

Oxwich Park: stepping back from the brink – contractual interpretation after *Arnold v Britton*

by Simon Duncan

BACKGROUND

The courts have moved away from a literalist approach of contractual interpretation in recent years. There is greater emphasis on the commercial context of the contract concerned and protagonists can expect the court to adopt a more purposive view of any particular clause in their contract.

Lord Hoffmann set out the key principles of this new approach in *Investors Compensation Scheme Limited v West Bromwich Building Society* [1998] 1 WLR 896, at pages 912-13:

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 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...*
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 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...

5. *The rule that words should be given their ‘natural and ordinary meaning’ reflects the common sense 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 Hoffmann developed these principles further in *Chartbrook Limited v Persimmon Homes Limited* [2009] AC 1101 where he said, citing the *Investors Compensation Scheme* case amongst others:

What is clear from these cases 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 (para 25).

This theme was later endorsed by Lord Clarke in *Rainy Sky SA v Kookmin Bank* [2011] 1 WLR 2900 where he said (endorsing a comment of Lord Steyn writing extra-judicially in (1997) 113 LQR 433 at 441):

Commercially minded judges would regard the commercial purpose of the contract as more important than niceties of language. And, in the event of doubt, the working assumption will be that a fair construction best matches the reasonable expectations of the parties (para 25).

ARNOLD V BRITTON

The facts of *Arnold v Britton* [2015] UKSC 36 were as follows. Oxwich Leisure Park is on the Gower Peninsula. It contains 91 chalets which overlook the sea on the south Gower coast. Each of the chalets is let on a lease of 99 years from December 25, 1974. The leases contained a service charge provision requiring the lessee:

Clause 3(2) – *To pay to the Lessor without any deductions in addition to the said rent as a proportionate part of the expenses and outgoings incurred by the Lessor in the repair maintenance renewal of the facilities of the Estate and the provision of services hereinafter set out the yearly sum of Ninety Pounds and Value Added Tax (if any) for the first year of the term hereby granted increasing thereafter by Ten pounds per hundred for each subsequent year or part thereof.*

The lessor contended therefore that she was entitled to a fixed annual charge of £90 for the first year of the term, increasing each subsequent year by 10 per cent on a compound basis. To put this into perspective, in 2072 the lessee would be liable to pay a service charge of £1,025,004.00 to cover his/her share of the costs incurred by the lessor of providing a refuse collection service, grass cutting etc on the park.

Perhaps unsurprisingly, the appellants (the current chalet tenants) contended that such a construction resulted in an increasingly absurdly high annual service charge. That could not be right. They considered that their liability be limited to a fair proportion of the lessor's costs of providing the services, subject to a maximum, of £90, increasing each year by 10 per cent compound. In effect the words "up to" should be read into the clause between the words "hereinafter set out" and "the yearly sum."

For various reasons, the tenants could not avail themselves of any of the statutory provisions that might otherwise have given them a remedy. The appellants had succeeded at first instance, but they had failed in both the High Court and the Court of Appeal.

The Supreme Court decision

By a majority the Supreme Court (Lords Neuberger, Sumption, Hughes and Hodge) dismissed the appeal. Lord Neuberger gave the leading speech, and he began by setting out the key principles of interpretation:

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 (at paragraph 14). And it does so by focussing on the meaning of the relevant words, in this case

clause 3(2) ... in their documentary, factual and commercial context. The 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 or 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 (para 15).*

Furthermore, and seemingly rowing back against the dicta of Lord Hoffmann in *Chartbrook* alluding to unlimited quantities of red ink, he added:

... 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, the 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 (para 17).

... 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... (para 19).

Applying this approach, the majority preferred the lessor's interpretation and the appeal was dismissed.

The leases had been entered into at a time when inflation was high and effectively reducing the value of money. At that time, if inflation was running at 10 per cent, it was risky for both the lessor and lessee, under a contract to last 90 years, to agree a fixed sum that was only to increase by 10 per cent a year. Higher than 10 per cent the lessees benefit, lower (as it has been since 1983) the lessor benefits, but hindsight should not be applied.

Lord Carnwath's speech

Lord Carnwath considered that the impugned clause could not be interpreted to mean that the lessor was to receive a proportionate amount of the sums expended in maintaining the common areas of the park, whilst at the same time granting the Lessor an escalating sum that could be out of all proportion to this sum.

He pointed out that the court had had to fix the terms of

a new business lease before in an era of high inflation and this was done where there were nine units by requiring the tenant to pay one-ninth of the cost of providing the services under the covenant in addition to the rent payable under the lease (see *Hyams v Titan Properties* (1972) 24 P & CR 359 and para 130).

Accordingly, he reached the conclusion that:

The limited addition proposed by the Lessees does not do so much violence to the contractual language as to justify a result which is commercial nonsense (para 158).

Practical issues

The majority decision was less damaging to the lessees than one might imagine. As matters then stood, their options would appear to have been that they either surrender the leases, something which would have required the consent of the lessor. Alternatively, the lessees could have defaulted on the service charge and the lessor could have exercised a right of forfeiture and then pursued the former lessee for the arrears. This would have been an unsatisfactory state of affairs for either party. Perhaps in view of this, the lessor informed the court that should the lessees' appeal fail, it was intended that the service charge provision be renegotiated for "pragmatic" reasons.

It seems to the author this knowledge may have emboldened

their Lordships to take a less purposive view of the service charge provision. That said, this more restrictive approach had been heralded in *Marley v Rawlings* [2014] UKSC 2. Lord Neuberger gave the leading speech in that case too in January 2014.

Referring to Lord Hoffmann's speech in *Investors Compensation Scheme* he expressed the view that some of the language employed 'may be a little extravagant.' He also said that Lord Hoffmann's comments about there being no limit to the amount of red ink which the court is allowed (in *Chartbrook*) had led to academic debate to the effect that Lord Hoffmann had departed from established legal principles in making these observations (paras 36 to 40).

Accordingly, *Arnold v Britton* was probably the first suitable case to reach the Supreme Court since *Marley v Rawlings* which afforded Lord Neuberger the opportunity to reaffirm the principles of interpretation free of any of Lord Hoffmann's "extravagance." As a result the scope for the lower courts to apply a purposive interpretation to contractual clauses must now be reduced.

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