Contractual Interpretation – An Anglo/Australian Journey

The Lehane Lecture 2024

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Introduction

1. The interpretation of contracts is central to civil law practice. Given its fundamental practical importance, one might reasonably expect the relevant principles of interpretation to be clear and settled. However, numerous and varying court decisions over the last thirty years in both England and Australia show that this is far from being the case. Vexed and contentious questions remain and much judicial and academic ink has been spent discussing what the applicable principles are understood to be or should be. In both countries much of the discussion has stemmed from seminal decisions given by the highest court – in the UK Lord Hoffmann's judgment in the House of Lords decision in *Investors Compensations Scheme Ltd v West Bromwich Building Society* ('*ICS*') [1998] 1 WLR 896; in Australia the decision of the High Court in *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales ('Codelfa')* [1982] HCA 24.

2. It might be asked why it is necessary to have any normative rules on the subject of the interpretation of contracts. Why do we not simply read the contract and decide what it means? There are a number of answers to that question. They include:
    a. Firstly, fairness demands, that different judges, and the same judges in different cases, should reach the same answer on materially the same legal questions;

b. Secondly, people who enter into contracts, and their advisers, should be enabled to know what the courts will be likely to hold those contracts to mean, if a dispute should arise; and
c. Thirdly, it is in the interest of the parties to a contract, and in the public interest, that there should be restraints on undue time and money being spent on what should be a limited interpretative task.

3. It has been said that the interpretation of contracts and the meaning of language can never be entirely free of artifice[1]. This artifice is in part due to the ambiguity inherent in language. The German philosopher, Ludwig Wittgenstein. likened the use of language to the art of playing a game[2]. This game is governed by a complex set of rules, which in turn convey meaning to its intended audience. Whilst the rules themselves may be fairly clear, language and its use in different contexts can introduce ambiguity.

4. The task of deciphering contracts can therefore be a complex one. This is further complicated by the retrospective task of interpretation that judges undertake. We are not privy to the circumstances and context within which people make agreements. We have no unique insight into the mindset and aims of the parties. Courts nevertheless have to seek to divine the common intention of the parties.

5. At common law, this is an objective rather than a subjective task. The court is not interested in the subjective intentions of the parties but must instead identify intention

[1] Lord Sumption, "A question of taste: the Supreme court and the Interpretation of Contracts" Harris Society Annual Lecture, Oxford, 2017
[2] Tilghman, B. R. "Wittgenstein, Games, and Art." The Journal of Aesthetics and Art Criticism 31, no. 4 (1973): 517–24. https://doi.org/10.2307/429325.

with reference to what a reasonable person would have understood the contractual term in question to mean. In *Sirius International Insurance Co v FAI General Insurance Ltd* [2004] UKHL 54, Lord Steyn quoted the words of the famous Christian apologist William Paley: 'the tyrant Temures promised the garrison of Sebastia that no blood would be shed if they surrendered to him. They surrendered to him. He shed no blood. He buried them all alive' [19]. The reason that one knows that Temures committed an injustice is that we intuitively know the difference between, on the one hand, the subjective meaning of the utterance, and on the other, what a reasonable person to whom the promise was made would understand the speaker to mean. The objective intention that the court searches for is distinct from subjective meaning.

6. To this end, there are two general approaches to contractual interpretation, often cited as opposites to each other, that are commonly referenced:
    a. 'Textualism' favours the primacy of the natural or ordinary meaning of the words. This theory of interpretation focuses on the contract wording and requires the court to determine the common intention from a restricted evidence-base.
    b. 'Contextualism' by contrast, considers that words have no natural and ordinary meaning divorced from their context and involves consideration of any extraneous material which might help interpret, add to, or even vary the words used. Under this approach much more weight is given to evidence outside the contract itself.

7. *ICS* may be said to represent a strong endorsement of the contextualist approach. It allows for the admission of any evidence which was available to the parties and would have affected the way in which the language used in the contract would have been understood by a reasonable person. This may be described as a 'purist' approach. Any evidence which may assist in achieving interpretative accuracy should be admitted.

8. *Codelfa* focuses more on a textualist approach and limits the evidence which may be admitted to aid the interpretative task. It does so by imposing what has generally been referred to as an 'ambiguity gateway'. Evidence of surrounding circumstances is only admissible if the language of the contract is "ambiguous or susceptible of more than one meaning". This may be described as a 'pragmatic' approach. The search for interpretative accuracy has a cost in terms of the time and expense involved in extensive evidential inquiry for what may ultimately be marginal, if any, gains. To that end limitations should be imposed, as they are by the ambiguity gateway.

9. *ICS* and *Codelfa* therefore represent very different starting points. In this talk I propose to trace how the law in England and Australia has developed from those starting points, to suggest that there has been a degree of convergence and also to discuss ways in which a balance between purism and pragmatism may be struck.

The English journey

10. The modern journey begins with *ICS.*

a. *ICS* 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 recission for undue influence or otherwise)". The issue was whether 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 concluded that when executing the contract of assignment there was no apparent intention to exclude damages claims.

b. In declaring that much of the "old intellectual baggage" of legal interpretation must be discarded, Lord Hoffmann proposed that the formalistic canons of constructions should have a much smaller part to play in what he recognised as the essentially intuitive exercise of contractual interpretation. He set out five principles of contractual interpretation:

c. In summary, 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 are excluded from this background information.

(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.

11. From the start there were some objections to the all-embracing approach adopted by Lord Hoffmann in *ICS* and its practical consequences for litigation and arbitration.

12. That is perhaps not surprising, given that Lord Hoffmann's matrix of facts included "absolutely anything which would have affected the way in which the language of the document would have been understood by a reasonable man". Lord Hoffmann appeared to recognise the expansive implications of this in his clarification of the second principle in *BCCI v Ali* [2002] 1 AC 251 that the matrix referred to anything a reasonable man would regard as "relevant" [269].

13. A striking example of contemporaneous doubt being expressed as to the wisdom of the *ICS* approach is the judgment of Saville LJ in *National Bank of Sharjah v Dellborg* [1997] EWCA Civ 2070 in which he stated as follows:

"…such an approach would seem to entail that even where the words that the parties have chosen to use have only one meaning; and that meaning (bearing in mind the aim or purpose of the agreement) is not self-evidently nonsensical, the Court will not be allowed to adopt that meaning without an explanation of

> the surrounding circumstances which would involve discovery, interrogatories, cross-examination and the like; for a party seeking to challenge that could assert with great force that until the circumstances are fully examined, it is impossible to decide whether or not they should override the plain words of the agreement. This would do nothing but add to the costs and delays of litigation and indeed of arbitration, much of which is concerned with interpreting agreements.
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> …
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> To my mind there is much to be said for the simple rule that where the words the parties have chosen to use have only one meaning, and that meaning (bearing in mind the aim or purpose of the agreement) is not self evidently nonsensical, the law should take that to be their intended agreement, and should allow the surrounding circumstances to override what (*ex hypothesi*) is clear and obvious. This would enable all to know where they stand without the need for further investigations; and for the court to provide the answer, where the point is contested, without undue delay or expense".

14. Similar doubts were expressed by Staughton LJ judicially in *Scottish Power Plc v Britoil (Exploration) Ltd* [1997] EWCA 2752 where he observed that the inclusion of "a large volume of additional background material often added little to the court's understanding of the contract between the parties and merely increased the expense of litigation" and extra-judicially in an article in the Cambridge Law Journal ([1999] 58 CLJ 303). In *Wire TV Ltd v CableTel (UK) Ltd* [1998] CLC 244, 257 Lightman J agreed with Staughton LJ and complained of the "flood of evidence" that had resulted from following *ICS,* the greater part of which he found to be totally unhelpful.

15. The approach in *ICS* was nevertheless affirmed by the House of Lords in *Chartwood Ltd v Persimmon Homes Ltd* [2009] 1 AC 1101. It was further developed by the Supreme Court in *Rainy Sky SA v Kookmin Bank ('Rainy Sky')* [2011] UKSC in which the importance of business common sense was brought to the fore.

    a. The case concerned the interpretation of refund guarantees issued by Kookmin Bank to protect advance payments made by buyers to a shipbuilder under shipbuilding contracts.

    b. A long and poorly-drafted clause required the bank to pay "such sums". The question was which sums these words referred back to. Two interpretations were possible:

        i. The buyer's case, which was that the sums were "instalments" mentioned earlier in the same sentence, as the sums due under the shipbuilding contract, including the refund of advance payments on the shipbuilder's insolvency; and

        ii. The bank's case, which was that these sums were those mentioned in the previous sub-clause, payable on various guarantee trigger events but not insolvency.

    c. The shipbuilder suffered financial difficulties and the buyer claimed under the guarantees. The bank argued that, properly interpreted, its guarantee obligations were not triggered by the shipbuilder's insolvency. Insolvency was not specifically mentioned in the guarantee bond but other events such as rejection or total loss of the vessel were. Under the shipbuilding contract, however, the shipbuilder was required to refund advance payments if it became insolvent. The arguments were finely balanced; at first instance the

judge ruled in the buyer's favour but the Court of Appeal overturned the decision by a majority.

d. The Supreme Court considered the role to be played by business common sense in deciding what the parties meant. In cases where the parties have used completely unambiguous language, the court must apply it. However, in many cases, as here, two interpretations are possible. Often, neither of them will flout business common sense. In that case, it is generally appropriate to prefer the interpretation which is most consistent with *business common sense*. It is not necessary to conclude that a particular interpretation would produce an absurd or irrational result before having regard to the commercial purpose of the agreement.

e. If they had looked only at the language, the Supreme Court's judgment suggested they might have preferred the bank's interpretation. However, the argument that proved fatal to the bank's interpretation was that it would lead to what the judge called a “surprising and uncommercial result”. On the bank's interpretation, the guarantees would cover every situation in which the buyers could claim a refund, except the situation in which they were most likely to need it, namely the shipbuilder's insolvency. The bank could not suggest any commercial reason for the buyer to have agreed to this. The Supreme Court therefore, agreeing with the judge and Sir Simon Tuckey in the Court of Appeal, preferred the buyer's interpretation, because it was consistent with the commercial purpose of the guarantees in a way that the bank's was not.

16. Following *Rainy Sky* it became commonplace for the court to be faced with detailed and complex arguments from each party as to why their interpretation was more

consistent with business common sense. This exposed the practical difficulties of over-reliance on such an approach. As I observed in *Cottonex Anstalt v Patriot Spinning Mills Ltd* [2014] EWHC 236 (Comm), [2014] 1 Lloyd's Rep 615 at para 57:

> "…it will only be appropriate to give effect to the interpretation which is most consistent with business common sense where that can be ascertained by the court. In many cases that is only likely to be so where it is clear to the court that one interpretation makes more business common sense. If, as frequently happens, there are arguments either way the court is unlikely to be able to conclude with confidence that there is an interpretation which makes more business common sense. It is often difficult for a court of law to make nice judgments as to where business common sense lies".

17. Neither the advocates who argue the points of construction nor the judges who determine them are commercial men. Judges are not necessarily well-placed to determine what business common sense requires. Since judges are often moulded by notions of fairness, proportionality and are outcome driven, they may approach questions of contractual interpretation differently to the parties that entered into commercial agreements with a competitive spirit and with the aim to serve their own interests. As Neuberger LJ cautioned in *Skanska Rasleigh Weatherfoil Ltd* [2006] EWCA Civ 1732 at para 22:

> "Judges are not always the most commercially-minded, let alone the most commercially experienced, of people, and should, I think, avoid arrogating to themselves overconfidently the role of commercial reasonableness or likelihood".

18. In *Arnold v Britton* [2015] 2 W.L.R. 1593 the Supreme Court refined the approach adopted in *ICS* and *Rainy Sky* – indeed many have said that the court departed from it. The court was required to interpret a service charge provision in relation to a 99 year leasehold agreement.

    a. The agreement itself related to a holiday home in South Wales. 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.

    b. 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.

    c. 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 that "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" [17]. He went on to note that that "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" [19]. In other words, Lord Neuberger sought to give greater weight to the words used in the contract and to discourage courts from re-writing agreements to reflect the courts view of commercial common sense.

19. The court made clear that business or commercial 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.

20. Commentators were divided over whether this case marked a retreat from Lord Hoffmann's principles in *ICS* and over whether changes to the principles of interpretation were desirable.
    a. Richard Calnan remarked: "There is a distinct chill in the air … The Supreme Court, under the influence of Lord Neuberger, has stressed that the main focus should be on the natural meaning of the words the parties have used, and that twisting the meaning of those words to reflect commercial common sense should be a minority sport"[3].
    b. Sir Geoffrey Vos commented that it represented a "sea change in the law" and concluded that now "there is not, save anyway in a most exceptional case or a case of obvious absurdity, any scope for adjusting the language to reflect what

[3] Richard Calnan, "Principles of Contractual Interpretation", 2nd edn, 2017, 27

the objective observer would think the parties must actually have meant in the light either of the other terms of the written contract or the available factual matrix"[4].

c. Lord Sumption wrote that the Supreme Court had "sounded the retreat". He welcomed what he saw as a renewed emphasis on the language used, observing that "language, properly used, should speak for itself and it usually does"[5]. He criticised the approach in *ICS* for presuming an inherent adaptability of all language and its disparagement of dictionaries and grammars as tools of interpretation. He commented that: "the Supreme Court has begun to withdraw from the more advanced positions seized during the Hoffmann offensive, to what I see as a more defensible approach".

21. This led to a robust response from Lord Hoffmann in a Law Quarterly Review article entitled "Language and Lawyers"[6]. He criticised Lord Sumption's view as a form of "nostalgia" for the stricter approach of a bygone age, took issue with Lord Sumption's characterisation of his own approach, and concluded: "let us not go back to the dark ages of word magic, of irrebuttable presumptions by which the intentions of a user of language are stretched, truncated or otherwise mangled to give effect to the 'admissible', 'strict and proper', 'natural and ordinary' or 'autonomous' meanings of words, even when it is obvious that it was not the meaning the author, actual or notional, could have intended."

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[4] Geoffrey Vos, "Contractual Interpretation: Do Judges Sometimes Say One Thing and Do Another" (2017) 23 Canta LR 1, at 11

[5] Lord Sumption "A Question of Taste", Supreme Court Yearbook vol 8 (2016-17)

[6] (2018) 134 LQR 553

22. Meanwhile, in *Wood v Capita Insurance Services Ltd* [2017] UKSC 24 the Supreme Court sought to calm these increasingly turbulent waters. Lord Hodge, giving the majority judgment said that *Arnold v Britton* had not involved a change in approach from *Rainy Sky* and that "the recent history of the common law of contractual interpretation is one of continuity rather than change".

    a. The case concerned whether liability for past mis-selling was recoverable under an imprecise and "opaque" indemnity in an share purchase agreement. The indemnity required the seller to indemnify the buyer against a comprehensive list of events arising out of "claims or complaints registered with the [company's regulator]… against the company". The seller argued that it did not have to indemnify the buyer because the company had reported itself to the regulator, so there was no complaint against it.

    b. Although the Supreme Court considered the indemnity in its contractual and commercial context, it concluded that the interpretative tool of "principal" importance was still a "careful examination of the language" [42].

    c. The Supreme Court adopted the literal interpretation of the indemnity advanced by the seller and disregarded what many would have understood to be the parties' commercial intention in agreeing such an indemnity.

    d. Lord Hodge noted that it has long been accepted that interpretation is not a purely "literalist exercise focused solely on... the wording" but requires consideration of the contract as a whole, the wider context, business common sense and the commercial purpose. According to Lord Hodge, the amount of weight attributed to each of these factors depends on the context. The Supreme Court expressly acknowledged that some contracts may need to be interpreted with "greater emphasis" on their factual matrix and commercial purpose for

reasons such as informality, brevity, differing drafting practises, deadline pressures and failures of communication.

e. Lord Hodge also addressed the longstanding tension between contextualism and textualism. He added: "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."

23. This compromise approach has largely been successful and in many decisions requiring contractual interpretation it is now often the only case cited. The *Wood v Capita* approach may be summarised as follows:

    a. The contract must be interpreted objectively by asking what a reasonable person, with all the background knowledge which would reasonably have been available to the parties when they entered into the contract, would have understood the language of the contract to mean.

    b. The court must consider the contract as a whole and, depending on the nature, formality and quality of its drafting, give more or less weight to elements of the wider context in reaching its view as to its objective meaning.

    c. Interpretation is a unitary exercise which involves an iterative process by which each suggested interpretation is checked against the provisions of the contract and its implications and consequences are investigated.

24. Although there are no principles applicable to the interpretation of particular categories of contract, the nature of the contract may influence the relative weight to be given to the text of the contract, and the overall context on the other. This is helpful for judges as it allows them to tailor their approach to the contract in question.

25. Where a contract has been professionally drafted, there is less room for departure from a textual analysis. For example, as I explained, in *National Bank of Kazakhstan v the Bank of New York Mellon SA/NV, London Branch* [2018] EWCA Civ 1390*:* "In the present case, the [contract] is a carefully drafted and formal contract, drawn up with the assistance of lawyers and concluded between sophisticated parties. There is no suggestion that anything has gone wrong in the drafting process. Nor is there any patent ambiguity in the term used in clause 16(i). In accordance with the guidance in *Wood v Capita,* it is the type of agreement in relation to which textual analysis is of particular relevance" [39].

26. *Wood v Capita* therefore gives freedom to judges to decide the appropriate weight to be given to context in each case. There is no rule that it is always of importance and there are many cases in which the text is likely to be given predominant weight. As Mr Justice Foxton has stated: "we are all purposive sheep now, just as we are all literalist goats" with "the approach to construction now confirmed as one requiring a 'unitary exercise' which accommodates bovids of both kinds"[7].

[7] See Foxton D, "The Status of the Special Rules of Construction of Exemption Clauses in Commercial Contracts" [2021] JBL 205.

27. In summary, although there is no limit other than relevance to the evidence of surrounding circumstances which may be admitted, *Wood v Capita* means that in many cases such evidence will be limited and the main focus will be on the text of the contract. In this way the development of the law since *ICS* has addressed some of the pragmatic concerns which arise if too purist an approach is taken and the dangers of an evidential 'free for all' which it was feared would result from *ICS* have been tempered.

The Australian journey

28. The Australian journey starts with *Codelfa* and Mason J's statement of the "true rule":

> "The true rule is that evidence of surrounding circumstances is admissible to assist in the interpretation of the contract if the language is ambiguous or susceptible of more than one meaning. But it is not admissible to contradict the language of the contract when it has a plain meaning".

29. Any description of subsequent developments is complex given the involvement of federal and state courts and the fact that they have not all spoken with one voice. Given your much greater familiarity with Australian law I shall attempt only a brief summary.

30. In a series of decisions the High Court appeared to state the law in similar terms to *ICS* and to have regard to surrounding circumstances without applying any ambiguity threshold. For example:

a. In *Maggbury Pty Ltd Hafele Australia Pty Ltd* [2001] HCA 70, the majority stated that: "interpretation of a written contract involves, as Lord Hoffmann has put it: '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."

b. In *Pacific Carriers Ltd v BNP Paribas* [2004] HCA 35 the High Court held that the construction of letters of indemnity was to be determined by what a reasonable person would have understood them to mean and addressed that question by considering the text of the letters of indemnity, the surrounding circumstances known to the parties and the purpose and object of the transaction without regard to whether there was ambiguity.

c. In *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* (2004) 219 CLR 165, the High Court considered surrounding circumstances to ascertain the meaning of an exclusion clause within a credit application form. The panel agreed that the exclusion clause applied, even though Alphapharm had not read it and concluded that "it is not the subjective belief or understandings of the parties about their rights and liabilities that govern their contractual relations. What matters is what each party by words and conduct would have led a reasonable person in the position of the other party to believe"; "that normally requires consideration not only of the text, but also of the surrounding circumstances known to the parties, and the purpose of object of the transaction" [179].

31. However, the High Court has also expressly affirmed the continued applicability of *Codelfa*. In *Royal Botanic Gardens and Domain Trust v South Sydney City Council*

[2002] HCA 5 (‘*Royal Botanic*’), the majority explained that “reference was made in argument to several decisions of the High Court, delivered since *Codelfa* but without reference to it ...[however] it is unnecessary to determine whether their Lordships there took a broader view of the admissible "background" than was taken in *Codelfa* or, if so, whether those views should be preferred to those of this Court. Until that determination is made by this Court, other Australian courts, if they discern any inconsistency with *Codelfa*, should continue to follow *Codelfa”* [29]. In criticising the contextualist approach Kirby J trenchantly observed that: “It is as if some who have responsibility of interpretation of legal words find the reading and analysis of the texts themselves distasteful, like dentists happy to talk about the problem, but loathe to pull a tooth” [70].

32. Similarly in *Western Export Services Inc v Jireh International Pty Ltd* [2011] HCA 45, three judges of the High Court, in refusing special leave to appeal, said “the position of *Codelfa*, as a binding authority, was made clear in the joint reasons of five Justices in *Royal Botanic* and it should not have been necessary to reiterate the point here” [4]**.**

33. The subsequent High Court decision in *Electricity Generation Corporation v Woodside Energy* [2014] 251 CLR 640 (*‘Woodside’*) arguably allowed for a wider consideration of surrounding circumstances, at least in relation to commercial contracts. Although the High Court cited *Codelfa* with approval, it also stated that “the meaning of the terms of a commercial contract is to be determined by what a reasonable businessperson would have understood those terms to mean. That approach is not unfamiliar. As reaffirmed, it will require consideration of the

language used by the parties, the surrounding circumstances known to them and the commercial purpose or objects to be secured by the contract. Appreciation of the commercial purpose or objects is facilitated by an understanding "of the genesis of the transaction, the background, the context [and] the market in which the parties are operating" [35]. No mention was made of the need for ambiguity.

34. *Woodside* was followed by the High Court decision in *Mount Bruce Mining Pty Ltd v Wright Prospecting Pty Ltd* [2015] 256 (‘*Mount Bruce’)* which confirmed that *Codelfa* remained the law and sought to clarify the analysis in *Woodside* by framing it as merely allowing the court to consider “the language used by the parties in the contract, the circumstances addressed by the contract and the commercial purpose or objects to be secured by the contract” [47] and stating that “ordinarily” this is possible by reference to the contract alone” [48].

35. The High Court in *Mount Bruce* also pointed out an additional query left unanswered by *Codelfa* as to how ambiguity might be identified in the contract itself and whether the court will consider surrounding circumstances to identify ambiguity [49, 110, 111]. However, the High Court did not answer its own question, as the need to did not arise on the facts of the case.

36. In the light of the uncertainty surrounding the status of *Codelfa* differing views have been taken by intermediate appellate courts as to the need to apply the ambiguity gateway. In New South Wales, there is now a well-established line of authority which holds that it is not necessary to point to ‘ambiguity’ before having recourse to evidence of ‘surrounding circumstances’.

a. In *Franklins v Metcash* [2009] NSWCA 407 Campbell JA held that ambiguity was not a necessary requirement before recourse could be had to extrinsic evidence.

b. In *Mainteck Services Pty Ltd v Stein Heurtey SA ('Mainteck')* [2014] NSWCA 184, Leeming JA explained the difficulties of applying an ambiguity threshold, observing that "whether contractual language has a 'plain meaning' is (a) a conclusion and (b) a conclusion which cannot be reached until one has had regard to the context" [79]. He also held that *Woodside* was authority that the surrounding circumstances "require consideration".

c. Similarly, in *Cherry v Steele-Park* [2017] NSWCA 295, Leeming JA reviewed the relevant authorities and concluded that "[t]here is now a deal of authority for the proposition that whether there is in truth a constructional choice available to a written contract cannot be determined without first at least considering evidence of surrounding circumstances" [76].

37. Courts in other states have taken a more cautious approach. The courts of Western Australia, for example, continue to subscribe to an 'ambiguity gateway'. In *Technomin Australia Pty Ltd v Xstrata Nickel Australasia Operations Pty Ltd* [2014] WASCA 164, McLure J explained: "after careful consideration of multiple High Court decisions on the subject, a number of intermediate appellate courts in this country came to the view that evidence of surrounding circumstances was always admissible to assist in the construction of a contract, whether or not the contractual language was ambiguous or susceptible of more than one meaning. However… This court has taken the view that the guidance in *Western Export Services* should be followed until further direction from the High Court" [34-35].

38. Although *Codelfa* remains the law, there would therefore appear to have been a retreat from a strict application of the ambiguity threshold. Either it is not applied at all, or it is not applied to the question of whether there is ambiguity, or it is found that it is not necessary to apply it as there is ambiguity. Indeed, if the meaning of a contract term is to be litigated most skilled practitioners will be able to unearth ambiguity or more than one possible meaning.

39. Even where the ambiguity gateway is applied, its effect may be limited. This is because *Mount Bruce* recognises that recourse to "events, circumstances and things external to the contract…may be necessary in identifying the commercial purpose or objects of the contract where that task is facilitated by an understanding "of the genesis of the transaction, the background, the context [and] the market in which parties are operating" [49]. Relatedly, a court is also entitled to approach the task of interpreting a commercial contract "on the assumption "that the parties intended to produce a commercial result"" [51]. The court is therefore entitled to access a fairly expansive set of material to guide it in its interpretative task even if regard cannot be had to wider surrounding circumstances.

40. It follows that even in those courts where the ambiguity threshold is applied, there are going to be many cases in which regard can be had to surrounding circumstances because there is ambiguity and, even where they cannot be, many of the factors which a UK court would take into account can also be considered by the Australian courts. The result is that, despite their very different starting points, subsequent

developments indicate that the position in our two jurisdictions may not be very far apart.

Conclusion:

41. In practice the English 'purist' approach is not as expansive as might be thought since there will be many cases in which the wider context is not considered to be of great importance. Conversely, in practice the Australian 'pragmatic' approach is not as limiting as might be thought as there will be many cases in which regard can be had to some, if not all, relevant surrounding circumstances.

42. Whilst the purist approach may be said to be the more principled, the pragmatic approach reflects legitimate concerns to limit the time, cost and complexity of evidential inquiry relating to issues of contract interpretation.

43. An ambiguity threshold may, however, be said to be a blunt instrument for addressing such concerns. An alternative and more flexible way of doing so is through the use of effective case management.

44. The English Commercial Court found that many of Saville LJ's predictions as to the cost and time of litigating issues of contractual interpretation were borne out by practical experience. In particular, it was common to have extensive disclosure and questioning at trial addressed to factual matrix matters that ultimately were of little assistance to the court. To redress this, strict pleading requirements were introduced

if factual matrix matters were to be relied upon. The Commercial Court Guide states as follows:

> "(h) 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 set out in its statement of case 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".

45. By requiring careful thought to be given to the specific relevance of the factual matrix, if any, at an early stage of proceedings this provision has been found significantly to reduce disclosure and trial evidence relating to background knowledge. Too often the approach of parties was to throw everything in and then see what came out at the end of trial. This is no longer possible.

46. A similar approach has been adopted in Singapore[8] and also in Scotland. As Lord Hodge observed in *Arnold v Britton* (para 74), there is much to be said for the practice there "of requiring parties to give notice in their written pleadings both of the nature of the surrounding circumstances on which they rely and of their assertions as to the effect of those facts on the construction of the disputed words".

[8] See the judgment by Menon CJ in *Sembcorp Marine Ltd v PPL Holdings Pte Ltd* [2013] 4 SLR 1029 at paras 114-124

47. Pleading requirements such as these, which have proved very successful in practice, offer another way of controlling the evidence to be adduced on matters of interpretation. They offer a means of marrying purism and pragmatism. In appropriate cases the purist approach can be adopted, but in many cases a more pragmatic approach is likely to result. Rigour leads to realism.

48. Building on the experience of the English and other courts, adopting similar case management procedures could be considered by the courts here not only as a possible alternative to the ambiguity threshold but as a desirable means of pragmatic control in all cases.

49. In conclusion, the contractual interpretation journey of both the English courts and the Australian courts over the last thirty years has involved various twists and turns but they seem now to have arrived at a largely similar destination post. In England the road ahead after *Wood v Capita* appears to reasonably straight and settled. In Australia the status of *Codelfa* remains an issue but perhaps more in theory than in practice. As in so many areas of the law, we can each learn and benefit from each other's experience.