Implying terms in law

IMPLYING TERMS IN LAW: *BELIZE* NO MORE?

On its face, *Marks & Spencer Plc v BNP Paribas Securities Services Trust Company (Jersey)) Ltd.* ("M&S")[1] is a decision of the Supreme Court that addresses a narrow point of law. In particular, the matter for resolution was whether a tenant was entitled to a partial rebate of an advance payment of the final quarter's rent where it had terminated a commercial lease early in terms of a break option. However, M&S is of much broader significance. It signposts the way forward for the emergence of future jurisprudence in a crucial area of contract law, namely the law to be applied in respect of the implication of terms. By compelling the Supreme Court to address the relationship between the contractual rules regulating the interpretation of express terms and the implication of terms, it afforded the Justices in that court their first opportunity to express a view on the approach adopted by Lord Hoffmann in the decision of the Judicial Committee of the Privy Council in *Attorney-General of Belize v Belize Telecom* ("Belize").[2]

THE FACTS AND THE DECISION

BNP Paribas as landlords entered into four commercial leases with Marks & Spencer in respect of the latter's occupation of various floors of a building in Paddington basin in London. The leases contained a break clause, empowering Marks & Spencer to bring the leases to a premature end by paying a premium equivalent to one year's rent and providing at least six months' prior written notice of its intention to break. In accordance with standard practice, the lease stipulated that the rent each quarter was payable in advance. When the tenant exercised its right to break, it sought to recover part of the rent it had paid in advance to the landlord in respect of the final quarter period, i.e. the portion of the rent attributable to the period from the date of termination to the end of the final quarter. One of the techniques it adopted to try and meet that objective was to rely on the law on the implication of terms. In a unanimous decision, the Supreme Court rejected the tenant's arguments on a number of grounds. As far as the implication point goes, the Supreme Court opined that although it might be necessary in terms of business efficacy for a term to be implied that the tenant receive a partial rebate of the rent paid in advance, there was little force in the contention that it was necessary to make the contract work, or to deprive of it of absurdity. For that reason, the tenant's appeal was

[1] [2015] UKSC 72; [2015] 3 WLR 1843.
[2] [2009] UKPC 10; [2009] 1 WLR 1988.

unsuccessful. Whilst the outcome was perhaps unsurprising, what was particularly noteworthy was the degree to which the Justices of the Supreme Court differed in their respective opinions on the approach adopted by Lord Hoffmann in Belize.

B. THE IMPACT OF M&S ON BELIZE

In Belize, Lord Hoffmann delivered the unanimous judgment of the Judicial Committee of the Privy Council. The case concerned the implication of a term in fact, and Lord Hoffmann's judgment has been treated as a characteristic attempt to recalibrate the rules applicable in a particular area of contract law.[3] For example, departing from orthodoxy, his Lordship asserted that the process of implication of a proposed term involved asking 'whether such a provision would spell out in express words what the instrument, reading against the relevant background, would reasonably understood to mean.'[4] By approaching the law of implication in that way, Lord Hoffmann did two things. First, he explicitly relegated the importance of the familiar 'necessary to give business efficacy'[5] and the 'officious bystander… so obvious that it goes without saying'[6] tests, articulating the point that these prescriptions tended to confuse rather than illuminate. His Lordship was concerned that these tests had been permitted to take on a life of their own, which obscured the true purpose of the exercise of the implication of terms. This leads us on to the second proposition adopted by Lord Hoffmann, namely that the 'implication of a term is an exercise in the construction of the instrument as a whole',[7] i.e. simply another means of interpreting a contract. This served to situate the doctrine of implied terms firmly within the principles of contractual interpretation and edged domestic law somewhat closer to the position in German law, where the process of 'supplementary' or 'constructive' interpretation is applied to fill a gap in a contract.[8] Whilst this approach may indeed be valid if a broad interpretation is afforded to the concept of 'construction', it jars to

[3] See the discussion in J. McCaughran, 'Implied Terms: the journey of the man on the Clapham omnibus' (2011) 70 *Cambridge Law Journal* 607 and Lord Grabiner, 'The Iterative Process of Contractual Interpretation' (2012) 129 *Law Quarterly Review* 41. For the reason that Lord Hoffmann departed from orthodox contract law, his recasting of the doctrine of implied terms has been criticised: P. Davies, 'Recent Developments in the Law of Implied Terms' (2010) *Lloyd's Maritime and Commercial Law Quarterly* 140. However, for an opposite view, see R. Hooley, 'Implied Terms After *Belize Telecom*' (2014) 73 *Cambridge Law Journal* 315.
[4] [2009] UKPC 10; [2009] 1 WLR 1988, 1994B-D.
[5] *The Moorcock* (1889) 14 PD 64, 68 per Bowen LJ and *Reigate v Union Manufacturing Co (Ramsbottom) Ltd* [1918] 1 KB 592, 605 per Scrutton LJ.
[6] *Shirlaw v Southern Foundries (1926) Ltd* [1939] 2 KB 206, 227 per MacKinnon LJ.
[7] [2009] UKPC 10; [2009] 1 WLR 1988, 1993F.
[8] H. Beale, B. Fauvarque-Cosson, J. Rutgers, D. Tallon and S. Vogenauer, *Cases, Materials and Text on Contract Law*, 2nd edn (Oxford, Hart Publishing, 2010) 749.

the extent that the law controlling the implication of terms in fact has generally been treated as an exercise in the addition of provisions into a contract *that are not there*, i.e. 'gap-filling'. This can be contrasted with the work that the law of interpretation has been traditionally considered to do, namely the ascertainment of the meaning of the express terms of the contract that are contained in the contract itself.

As such, Lord Hoffmann, took the view that the interpretation, addition, and interpolation of contractual provisions were all part and parcel of the exercise of construction, with the latter entailing an enquiry into what meaning the parties intended to convey, all in accordance with what a reasonable person would understand the contract to mean. It is this formulation which was addressed by the Supreme Court in M&S. In particular, delivering the main judgment of the Supreme Court, Lord Neuberger (with whom Lords Sumption and Hodge agreed) expressed scepticism about the proposition that the interpolation of words formed an integral component of the process of interpretation. Although Lord Neuberger accepted that implication involved the ascertainment of what the contracting parties must have intended to agree by their contract, as well as the scope of what they intended to cover, he opined that by casting implication as simply a part of the exercise of interpretation, Lord Hoffmann's formulation tended to 'obscure the fact that construing the words used and implying additional words are different processes governed by different rules… [and] when one is implying a term or a phrase, one is not construing words, as the words to be implied are ex hypothesi not there to be construed; and to speak of construing the contract as a whole, including the implied terms, is not helpful, not least because it begs the question as to what construction actually means in this context..'[9] By approaching matters in this way, Lord Neuberger reasserted the traditional division between the law of interpretation and implication, whilst implicitly acknowledging that broadly construed, the notion of 'construction' - in the sense of ascertaining what the parties intended to mean, or must have intended to mean - includes both of these exercises.[10] Furthermore, Lord Neuberger was clear that the interpretation of express terms and the implication of terms were sequential and separate stages in the 'construction' of a contract: the process of implication came naturally after the former process of interpretation and both exercises were thus mutually exclusive.[11]

[9] [2015] 3 WLR 1843, 1852G-1853A.
[10] This is reflective of the discussion on the distinction between the 'construction' and 'interpretation' of a contract in W. W. McBryde, *The Law of Contract in Scotland*, 3rd edn. (Edinburgh, W Green, 2007), para. 8-05. Lords Carnwath and Clarke agreed with Lord Neuberger on this point: [2015] 3 WLR 1843, 1864C-D and 1865G-1866A.
[11] [2015] 3 WLR 1843, 1852H-1853D.

A potential consequence of the setting aside of the well-known 'business efficacy' and 'officious bystander'[12] tests in Belize was that Lord Hoffmann had removed the oft-versed formulation that the implication of the proposed term must be necessary in order to make the contract workable. By referring to the 'reasonable addressee',[13] Lord Hoffmann could be taken to have diluted the traditional strong test of necessity.[14] For example, one might argue that entrusting the enquiry to the reasonable reader would equate to a duty to consider whether the proposed term was reasonable, rather than necessary. However, Lord Neuberger was not convinced and ruled that Lord Hoffmann had not sought to loosen the strict test of necessity. As such, it continued to be essential that the proposed term must 'be so obvious as to go without saying or to be necessary for business efficacy.'[15] Likewise, Lords Carnwath and Clarke agreed with Lord Neuberger.[16] However, where Lords Neuberger and Carnwath parted company was on what exactly Lord Hoffmann had had in mind when he claimed that implication was part and parcel of construction. For example, Lord Carnwath was not convinced by Lord Neuberger's understanding of interpretation and implication as mutually exclusive processes that operated consecutively. Instead, he preferred to view them as forming part of a wider, *iterative* process of construction.[17] Whilst this may seem like a distinction without practical substance, it is suggested that it will assume importance where a party raises proceedings to have the courts interpolate words into a contract: Lord Neuberger would appear to have curtailed the scope for interpolation to be eligible where a claim is rooted in the law of contractual interpretation, whereas Lord Carnwath's formulation leaves open that possibility.

C. CONCLUSION

Although Belize was a decision of the Judicial Committee of the Privy Council and was strictly, not binding, by the time that the Court of Appeal came to consider it in *Mediterranean Salvage & Towage Ltd. v Seamar Trading & Commerce Inc.*,[18] Lord Clarke MR had anticipated that Lord Hoffmann's 'analysis will soon be as much referred to as his approach to the construction of contracts in *Investors Compensation Scheme Ltd v West Bromwich Building Society*

[12] *Shirlaw v Southern Foundries (1926) Ltd* [1939] 2 KB 206, 227 per MacKinnon LJ.
[13] [2009] 1 WLR 1988, 1993D.
[14] See the discussion in C. Peters, 'The Implication of Terms in Fact' (2010) 68 *Cambridge Law Journal* 513, 514.
[15] [2015] 3 WLR 1843, 1851F.
[16] [2015] 3 WLR 1843, 1861E, 1863C and 1866A-C.
[17] [2015] 3 WLR 1843, 1864F-H. See also Lord Grabiner, 'The Iterative Process of Contractual Interpretation' (2012) 129 *Law Quarterly Review* 41.
[18] [2010] 1 All ER (Comm) 1.

[("ICS")][19]...'[20] However, as this note has demonstrated, the outcome of the M&S adjudication has been the opposite of what Lord Clarke predicted, that is to say, the marginalisation of the authority of Lord Hoffmann's conceptualisation of the proper rules to be applied in the context of the implication of terms. Notwithstanding Lord Carnwath's spirited defence of Lord Hoffmann's formulation in Belize, what stands out from M&S – and is likely to be the most telling intervention – is Lord Neuberger's memorable statement that 'the right course for us to take is to say that [Lord Hoffmann's] observations [in Belize] should henceforth be treated as a characteristically inspired discussion rather than authoritative guidance on the law of implied terms.'[21] Alongside *Arnold v Britton*[22] which heralded the downgrading of the status of the 'business common sense' and 'commercially sensible construction' test embraced by Lord Hoffmann in ICS, M&S marks something of a reining in by Lord Neuberger of the towering legacy that Lord Hoffmann had sought to bequeath to domestic contract law.

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[19] [1998] 1 WLR 896. Writer's annotations are shown in square brackets.
[20] [2010] 1 All ER (Comm) 1, 5b-c.
[21] 1853H.
[22] [2015] UKSC 36, [2015] 2 WLR 1593. For commentary, see R. C. Connal QC, Has the Rainy Sky Dried Up? *Arnold v Britton* and Commercial Interpretation' (2016) 20 *Edinburgh Law Review* 71.