bargain that the parties have freely chosen to make (see also *BP Gas Marketing Ltd* v. *La Société Sonatrach* [2016] EWHC 2461 (Comm), [274]). This desire to avoid being seen to rewrite the contract for the parties helps to explain why it is that courts are hesitant to invoke considerations of commercial common sense in order to override what appears to be the clear meaning of the contract negotiated by the parties. The jurisdiction to depart from the clear meaning of the words agreed by the parties must therefore be exercised with considerable caution. Thus in *Carillion Construction Ltd* v. *Emcor Engineering Services Ltd* [2017] EWCA Civ 65, [2017] BLR 203, [46] Jackson LJ stated that it is 'only in exceptional cases' that commercial common sense can 'drive the court to depart from the natural meaning of contractual provisions' (see also *Grove Developments Ltd* v. *Balfour Beatty Regional Construction Ltd* [2016] EWCA Civ 990, [2017] 1 WLR 1893, [42]). But there does come a point where the consequences of giving to the words their ordinary and natural meaning is so absurd that the court will be prepared to depart from that meaning and adopt a more commercially sensible construction. One such case is *Sutton Housing Partnership Ltd* v. *Rydon Maintenance Ltd* [2017] EWCA Civ 359, where the Court of Appeal rejected the defendant's construction of the contract on the ground that it would have rendered inoperable important parts of the contract. These
p. 392 consequences were held to be 'extraordinary' ↵ and to amount to 'an absurdity, which no-one could have intended'. The claimant's interpretation was accepted on the basis that it was 'the only rational interpretation of the curious provisions into which the parties have entered'. However, it is important to remember that

Sutton Housing Partnership is the exception, not the rule. In the standard case, where the parties have access to legal advice, the court is more likely to give greater weight to the words used by the parties and to give them their ordinary and natural meaning because in doing so they will give effect to the intention of the parties, objectively ascertained.

Further Reading

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Notes

[1] Rectification is discussed in more detail at 16.7. Rectification only comes into play once the meaning of the words used by the parties has been ascertained (for further consideration of the relationship between rectification and interpretation see A Burrows, 'Construction and Rectification' in A Burrows and E Peel (eds), *Contract Terms* (Oxford University Press, 2007), p. 77). A contract can be rectified if there has been a defect in the recording of the contract so that the written agreement does not reflect the agreement which the parties intended to make. On the other hand, if the agreement does give effect to the intention of the parties, there is nothing for the court to rectify.

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