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CONSTRUCTION OF COMMERCIAL CONTRACTS AND PAROL EVIDENCE

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This article argues that theories of interpretation and pragmatics offer solid proof that the rule-based model of construction is flawed and that the judicial shift to commercial interpretation is correct. One insight gained by analysing in the light of these theories what the courts in fact do when they construe commercial contracts is the impossibility of limiting the context to any given set of data, since the contextual-dependence of sentences is both the generator and resolver of any set of interpretative hypotheses. Other valuable insights are that a principle of rationality is necessarily presupposed in any institutionalised interactive goal-oriented communication and that the principle of instrumental rationality necessarily presupposed in the making of a contract is that the assignment of meaning shall accord with the commercial purposes of the contract.

I. RULES OF CONSTRUCTION

More than half a century ago, Lord Devlin likened the lawyer's reliance on rules of construction[1] to the conduct of a post mortem examination. He said this:

> If all lawyers were made doctors overnight, they would flock to the dissecting rooms, for I am sure that they would prefer corpses to live patients. The lawyer starts, for example, by telling himself that he construes contracts so as to ascertain the intentions of the parties; but before long he has invented canons of construction and other rules which make things easier for himself but much more difficult for the parties who do not know the rules.[2]

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1 Some prefer the terminology of interpretation, saying that the courts must ascertain the meaning of the language of the contract. I have chosen the terminology of construction to reflect the thesis of this article, namely that the courts in ascertaining the meaning must apply a principle of instrumental rationality so that construction involves the process of interpretation and the application of an objective principle. But the courts use the terms, interpretation and construction, interchangeably. See *Investors Compensation Scheme Ltd. v. West Bromwich Building Society* [1998] 1 All E.R. 98 at 114-115 (H.L.). See also *Don King Productions Ltd. v. Warren* [1998] 2 Lloyd's Rep. 176 at 188-189 (Ch.). Lord Steyn in *Equitable Life Assurance Society v. Hyman* [2002] 1 A.C. 408 at 458-459 (H.L.) uses the term construction to cover interpretation and implication of terms (in fact). Whether implication in fact is "entirely constructional in nature" is not discussed in this article.

2 Patrick Devlin, "The Relation Between Commercial Law and Commercial Practice" (1951) 14 M.L.R. 249 at 251-252.

The penchant for post mortem analysis, apparently, has not changed and may have escalated. The proof of it is ready at hand in the kind of contractual documents which emanate from the lawyer, As he construes, so the lawyer drafts a contract. His searching blade continues to incline him to an excessively defensive posture when he comes to draft commercial contracts. He feels the need to leave no stone unturned. Convinced that he cannot do less for his client, he will ensure that his draft will not be short on length and prescription. The result—his contract looks like a treatise on the law of contracts.

This predilection for details seems, at first, hard to understand. Would not a draftsman drafting a commercial contract adopt a more minimalist draft, drawing heavily on custom or usage? But although regrettable, the impact of custom is far less than one might think. In a less sedate commercial world, changes may happen too swiftly for a custom as stringently defined by the law to develop.[3] At best, there is a practice or usage which the law ignores when it is not known or would not reasonably be known to both parties and in any case it is likely to change perhaps just when it might otherwise have attained the status of a custom. Moreover, it changes incrementally because the pace of innovation though powerful is largely incremental and adaptive. The result is that its manifestations are seen more in the details, and less in the heads of agreement, and the details become more or as important in defining the shape and complexion of the contract.

The fact is that lawyers have left their marks on the way business people make contracts;[4] and the rules of construction they have helped to develop now form part of the commercial matrix.[5] For some, the process of construing the written contract devised under these circumstances and underscored by a strong enduring belief in party autonomy can only be rule-based.[6] There is inevitably a tension between certainty,[7] which application of rules of construction promotes, and innovation, which party autonomy expresses; and the question for them is how to strike that happy balance between certainty and innovation? If this equilibrium were the only consideration in construction, not everyone would approve of giving rules of construction such a prominent role. The great certainty which rules achieve is often exaggerated. First, if the tendency to stipulate in detail is inevitable, the success of any rule of construction derived perhaps from some "average practice", paradoxically, is bound

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3 To qualify as custom, the usage must be notorious, generally accepted by those who do business in the trade or market concerned as having intrinsic binding force, reasonable and must not be repugnant to the particular relations which the parties have established between themselves. See *Chan Cheng Kum v. Wah Tat Bank* [1971] 1 M.L.J. 177 at 179 (P.C.).

4 See Diplock L.J. in *Sydall v. Castings Ltd.* [1967] 1 Q.B. 302 at 313-314 (EWCA Civ.).

5 As in *Lishman v. Christie* (1887) 19 Q.B.D. 333 (EWCA Civ.). See also *The Nifa* [1892] P. 411 (Div. Ct.). Lord Devlin blamed the lawyer's written contract for killing custom, but perhaps the courts must share the responsibility for setting too high a standard for the admissibility of custom, refusing to let custom prevail over the written word. Whether the courts killed the custom is a matter of nice conjecture but the fact is that in the organised trades, the written contract has killed or virtually killed the role of custom; there are few businessmen who today can safely rely on custom. *Cf. Cory Bros. v. Baldan* [1997] 2 Lloyd's Rep. 58 (Q.B.) where the court found that there was a custom that London freight forwarders were personally liable for the freight even though they were known to be acting as agents only.

6 In the application sense so that construction depends on applying rules of construction.

7 Described as the great object in all mercantile transactions. See *Vallejo v. Wheeler* (1774) 1 Cowp. 143 at 153 (K.B.) and *The Starsin* [2004] 1 A.C. 715 (H.L.) at para. 13 [*Starsin*].

to be ephemeral or short lived. Second, the justification for elevating a rule of construction to such prominence has never really been put on a solid footing. Further, the rules would self-perpetuate. In the long run, the rules pile up. Disputes about the construction of a contract are more or as likely than other contractual disputes to end up in the highest court for an irrefutable decision. The resultant rule will be noticed and will provoke a response: there will be reliance on it or drafting around it. Thus, the complexity propagates at the expense of the certainty rules are said to promote.

There are more fundamental considerations casting doubts on a rule-based model of construction which this article examines. A rule-based model is touted as an effective and efficient safeguard of party intention besides promoting certainty but is that truly the goal of construction when the making of a contract necessarily involves the interactive and purposive use of language, when the language of a contract is far from the language of judgment, or experience? Since a steady stream of House of Lords cases approved of the 'principle'[8] of commercial purposes,[9] the contract's commercial purpose has become an accepted element of the process of construction and is seen as vital to the use of language in making a contract. In this article, the terminology of principle of commercial purposes is used advisedly in contrast to the preferred terminology of contextual approach.[10] The need to relate the rules of construction to this principle supplies the further reason for a closer scrutiny of the rule-based model which is carried out in the first part of this article.[11]

A. *Criticisms of Rule-Based Construction*[12]

The hold of intention in contractual construction seems unshakeable and there are innumerable pronouncements that in construing a contract, there is only one pre-eminent goal, namely the ascertainment of the parties' intentions. To that end, "[i]n

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8 I use this word deliberately to reflect the thesis of this article and justify it in the conclusion.

9 *Charter Reinsurance Co. Ltd. v. Fagan* [1997] A.C. 313 [*Charter Reinsurance*]; *Mannai Investments Ltd. v. Eagle Building Society* [1997] A.C. 749 [*Mannai Investments*]; *Investors Compensation Scheme Ltd. v. West Bromwich Building Society* [1998] 1 W.L.R. 896 [*Investors Compensation Scheme*]; *Bank of Credit and Commercial International S.A. (in compulsory liq.) v. Ali* [2002] 1 A.C. 251 [*Bank of Credit*]; *Stars*in, *supra* note 7. For critiques, see P.V. Baker, "Reconstructing the Rules of Construction" (1998) 114 L.Q.R. 55; M. Clarke, "Construction of the Policy and the Policy of Construction" [1996] L.M.C.L.Q. 433; Sir Christopher Staughton, "How Do the Courts Interpret Commercial Contracts" [1999] C.L.J. 303; Gerard McMeel, "The Rise of Commercial Construction in Contract Law" [1998] L.M.C.L.Q. 382; Alan Berg, "Thrashing Through the Undergrowth" (2006) 122 L.Q.R. 354; James Jacob Spigelman, "From Text to Context: Contemporary Contractual Interpretation" (2007) 81 A.L.J. 322.

10 As in *Zurich Insurance (Singapore) Pte. Ltd. v. B-Gold Interior Design & Construction Pte. Ltd.* [2008] 3 S.L.R. 1029 (C.A.) [*Zurich Insurance*]. Lord Steyn in *Mannai Investments*, *supra* note 9 at 770 prefers the terminology of the principle of commercial construction.

11 It is acknowledged that some of the observations critical of the rule-based model have been made before; in some cases, as early as the 1940s. See Karl Llewellyn "Remarks on the Theory of Appellate Decision and the Rules or Canons about How Statutes are to be Construed" (1949-50) 3 Vand. L. Rev. 395 at 401. What has not been done is to examine the rule-based model in the light of theories of meaning. Part I of this article thus has a specialised focus.

12 Gerard McMeel, *The Construction of Contracts etc* (Oxford: Oxford University Press, 2007) 17 [*The Construction of Contracts*] calls this the traditional or literalist approach.

seeking to construe a clause in a contract there is no scope for adopting either a liberal or narrow approach, whatever that may mean. The exercise which has to be undertaken is to determine what the words used mean. It can happen that in doing so one is driven to the conclusion that that clause is ambiguous, that it has two possible meanings. In those circumstances the Court has to prefer one above the other in accordance with settled principles."[13] This is but one of many similar remarks which continue to be made or cited alongside the newly minted principle of commercial purposes. Typically, the giving effect to the intentions of the parties is stated first and somewhere down the line of propositions, it is also stated that the construction to be applied cannot frustrate the reasonable expectations of businessmen.[14] In this first part of the article, the central argument is essentially negative: that an intention-based paradigm reflective of a strong theory of meaning and implemented by a rule-based model, which sees construction as primarily directed at resolving ambiguous language, is flawed.

If the search for communicative intention was what construction was all about, there would be little doubt that the 'intention and rule'-based model was correct or appropriate. According to Grice, for whom the meaning of any sentence lies in the recognition of the communicative intention of the speaker (or writer), there may be a separation between the speaker's intention to produce an effect in the interlocutor's mind and meaning (*i.e.*, recognition of the intention in the interlocutor's mind).[15] This is because the interlocutor relies on conventions or conversational maxims (which identify the syntactic and semantic properties of the speaker's utterance) when interpreting the speaker's language. The speaker of course does likewise when expressing his intention. The reliance on conventions in assigning meaning implies that a speaker may not hold the belief "p" but may successfully employ the conventions to convey that "p". This is the problem of implicature or indirect meaning in which communication breaks-down when the speaker deliberately or ostensively violates the conversational maxims whilst employing them.[16] One further implication is this. The detection of reliance on conventions and possibilities of 'detachment' on the part of the speaker requires application of the rules of conventions, making application of rules of construction inevitable under an intention-based theory of meaning.[17]

On the other hand, a person may mean what he says or say what he means but his interlocutor understands him to say and mean a different thing because the speaker is ignorant of the conversational maxims or makes an error when employing the maxims. The truth and falsity of his holding the intention which his interlocutor recognises must be ascertained by scrutinising his utterance (the datum) for consistency and sincerity. Importantly, the deviation between intention and meaning under these conditions is causal rather than intentional. It is not an implicature and thus, no amount of interpretation will eliminate it. The problem is one of datum; and if

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13 *Ashville Investments Ltd v. Elmer Contractors Ltd.* [1989] 1 Q.B. 488 at 494 (EWCA Civ.).

14 See Lord Bingham of Cornhill in *Starsin*, *supra* note 7 at para. 12.

15 Herbert Paul Grice, "Meaning" (1957) 66 Philosophical Review 377.

16 A word or statement is ambiguous "when it has two (or more) primary meanings, each of [which may] be adopted without distortion of the language". See Kim Lewison, *The Interpretation of Contracts*, 4th ed. (London: Sweet & Maxwell, 2007) 299.

17 See also David Lewis, *Convention: A Philosophical Study* (Cambridge: Massachusetts Harvard University Press, 1969) who argues that meaning is a consequence of conventional signaling.

there is to be any restriction of the evidence to ensure that the ascription of truth and falsity can be undertaken effectively, only the datum will be affected.

According to the strong theory of meaning then, construction involves two distinct phases and an orderly progression, beginning with the determination of the objective datum (which ensures that the speaker is not rule-ignorant or making an error in employing the conventions which are matters of causality) and going on to interpretation or the assigning of meaning through application of the conventional rules (which includes resolving the problem of implicatures). As a result of this operation of the rules of convention on the datum the meaning emerges.

The 'intention and rule'-based model which is derived from such a theory may be criticised because it does not match what the courts are nowadays doing when they interpret a contract. We know something is wrong when whilst assuming an intention-based paradigm and hence adopting a rule-based model, the courts have not faithfully maintained it. They have added an important qualification, namely that the intention is not the subjective intention of either party but the common intention, realistically and objectively understood. In the words of Lord Wilberforce:

> When one speaks of the intention of the parties to the contract one speaks objectively—the parties cannot themselves give direct evidence of what their intention was—and 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.[18]

Putting it in the way that he does, Lord Wilberforce affirms that the objective common intention of reasonable people in the parties' positions is the primary concern of the court of construction.[19]

The first criticism then is that under the qualification which the courts have introduced, and whether this is realised or not, there is a significant departure from the strong theory of meaning underpinning the rule-based model. The qualification embraces another theory, which may be described as a 'prediction and control' theory. 'Prediction and control' theorists argue that theories of meaning in the strong sense (which posit a subjective intention matched by a subjective mental state, recognition of the intention) have slight lessons for the court of construction because "[t]he language of contract is directed not at describing experiences but at controlling human behaviour, ordinarily the behaviour of the contracting parties. The concern of the court is not with the truth of this language but with the expectations that it aroused in

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[18] *Reardon-Smith Line Ltd. v. Yngvar Hansen-Tangen* [1976] 1 W.L.R. 989 at 996 (H.L.). See also Lord Reid in *McCutcheon v. David MacBrayne Ltd.* [1964] 1 W.L.R. 125 (H.L.). *Cf. Magenta Resources (S) Pte. Ltd. v. China Resources (S) Pte. Ltd.* [1996] 3 S.L.R. 62 at 79 (H.C.):

> In the interpretation of a contract the court is seeking to ascertain what the true agreement of the parties as expressed in the contract is. In so doing, the court is entitled to look at the factual matrix in which the contract was concluded and is entitled to *take into account each party's view as to what the words of the contract was intended to mean*.

(The italicised portion seems incorrect.)

[19] This incidentally is not the same as asking about the intention as it would appear to reasonable people hearing the expressions, explicit or implicit, of intention. If so, we would be interested only in the expectations of the interlocutor, which is denied. *Cf.* Lord Diplock in *The Nema* [1982] A.C. 724 at 736 (H.L.) [*The Nema*] who refers to the mutual intentions. *Cf.* also Lord Hoffmann, "The Intolerable Wrestle with Words and Meaning" (1998) 56 S.A.L.J. 656 at 660-661.

the parties."[20] The purpose of construction then is to discover the common expectations of the parties as to the nature and extent of their desired level of prediction and control. The application of rules of convention is inadequate for these purposes. One reason is that it predicates that the speaker and his interlocutor wish to cooperate in the ascertainment of the speaker's meaning, a predicate which Grice termed the principle of cooperation. This cooperative condition which provides the *raison d'etre* for the application of the rules of convention is questionable where the parties are at least mildly antagonistic.

The chief reason however is that rules of convention are inappropriate for ascertaining the objective intention (which stands for the common expectations aroused by the language of the parties) on account of an added dimension when language is used not so much to convey meaning as pragmatically so as to convey their purpose in achieving a desired state or condition and in eliciting conduct directed at such a state or condition. The use of conventions itself becomes pragmatic; it may serve to cajole, coax, induce and lead, or divert or concentrate attention. The speaker no longer seeks to ensure that his meaning remains immutable by focusing on core contents or meaning. What he seeks to do is rather to create an effect or induce or arouse a state of action or inaction; if necessary he will rely on a penumbral sense. When rules of convention are to create predictable kinds of behaviour or controlled conduct, they cease to be immutable in meaning even in the Gricean sense. This point can be expressed in terms of the terminology of hard, soft and fuzzy language. Hard language has immutable meaning because a speaker intends to communicate a certain meaning which the interlocutor recognises. In formal terms, a hard language is a language in which for every "x", it is true that either "x" belongs to A or that it is not the case that x belongs to A. A soft language is the negation of the hard language. It is not true that either "x" belongs to A or that it is the case that "x" does not belong to A. A fuzzy language has features of both the hard and the soft. There are instances of "x" for which it is true that either "x" belongs to A or that it is not the case that "x" belongs to A. There are also instances of "x" for which this is not true. The contracting party seeking to induce a state of predictable control is unlikely to be using a hard language all the time but is likely to be using fuzzy language some of the time. When the interpreter applies an 'intention and rule'-based model, which assumes that the contracting party is using a hard language, he must go terribly wrong at least sometimes.

A second criticism of the rule-based model follows from the first. With the shift from intention to common expectations the interpretative process necessarily alters. It necessarily enlarges. Again, it can be seen that the courts pay lip service to the predicates of the rule-based model when they assume an enlarged role in interpreting the contract. Under the strong theory of meaning earlier outlined, two types of ambiguity may be identified. By definition the holding of an intention requires an exclusive selection among possible mental states and as corollary the possibility of alternative intentions is denied. Vague intentions therefore cannot be construed because they are impossible in conception and thus meaningless in expression even when the conventional rules are observed. To attribute meaning to vague intentions

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[20] Edward Allan Farnsworth, *Contracts*, 2d ed. (Boston: Wolters Kluwer Law & Business, 1990) para. 7.7. See also Edward Allan Farnsworth "'Meaning' in the Law of Contract" (1967) 76 Yale L.J. 939 [*Meaning*].

would be to make a contract for the parties, not to construe the contract they have made. This first kind of ambiguity arising out of vague express intentions may be designated as patent ambiguity.[21] The second kind may be designated as hidden (latent) ambiguity because the speaker has not intended to communicate the direct meaning of his words but another indirect meaning. The reason that the interpretative process is of limited scope under the strong theory is that it identifies merely two cases of latent ambiguity or incompleteness; one, where the speaker decides consciously not to observe the rules of convention and two, where the speaker consciously rejects them, whilst employing them. All other cases are not true cases of interpretation. As has been mentioned, the text or discourse of a rule-ignorant speaker or the speaker who makes an error as to the rules of convention does not call for interpretation but for causal proof of the ignorance or the error. There is no ambiguity in his text or discourse once the causal explanation of the utterance has been exposed as part of the determination of the datum.[22]

Consistently with the strong theory, the *Evidence Act*[23] distinguishes between patent ambiguity and latent ambiguity. Section 95 dealing with patent ambiguity, says that when the language used in a document is on its face ambiguous or defective, evidence may not be given of facts which would show its meaning or supply its defects. This is illustrated by the example of a contract to sell light sandals—does this mean light-coloured sandals or sandals of light weight? The same expression bears two entirely different connotations and thus we say it is (patently) ambiguous and the Act says extrinsic evidence is inadmissible to clarify which is the intended meaning. Then the Act goes on to identify three categories of latent ambiguity. One is ambiguity in reference to the existing facts, though the language is plain in itself: see section 97. The second is ambiguity in relation to persons or things included within an obligation: see section 98. The third is ambiguity arising from partial applicability (an equivocation): see section 99. In all three categories, the principle is that without extrinsic evidence, the ambiguity lies undetected and that as extrinsic evidence is the means of its detection, extrinsic evidence is also the means of its dissolution.[24]

The case law, whether on the Act or otherwise,[25] indicates however that these formal definitions are generally ignored. In theory a patent ambiguity is self-declaratory. It reveals mutually exclusive intentions and hence no extrinsic evidence is necessary to reveal it, unlike a latent ambiguity, and no amount of extrinsic evidence can clear it. In the example given by the *Evidence Act* of a contract to sell light sandals, there

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21 *Cf.* Farnsworth, *Meaning*, *ibid.* at 951 who distinguishes between vagueness and ambiguity.

22 It is worthwhile pointing out that a strong theory of meaning does not warn us that the meaning of language is easily subverted by unrestricted inferences. Some writers and judges are found of saying that if the meaning to be ascertained by rules of convention is to be stable, there must be little scope for extrinsic evidence for the purposes of clarification by inferential reasoning. There is however no warrant for this, if we are true to the strong theory. Except when it is vague, the language bears only one meaning, the intended meaning. This singular meaning, fixed at the time of utterance and unalterable thereafter, the rules of convention will determine unless there is ostensive violation or rejection of the rules. Latent ambiguities (or partial applicability) are the result of ostensive violation or rejection of the rules, and create incomplete meanings or gaps that can be resolved by extrinsic evidence of ostensive violation or rejection of the rules.

23 Cap. 97, 1997 Rev. Ed. Sing. [*Evidence Act*]

24 See *Smith v. Thompson* (1849) 8 C.B. 44 per Maule J.

25 See *Bank of Credit*, *supra* note 9 at paras. 55-57.

is a patent ambiguity in the reference to light sandals because on its face the reference to light could be a reference to colour or weight, which are mutually exclusive descriptors. As the speaker holds mutually exclusive intentions, it is impossible for the interlocutor to recognise either the one or the other. The interlocutor recognises that there are mutually exclusive intentions if the speaker has correctly used the rules of convention. But if this example were taken seriously as illustrating the definition of patent ambiguity, there would be no end of patent ambiguities since so far as adjectives go, they frequently have at least two non overlapping and alternative connotations. Unable to accept the inexorable logic of the patent ambiguity, the courts in effect admit extrinsic evidence that the interlocutor in fact recognised only one meaning intended by the speaker or that a reasonable interlocutor would recognise only one of these meanings. If there is extrinsic evidence to show that one party understood the mutually exclusive meanings of the other to be either one or the other, or that the speaker actually meant one of the mutually exclusive meanings his language evoked, the ambiguity is regarded as latent not patent. Typically this is done by pronouncing the contract to be badly drafted which presupposes that this is not a case of vague intentions or patent ambiguity.[26] Immediately the door is open to admit contextual information to resolve the incompleteness in the text. To be faithful to the strong theory of meaning, the determination of mutually exclusive intentions must be purely facile and conventional. The courts however use the extrinsic evidence to determine whether there is a patent ambiguity and where the ambiguity can be resolved, it is not patent.[27] This approach cannot be defended on the strong theory of meaning but would make sense if the common expectations of the parties must be fostered.

Turning to the associated idea of the plain language, it is clear from the strong theory of meaning that the clarity or obscurity of the speaker's sentences is not a matter of interpretation. Consistently with the strong theory, section 96 says that when language used in a document is plain in itself and when it applies accurately to existing facts, evidence may not be given to show that it was not meant to apply to such facts. The purpose of extrinsic evidence showing the relationship between the language and existing facts is singularly to affirm that the meaning of the language is plain. Thus, like the patently ambiguous language, the determination of clarity does not depend on the interpretative process.[28] Like the patent ambiguity, the clarity of a text is absolute, not contextual. However, as with the patent ambiguity, the courts

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[26] See *Louis Dreyfus & Cie v. Parnaso* [1959] 1 Q.B. 498 at 512 reversed on other grounds in [1959] 2 Q.B. 49 (EWCA Civ.).

[27] Cf. Lord Bridge of Harwich in *Mitsui Construction Co. Ltd. v. A-G. of Hong Kong* (1986) 33 Build. L.R. 1 at 14 (P.C.) [*Mitsui Construction*]:

> [T]his is a badly drafted contract. This, of course, affords no reason to depart from the fundamental rule of construction of contractual documents that the intention of the parties must be ascertained from the language they have used, interpreted in the light of the relevant factual situation in which the contract was made.

[28] Especially, the commercial case: see *The Elpis* [1999] 1 Lloyd's Rep. 606 (H.C. Adm.) [*The Elpis*] where a letter of undertaking given to cargo owners was held to be clearly intended to cover all cargo owners, and not merely the plaintiffs, and this construction was then confirmed as consistent with the commercial purpose of the agreement and with common sense. See also *Zeus V* [1999] 1 Lloyd's Rep. 703 (H.C. Adm.) [*Zeus*]. For a case where it was said that there was no ambiguity, and no attempt to confirm it by examination of the commercial purpose, see *Kumagai-Zenecon Construction Pte. Ltd. v. Arab Bank plc.* [1997] 3 S.L.R. 770 (C.A.).

determine whether there is clarity in the plain meaning sense by reference to the 'untenable' result it would produce or by reference to the context.[29] As illustration of the second determination, the case of *Diversey (Far East) Pte. Ltd. v. Chai Chung Ching Chester*[30] may be cited. The parties were in dispute and the appellants had claimed as special damages (evident from the statement of claim) certain professional costs they had incurred in connection with the dispute. They eventually settled their claims under an agreement whereby they "unconditionally and irrevocably release[d] and discharge[d] the [respondents] … from any and all claims …" Both the High Court and the Court of Appeal held that the meaning of the term 'claims' was plain and that since, as the statement of claim showed, the appellants had made claims in respect of the professional costs which they had incurred, they had agreed to release and discharge the respondents from such claims. In other words, the decision that the meaning was clear depended on inferring from the fact that the appellants had made claims in respect of the professional costs which they had incurred that those costs were included in the terminology of claims.[31] As with the patent ambiguity, the courts consider contextual information ranging beyond what is strictly permissible under the strong theory. Clarity and patent ambiguity, alike, are become pragmatic (context-dependent) concepts and are determined in terms of the concrete situation rather than as an absolute property of the text itself.[32]

Indeed, when construing commercial contracts, some courts have ceased to bother to distinguish between patent ambiguity and latent ambiguity or to be concerned with what is clarity.[33] In other words, these courts treat patent ambiguity on a level with latent ambiguity; and in the one as in the other, extrinsic evidence of the surrounding circumstances will be admitted to resolve it. If the patent ambiguity is unresolvable by the extrinsic evidence, the term in question will be void for uncertainty. But this is true also of a latent ambiguity in those exceptional cases where the extrinsic evidence fails to resolve the ambiguity.[34] The distinction between patent and latent ambiguity

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[29] See the analysis in *Deutsche Genossenschaftsbank v. Burnhope* [1993] 2 Lloyd's Rep. 518 (H.C. (Eng.)). It is said in *Zurich Insurance*, *supra* note 10 at para. 83 in comments on the Court of Appeal decision in *Citicorp Investment Bank (Singapore) Ltd. v. Wee Ah Kee* [1997] 2 S.L.R. 759 that the extent to which the courts will go behind the clear meaning is one of degree. In the latter case, the Court of Appeal refused to disturb the clear meaning of a fresh loan agreement which provided that the call option should be terminated subject to two conditions.

[30] [1993] 1 S.L.R. 535 (C.A.).

[31] Take again a case such as *Wuensche Handelsgesellschaft International GmbH v. Tai Ping Insurance Co. Ltd.* [1998] 2 Lloyd's Rep. 8 (EWCA Civ.) where the insurers provided cover "ex factory in the People's Republic of China to warehouse in Hamburg". The fact was that the insurers knew that the goods would be coming from factories in the interior and therefore the words in quotes were clear; factory meant factory and not warehouse and PR China meant exactly that and not Zhenzhen.

[32] See the strong statement of Lord Hoffmann in *Charter Reinsurance*, *supra* note 9 at 391: "I think that in some cases the notion of words having a natural meaning is not a very helpful one. Because the meaning of words is so sensitive to syntax and context, the natural meaning of words in one sentence may be quite unnatural in another."

[33] So Lord Simon of Glaisdale says in *L. Schuler A.G. v. Wickman Machine Tool Sales Ltd.* [1974] A.C. 235 at 268 (H.L.) [*Schuler*]: "the distinctions between patent ambiguities, latent ambiguities and equivocations as regards admissibility of evidence are based on outmoded and highly technical and artificial rules and introduce absurd refinements". See also the bold pronouncements of Lord Wilberforce in *Ailsa Craig Fishing Co. Ltd. v. Malvern Fishing Ltd.* [1983] 1 W.L.R. 964 (H.L.).

[34] *Raffles v. Wichelhaus* (1864) 2 H. & C. 906 (Ct. of Exchequer) was such a case. Party A offered to carry ex p Peerless (intending the Peerless which would sail in October) but party B accepted intending the Peerless which would sail in December. The subjective intentions could be demonstrated as well

has therefore rightly been criticised as being obsolete.[35] Instead of applying it faithfully, the courts have recognised a wider range of contextual information which go beyond those which generate and resolve latent ambiguities.

B. *Criticisms of Strong Theory*

There are also more fundamental criticisms of the strong theory, which underpins the intention and rule-based model. The key assumption of the strong theory of meaning, namely that the intention can exist as a mental state independent of the language in which it is expressed, has been disputed. An alternative theory holds that language is indispensable to thought and mental state.[36] The thought or mental state exists only in so far as it is formed in a language. If so, there can be no difference between patent and latent ambiguity. Another theory denies that we can ever know the intention expressed in language if what we mean is the true meaning of that intention. Every interpretation is as valid as the other; for it is a recovery or reconstitution and indeed even the speaker necessarily only recovers his meaning.[37] If so, again there is no necessary legitimacy in the speaker's meaning, whether or not the language he has used is to be communicated to another. His interlocutor's meaning is as good as his and the distinction between patent and latent ambiguity is illusory in consequence. Another theory is that the formulation and articulation of an intention is over-determined. The possibility of isolating the intention from its effect is refuted since there are no objective mental states signifying the intention in any structural sense. Individuals are so much creatures of the time and society they inhabit that their intentions are consequences rather than causes of social practice or activity.[38] If so, the intention is not the cause of contracting as a social activity but is its consequence. As a consequence of engaging in the social activity of contracting, parties come to hold intentions about the contract. An even more extreme theory deconstructs language as thought and intention.[39] The very nature of language robs the speaker of any authority over the meaning of what he says or writes. The meaning resides then in the structure of the language, determined by the power relationships in the society. In a society which favours contracting, the meaning to be given to the contract is the result of the preferred power relationship. This article is not the place to evaluate the extent to which the strong theory is discredited by these theories. Indeed, evaluation may be out of place as the law as made by judges certainly cannot

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as the existence in fact of two ships, denominated the Peerless, one to sail in October and the other in December, for the purposes of showing that the parties were not *ad idem* on a material term. But whatever extrinsic evidence there was could not resolve the latent ambiguity and therefore the contract was not formed.

35 Lord Simon of Glaisdale in *Schuler*, *supra* note 33.

36 See Bice Benvenuto & Roger Kennedy, *The Work of Jacques Lacan* (London: Free Association Books, 1986).

37 See Roland Barthes, *Elements of Semiology* (London: Jonathan Cape, 1967); *Mythologies* (London: Jonathan Cape, 1972) who argues that the production of meaning is more than a correlation between signifier and signified but a cutting out of shapes.

38 Louis Althusser, *Lenin and Philosophy and Other Essays* (London: New Left Books, 1971) for instance, argues that ideology interpellates individuals as subjects. See also François Matheron, ed., *Louis Althusser: The Humanist Controversy and Other Writings (1966-1967)* (London: Verso, 2003).

39 Jacques Derrida, *Deconstruction in a nutshell etc.* (New York: Fordham University Press, 1997). See also Barry Stocker, ed., *Jacques Derrida: Basic Writings* (London: Routledge, 2007).

purport to choose between them nor can it halt between two opinions.[40] But at the least it would be foolish in view of these alternative theories to continue to take the theory which informs the rule-based model for granted.

II. Parol Evidence and Construction

In order to achieve the purposes of this article, it will further be necessary to consider the way in which the law gathers the formal information or materials (determines the objective datum) for construction by separating it from the interpretative (and inferential) process which leads to the interpreter's construct. A distinction along these lines between datum and the interpretative process that assigns meaning to the datum has been part of the Singapore law since the *Evidence Act* in 1893 portrayed the 'thin' parol evidence rule as a rule of evidence contained in sections 93 and 94. That there are even such rules of evidence has troubled many legal writers.[41] They ask:

> [I]s there a need to say the obvious that that which is determined objectively as the parties' contract shall not be varied by extrinsic evidence? If a contract might be set aside on grounds of vitiation, could it be otherwise that no evidence of vitiation would be admissible? Is there therefore a need to say that although the written contract may not be varied by extrinsic evidence, evidence of vitiation may be adduced to set it aside?

The parol evidence rule, they thus maintain, "is nothing more than a manifestation of the objective test of agreement" or "follows as a matter of course from the general rule as to the objective test of agreement".[42]

The key to explaining why the rules of evidence are not superfluously re-stating the objective test of substantive agreement is that they are statements of something else.[43] They are needed as provisions for the private regulation of evidence so that parties are permitted to control and prescribe the nature and amount of evidence which will be used as datum for construction of their contract, when the contract is entirely written.[44] Originally, it was the written evidence which was distrusted and oral evidence preferred as more reliable and authentic.[45] Against the historical

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[40] When there are so many plausible but divergent explanations of how we use language, it is not the judicial function to select among them. The negative injunction then is that the judicial interpreter must avoid making such a selection. Its task rather is to mediate impartially between the parties and allocate responsibilities, without interjecting its own views and prejudices.

[41] U.K., The Law Commission, *Law of Contract: The Parol Evidence Rule* (Working Paper No. 70) (Law Com. No. 154, 1986) at para. 2.7 says that the rule is no more than a circular statement when it is admitted or proved that the parties to a contract intended to make a fully integrated contract. Incidentally, the Law Commission identified three aspects of the rule. It is its second rule which covers the ground traversed by ss. 93 and 94. It does this without distinguishing as the enactments in Singapore do between substitution and variation. The Singapore Court of Appeal in *Zurich Insurance*, *supra* note 10 at para. 71 held that it is only s. 94 which embodies the thin parol evidence rule.

[42] See Edwin Peel, *Treitel: The Law of Contract*, 12th ed. (London: Sweet & Maxwell, 2007) paras. 6-012 and 6-013. See also Robert Stevens, "Objectivity, Mistake and the Parol Evidence Rule" in Andrew Burrows & Edwin Peel, eds., *Contract Terms* (London: Oxford University Press, 2007) ch. 6 at 109.

[43] See also Tan Yock Lin, "Writing and Signature in the Constitution and Proof of Contracts" [2003] 2 Sing. J.L.S. 333.

[44] *Cf.* Alex Stein, *Foundations of Evidence Law* (Oxford: Oxford University Press, 2005) 4, 5, and 25-31.

[45] See *Zurich Insurance*, *supra* note 10.

backdrop, the thin parol evidence rule which reversed the order of preference and conceded a role for the parties in regulating *ex ante* the evidence of their contract could hardly be superfluous. The reversing of the order is evident in section 93. Thus, if the parties say the writing shall be the sole evidence, extrinsic evidence will not be admissible to substitute for the writing. Even if they do not say so expressly, section 93 accomplishes the same result implicitly in the sense that if the parties reduce their contract entirely into writing, it is implied that they agree that the writing will be exclusive evidence and no other evidence will be allowed in substitution of the exclusive writing. There is accordingly little difference in substance between section 93 and the entire agreement clause,[46] except in one respect perhaps; namely that the agreement to make evidence conclusive may affect a particular term, without affecting the others, whereas section 93 makes the writing exclusive proof of an entirely written contract.[47]

Similarly, section 94 is not superfluously stating that whatever is operative or effective under the substantive law is provable by evidence. The purpose of section 94 is not to control substitutions of oral or other written terms for the written terms of the contract, which is what section 93 does, but the varying of them.[48] Although couched in proscriptive language (because it forbids varying the terms of the written contract), section 94 nontrivially allows enlargement of the datum to include facts showing consistency with or which amplify the writing.

The Act of course predicates that the determination of the objective datum for construction is logically preliminary to and precedes the process of construction.[49] Until that datum is clearly laid out, we do not know what we have to construe. In practice, however, the datum and the interpretative process may overlap in effect. Although the interpretative process is logically distinct from enlargement of the datum, there is an interplay between them in effect. Enlargement of the datum could have the same effect as that which would otherwise have been derived by interpretation. The greater the latitude for admissibility of evidence extrinsic to the written contract, that is to say the more liberal the expansion of the objective datum, the lesser may be the need to interpret the datum.[50] That is why in not a few cases, the question is framed as one of datum and then one realises that the party is in fact seeking to use extrinsic evidence to influence the construction by drawing an inference as to the meaning.[51]

There is an added complexity, namely that the Act also contemplates that extrinsic evidence may exceptionally be admitted to construe a contract if there are certain

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[46] *Cf. Quah Poh Hoe Peter v. Probo Pacific Leasing Pte. Ltd.* [1993] 1 S.L.R. 14 at 21 (C.A.) where the conclusive evidence rule (in s. 93) is stated as the parol evidence rule (in s. 94). For the correct analysis, see *Lee Chee Wei v. Tan How Peow Victor* [2007] 3 S.L.R. 537 (C.A.).

[47] See also Elisabeth Peden & John Carter, "Entire Agreement—and Similar Clauses" (2006) 22 J. Contract L. 1.

[48] Common law writers do not distinguish between substitution and variation. Both are regarded as concerned with the extent to which the document is to be treated as conclusive of its terms. See Edwin Peel, *Treitel: The Law of Contract*, *supra* note 42.

[49] See Ronald Dworkin, *Law's Empire* (London: Hart Publishing, 1998) 52: interpretation is an activity upon an existing object. See also Arthur Corbin, "The Interpretation of Words and the Parol Evidence Rule" (1965) 50 Cornell L.Q. 161 at 171; *Zurich Insurance*, *supra* note 10 at paras. 44 and 45.

[50] It does not conduce to clarity to describe the adduction of extrinsic evidence as an aid in the discovery or construction of its meaning as within the scope and concern of the parol evidence rule.

[51] See *Zurich Insurance*, *supra* note 10 at para. 66.

types of ambiguities calling for a resolution. This is the parol evidence rule in the wide or thick sense,[52] for which the Act makes provision in sections 95 to 100. Some of these provisions have already been discussed in some detail in Part I. Their general relationship with sections 93 and 94 (the datum) is also important. In particular, the existence of a large gulf separating sections 93 and 94 on the one hand and sections 95 to 100 on the other must not be overlooked. The former two enactments predicate an entirely written contract; the parties are given liberty to restrict the proof of an entirely written contract. However where interpretation is involved, the rules contained in sections 95 to 100 apply without distinction between entirely written and partly written contracts. They apply to any written term so that a contract which is partly written also attracts their attention.[53] This is a vital and large difference, for which there is documentation showing that it was deliberate. At common law, the rules contained in sections 95 to 100 were first laid down for the construction of such entirely written and unilateral documents as wills and testaments and '*inter vivos*' document disposing of property. These were deliberately extended to partly written contracts. As was said in *Zurich Insurance*:

> [I]n Stephen's Digest, Stephen acknowledged a great debt to the work of Vice Chancellor Wigram, Extrinsic Evidence in Aid of the Interpretation of Wills, stating that Article 98 differed from the six propositions of the vice chancellor only in its arrangement and form of expression and in the fact that it was not restricted to the interpretation of wills (see Stephen's Digest at p. 210).[54]

In short, the *Evidence Act* deals with evidence outside the four corners of an entirely written contract in a twofold manner by prohibiting substitution and variation of the datum, and with interpretation of any written term of the contract.

The Act has nothing to say about oral contracts and in particular sections 93 and 94 have nothing to say about partly written contracts. The provisions concerning interpretation, sections 95 to 100, focus on resolving any written term that is ambiguous in a specified manner and have nothing to say about other oral terms. In the case of oral contracts or oral terms, the datum has to be ascertained according to the objective test of agreement. There is simply no need to have specialised provisions regulating the datum such as those of sections 93 and 94 and the objective test of agreement of itself determines what is relevant and what is not for this purpose. Likewise, the construction of oral terms is performed apart from the rules contained in sections 95 to 100, without the restrictions imposed by reference to latent ambiguity. However, if the rules for interpreting wills can be extended to any written term of a contract, they must be extendible also to oral terms, since the interpretative process cannot change depending on whether the datum is a text or discourse (*i.e.*, the meaning of a

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[52] *Ibid*. at para. 33.

[53] The critical wording is "When the language used in a document", not "in not in an entirely written document".

[54] *Zurich Insurance*, *supra* note 10 at para. 73. Stephen's rationalisation did not accord with 19th century thinking as to how commercial documents should be construed. According to Lord Hoffmann in *Bank of Credit*, *supra* note 9 at para. 57:

> It was however unusual, even in the nineteenth century, for commercial documents to be interpreted according to rules of construction. The quest for certainty, which still dominated the construction of wills and deeds, was thought less important than the need to give effect to the actual commercial purpose of the document.

sentence must be medium-invariant). All studies of interpretation and pragmatics at least share this assumption.[55] At the level of practice, some of us may imagine that a person will be more careful to express his meaning clearly if he is going to make a written or partly written discourse; and that there ought to be some difference in the interpretative process. To the best of this author's knowledge, no theory bears this conjecture out. Rather the contextual-dependence of words is little affected by whether they are written or spoken.

In the case law, there is authority that the question of construction of a written contract is one of law whereas the question of construction of an oral contract is one of fact.[56] This however is no proof that therefore the interpretative processes of assigning a meaning differ depending on whether the contract is written or oral. The division between the roles of judge and jury reflects the need to regulate the datum when the contract is entirely written. It is a principle of efficiency to ensure that when the jury is responsible for finding the terms of an oral contract, it will also be entrusted with the ascertainment of meaning as well. However, it does not follow that the jury will be applying anything other than the same interpretative process if interpretation is a matter of logical inference. Incidentally, McMeel and the Singapore Court of Appeal in *Zurich Insurance* seem to be hinting that there is a difference between interpreting a written text and interpreting a discourse and that in the former case, the purpose of restricting admissible extrinsic evidence to evidence that will resolve a latent ambiguity is to preserve the effect of the thin parol evidence rule (corresponding to sections 93 and 94 in Singapore), and to prevent its subversion.[57] With respect, this mistakes the effect for the substance. In substance, the admissibility of evidence to resolve syntactical or semantic ambiguities, *i.e.*, whether grammatical or in terms of correspondence to substance, is only evidentiary in a sense. In fact, what happens is that where there is a gap or incompleteness in the meaning, the construing court is drawing an inference from the surrounding circumstances (context) that one of the two ambiguous meanings is correct. The admission of the extrinsic evidence is merely the necessarily entailed consequence of the inferential reasoning involved in the interpretative process of completing the sentence. There is no question of subverting the datum. Even if the preclusion of subversion of the thin parol evidence rule is part of the interpretative process, the preclusion rationale completely disappears or makes no sense when the contract is only partly written.

The second part of this article contains the positive submissions which build upon the distinction between datum and interpretative process, which has been clarified. It will be argued that the notion of contextual approach to interpretation does not adequately delineate the distinct elements involved in the determination of the speaker's meaning beyond underlining the possibly decisive importance of context or contextual dependence in the language of a contract. The distinct elements, if any, of the interpretative process must be delineated, bearing in mind that in logic and as a matter of pragmatics, there is no difference between the way we construe written and oral contracts since the meaning of an objective datum does not change depending on whether it is a text or a discourse. It will be argued that the inferences which are

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[55] Especially formal theories of meaning which pay no attention to the speaker and his intention.

[56] See *Torbett v. Faulkner* [1952] 2 T.L.R. 659 at 661 (EWCA Civ.).

[57] See *Zurich Insurance*, *supra* note 10 at paras. 62 to 66.

permissible under the operation of construction are governed by different considerations from those which inform the thin parol evidence rule; namely the avoidance of excessive and creative reasoning that will overstep the line between ascertainment of meaning and intervention (or imputation or attribution of meaning) and achievement of the object of the process which is the fostering of the making of a contract as a private, quasi-legislative act. An inferential reasoning by reference to latent ambiguity proves inadequate to meet these considerations but a principle of commercial purposes, which is essentially a principle of instrumental rationality, does.[58]

A. *Surrounding Circumstances: Datum or Interpretative Process?*

In the second part, we shall first examine the notion of surrounding circumstances and then that of commercial purposes, as they relate to the interpretative process. The various factors affecting the development of the notion of surrounding circumstances may be grouped roughly under two headings. These are the relationship with datum[59] and the relationship with interpretative process. As we have seen, the thin parol evidence rule is concerned solely with regulating the datum of an entirely written contract by rejecting substitutionary evidence and restricting extrinsic evidence to evidence of consistency and sincerity.[60] Extrinsic evidence adduced for the purposes of interpretation is a different matter. There are thus two broad ways to bring materials outside the four corners of the writing before the court. One is to attach it to the datum. The other is to use it to draw inferences in the interpretative process.

Where does the notion of surrounding circumstances belong? Certainly, it has never been defined and we are told that it can comprehend anything that is not in the writing of an entirely written contract. That being the case, its relationship with datum or with construction cannot be assumed but must be made explicit. Consider the question whether the market practice forms part of the surrounding circumstances. The question has provoked some strong reactions. In one of them, the court first describes the true nature of the appeal or recourse to market practice as "an attempt to influence the construction of the agreement subjectively, by reference to the opinions of market practitioners as to the normal and proper scope of a clause of this character …".[61] Then, it rejects the attempt as "completely unsound in practice".[62] On the other hand, if the market practice represents a rejection of an older process, some courts are prepared to accept, in effect, evidence of the market practice as showing the improbability that the parties could have intended to rely on a practice which had ceased to be operative.[63] The difference between the two cases is that the market practice is in one case adduced for the drawing of an interpretative inference

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58 This article does not discuss the point at which the process of construction shades into the process of implication. The latter has in fact been described as involving a process of construction of the agreement as a whole in its commercial setting.

59 Where the surrounding circumstances show that the parties made another contract superseding the earlier contract, this is also a matter of datum.

60 Thus, "consideration of the surrounding circumstances *and* the commercial purpose …": *The Elpis*, *supra* note 28 at 610.

61 *The Leegas* [1987] 1 Lloyd's Rep. 471 at 475 (Q.B.). As opposed to proving custom or usage or a market shorthand; *cf. American Airlines Inc. v. Hope* [1973] 1 Lloyd's Rep. 233 at 245.

62 *Ibid*.

63 See *MFI Properties Ltd. v. BICC Ltd.* [1986] 1 All E.R. 974 at 977 (Ch.) [*MFI Properties*].

while in another it is adduced as forming the datum.[64] The notion of surrounding circumstances, as these cases show, may be apt for one task but not another.[65]

Regrettably, whilst being clear that datum and interpretative process are different matters, the apex courts in two common law jurisdictions have in two recent cases respectively proceeded when dealing with surrounding circumstances (re-designated as contextual information) to obscure the distinction. In *Zurich Insurance*,[66] the Court of Appeal in Singapore has pronounced that the notion of surrounding circumstances is part of the datum of construction. After a searching examination of the arguments, the Court of Appeal held that the common law contextual approach to contractual interpretation is statutorily embedded in proviso (f) to section 94. With respect, the judgment was excellent in its tracing of the rise to prominence of the notion of contextual information. The court's historical research also impressively recalled how proviso (f) was originally part of the provisions relating to construction, namely of Article 98 which dealt with construction, but that it was however moved to Article 97 (which corresponds to section 94). But the conclusion, that the proviso, when moved to the provisions which define the datum, has nevertheless retained its function as an interpretative element, is unconvincing. There are a number of alternative plausible contrary explanations which the court did not consider. The proviso for instance could have been moved because the legislature misunderstood its function or desired it to serve a different function or did not wish to have it trammelled by the distinction between latent and patent ambiguities. To reach the conclusion at which the court arrived, there must be proof ruling out competing alternative explanations or hypotheses. *Prima facie*, as a proviso to section 94, proviso (f) serves to regulate the datum of construction; and so there must be proof to the contrary that this prima facie function was deliberately excluded. In a sense, the conclusion of the Court of Appeal that the proviso retained its pristine interpretative function in a setting about datum was also surprising because the Court had clearly distinguished between the datum and interpretative process in its exposition of the common law.

One unfortunate consequence of regarding the proviso (f) as containing the "contextual approach" in a jurisdiction like Singapore's is to subject the notion of surrounding circumstances to the overall constraint contained in the opening words of section 94. According to those words, the provisos to the section, including proviso (f), must not have the effect of varying or modifying the contract. Since the main operative part of section 94 requires that the application of the proviso (f) must not contradict, vary, modify or alter the written contract, and the effect of introducing evidence of surrounding circumstances will frequently be to vary, add to or modify the contract, proviso (f) ultimately is of limited scope.

The decision of the Court of Appeal in Singapore was in fact equivocal about where the notion should fit in because there were large discursive parts of the judgment in which the court seemed to be saying a different thing that the notion was part of

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64 See *Zeus*, *supra* note 28.

65 The question whether the surrounding circumstances are part of the factum or part of the process of construction is pretty much academic in jurisdictions which do not have to fit things into the correct pigeonholes. Singapore however is an example of the contrary. There, the *Evidence Act* creates pigeonholes and the courts have no liberty to embark on an untrammelled analysis.

66 *Supra* note 10.

the process of interpretation, not the datum. This equivocalness is perhaps to be expected, since in the common law development of the notion it has never been made clear whether the surrounding circumstances are datum or an interpretative element. In the seminal words of Lord Wilberforce the equivocation may be detected. He says:

> The general rule is that extrinsic evidence is not admissible for the construction of a written contract; the parties' intention must be ascertained. It is one and the same principle which excludes evidence of statements, or actions, during negotiations, at the time of the contract, any of which to the lay mind might at first seem proper to receive. … There are of course exceptions. … And evidence may be admitted of surrounding circumstances…[67]

The difficulty in understanding Lord Wilberforce is that the phrase "admissible for the construction of a written contract" may be referring to the datum or the interpretative process. Some courts have frowned upon references to the surrounding circumstances,[68] which they say are misleading to the extent that they suggest that subjective intention is relevant. They have preferred to speak of the factual matrix or background,[69] or "the genesis of the transaction, the background, the context, the market in which the parties are operating".[70] If anything, the change of terminology to background knowledge seems to point more to its relevance to datum than interpretative process. Others have charged references to the factual matrix with precisely the same fault. References to the reasonable man are increasingly common, since Lord Hoffmann gave it currency in a recent case, when he referred not only to the reasonable man but also to background knowledge. He said:

> Interpretation is the ascertainment of the meaning which the document would convey to a reasonable man having all the background knowledge which would reasonably have been made available to the parties in the situation in which they were at the time of the contract.[71]

So this seems to suggest that the background knowledge supplies materials for construction and is part of the datum of construction.

Not only has the opportunity to clarify whether surrounding circumstances are relevant to datum or interpretative process or both, been missed, the distinction has now further been obscured by the failure in the English cases to notice the difference between datum and interpretative process when grappling with pre-contractual negotiations.[72] Again, Lord Wilberforce paves the way with the view that subjective declarations or views, and thus of negotiations, notwithstanding they may be known

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67 *Schuler*, *supra* note 33 at 261.

68 *The Diana Prosperity* [1976] 2 Lloyd's Rep. 621 at 624 (Q.B.) [*Diana Prosperity*]: "[T]his phrase is imprecise: it can be illustrated but hardly defined". See also *Rabin v. Gerson Berger Association Ltd.* [1986] 1 W.L.R. 526 (EWCA Civ.).

69 See *Arbuthnott v. Fagan* [1996] L.R.L.R. 135 (EWCA Civ.); *Charrington & Co. Ltd. v. Wooder* [1914] A.C. 71 (H.L.). But see the criticisms in *Plumb Brothers v. Dolmac (Agriculture) Ltd.* [1984] 271 E.G. 373 (EWCA Civ.).

70 *Reardon-Smith Line Ltd.*, *supra* note 18 at 996.

71 *Investors Compensation Scheme*, *supra* note 9 at 912.

72 As stated in *Bank of Credit*, *supra* note 9 at 269, there are no conceptual limits to what can properly be regarded as background.

to each other as a result of communication to each other are unhelpful. In the words of Lord Wilberforce, which were spoken in *Prenn v. Simmonds*:

> The reason for not admitting evidence of these exchanges is not a technical one or even mainly of convenience. … It is simply that such evidence is unhelpful. By the nature of things, where negotiations are difficult, the parties' positions, with each passing letter are changing and until the final agreement, though converging, still different. … If the previous documents use different expressions, how does construction of those documents, itself a doubtful process, help on the construction of the contractual words.[73]

Significantly, Lord Wilberforce does not say that pre-contractual negotiations are inadmissible but that they are unhelpful to the task of construction. This suggests that the notion of background knowledge is an interpretative element and is relevant if it advances the interpretative process.

Not all cases on pre-contractual negotiations however stress that the court must focus on the purpose of admissibility of the evidence. In some cases, *a priori* distinctions are relied on which are consistent with an assumption that there is an exclusionary rule excluding evidence of prior negotiations.[74] So although a slip, initialled by the underwriters, may record the original agreement between the insured and the insurers, if a policy is finally issued, that will be the contract, and not the slip. The slip cannot be used as an aid in construction.[75] The contrary opinion however stresses that the rule is against evidence of prior negotiations, not a slip which is a concluded contract, since it "can be argued that an insurance slip is different from negotiations for the formation of a contract".[76] So evidence of a concluded agreement, whether oral or in writing, has been admitted as an aid to construction, because a concluded agreement is no longer changing.

Other cases displaying this understanding of the exclusionary rule have seen no difficulty in admitting alongside the exclusionary rule, and as background knowledge or information, subjective declarations which show that the declarant was knowledgeable about the existence of a fact, as opposed to showing that a word had a particular meaning to him.[77] Such cases sort out the impact of declarations of intention prior to contract by asking about the purposes for admissibility of the evidence. The evidence is admissible for any purpose (such as establishing the datum) other than the purpose of proving the meaning intended.

As has been noted, the Singapore Court of Appeal in *Zurich Insurance* regarded the surrounding circumstances as datum, within the meaning of proviso (f) to section 94. Having characterised the notion as datum, the court proceeded to describe contextual evidence as evidence that is relevant, reasonably available to all the contracting parties

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[73] [1971] 1 W.L.R. 1381 at 1384 (H.L.). Background knowledge includes in *Charter Reinsurance*, *supra* note 9, the history of reinsurance, the wider legal, regulatory and accounting regime applicable to reinsurance. See also *Secured Income Real Estate (Australia) Ltd. v. St. Martins Investments Proprietary Ltd.* (1979) 144 C.L.R. 596 where the Australian High Court refused to permit evidence of prior negotiations for the purposes of clarifying that by leases the parties meant commercial leases.

[74] See also *Coop International Pte. Ltd. v. Ebel S.A.* [1998] 3 S.L.R. 670 at 692 (H.C.).

[75] See Beldam L.J. in *Youell v. Bland Welch & Co. Ltd.* [1992] 2 Lloyd's Rep. 127 at 141 (EWCA Civ.).

[76] See *ibid*. at 133 per Staughton L.J. See also *The Karen Oltmann* [1976] 2 Lloyd's Rep. 708 at 712 (Q.B.) [*Karen Oltmann*].

[77] *Shore v. Wilson* (1842) 9 Cl. & F. 355 (H.L.). See also *Karen Oltmann*, *ibid*.

and relates to a clear or obvious context. It is not conditioned on the existence of any latent ambiguity. Where the context to be proved includes prior negotiations and subsequent conduct, the court found the views expressed in McMeel's article[78] and Lord Nicholls' article[79] persuasive.[80] The final conclusion was that there should be no absolute or rigid prohibition against evidence of previous negotiations or subsequent conduct, although, in the normal case, such evidence was likely to be inadmissible.

So according to the court, some prior negotiations will be ruled out as contextual evidence because they are irrelevant, others because they are not reasonably available to the other party, and still others because they do not relate to a clear or obvious context.[81] Subjective declarations of intent occurring in the course of negotiations but not communicated to the other party will usually not reasonably be available and will not count as contextual evidence. They are however admissible in the face of latent ambiguity.[82] Pre-contractual negotiations will involve both communicated and non-communicated subjective declarations of intent and so unless there is a latent ambiguity to resolve, the non-communicated subjective declarations of intent will be inadmissible.

The latest House of Lords observations on the same subject in *Chartbrook Ltd. v. Persimmon Homes Ltd.*[83] reveal marked differences with the observations of the Singapore Court of Appeal.[84] As to whether contextual evidence is necessarily evidence addressed to the parties, Lord Hoffmann says:

> The law sometimes deals with the problem by restricting the admissible background to that which would be available not merely to the contracting parties but also to others to whom the document is treated as having been addressed. Thus in *Bratton Seymour Service Co Ltd v. Oxborough* [1992] BCLC 693 the Court of Appeal decided that in construing the articles of association of the management company of a building divided into flats, background facts which would have been known to all the signatories were inadmissible because the articles should be regarded as addressed to anyone who read the register of companies, including persons who would have known nothing of the facts in question. In *The Starsin* (*Homburg Houtimport BV v. Agrosin Private Ltd* [2004] 1 AC 715) the House of Lords construed words which identified the carrier on the front of a bill of lading without reference to what it said on the back, on the ground that the bankers to whom the bill would be tendered could not be expected to read the small print.[85]

As to whether there is flexibility to admit pre-contractual negotiations as contextual background, Lord Hoffmann at para. 42 maintains that there is an exclusionary rule which excludes pre-contractual negotiations. He says this:

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78 Gerard McMeel, "Prior Negotiations and Subsequent Conduct—The Next Step Forward for Contractual Interpretation?" (2003) 119 L.Q.R. 272.

79 Lord Nicholls, "My Kingdom for a Horse: The Meaning of Words" (2005) 121 L.Q.R. 577.

80 The court did not comment on the application of the exclusionary rule in the Court of Appeal case of *MCST Plan No 1933 v. Liang Huat Aluminium Ltd.* [2001] 3 S.L.R. 253 [*MCST Plan No 1933*]. See also Ewan McKendrick, "Interpretation of Contracts and the Admissibility of Pre-Contractual Negotiations" [2005] 17 Sing. Ac. L.J. 248.

81 Presumably this also captures the private dictionary cases.

82 *Zurich Insurance*, *supra* note 10 at para. 132.

83 [2009] 3 W.L.R. 267 [*Chartbrook*].

84 The decision on rectification is not discussed.

85 *Chartbrook*, *supra* note 83 at para. 40.

> The rule excludes evidence of what was said or done during the course of negotiating the agreement for the purpose of drawing inferences about what the contract meant. It does not exclude the use of such evidence for other purposes: for example, to establish that a fact which may be relevant as background was known to the parties, or to support a claim for rectification or estoppel.[86]

Superficially there is agreement between both apex courts that contextual information is a matter of datum. But the Singapore Court of Appeal sees the datum as relevant to the interpretative process (which is illogical) whereas the House of Lords (in the judgment of Lord Hoffmann) more logically distinguishes it from the interpretative process. With respect, however, the above-quoted remarks of Lord Hoffmann are misleading in suggesting that establishing a background fact never serves the purposes of drawing inferences or that the relevance of a background fact is solely to serve as proof that the parties knew of its existence. Consequently, one cannot admit background facts (what was said or done) as an interpretative element. What has been overlooked is that contextual information has no *a priori* relevance. If the purpose of admitting evidence of pre-contractual negotiations is to substitute for the writing (datum), the courts must exclude the evidence. The exclusionary rule is a rule about the datum but Lord Hoffmann appears to express it as a rule about the interpretative process inasmuch as he implies that the evidence of pre-contractual negotiations can never be used to draw inferences about what the contract meant. So far as the interpretative process is involved, the question is not whether extrinsic evidence is admissible or excluded but whether the court of construction is permitted to draw certain types of inference in the interpretative process. If pre-contractual negotiations under certain circumstances are relevant contextual information in revealing the commercial purpose, it would be unfortunate to read the judgment in *Chartbrook* as forbidding the court of construction from having access to that information.

Neither decision is fully convincing. The Singapore obiter dicta may be criticised for sweeping all pre-contractual negotiations into the category of datum, thus underestimating the independent and distinct interpretative process, and then advocating a flexible treatment of pre-contractual negotiations, thus contradicting the categorisation of contextual information as datum. The English obiter dicta on the other hand may be criticised for sweeping all pre-contractual negotiations into the category of datum, and then maintaining inexorably the consequences of the categorisation as datum. Yet both courts agreed or assumed that the notion of surrounding circumstances has no conceptual distinctness. If the notion of surrounding circumstances cannot be defined and is comprehensible only by inquiring into the purposes for which they are relied on, and if the distinction between datum and interpretative process is valid, the answer is clear. Evidence of pre-contractual negotiations cannot be admitted to substitute for or vary the entirely written contract but is admissible for these purposes if the contract is only partly written. Moreover, the evidence is admissible if it can shed light on the interpretative process as proof of the commercial purposes of the parties and their contract. It is submitted therefore that notwithstanding the obiter dicta in both *Zurich Insurance* and *Chartbrook* that while prior negotiations evidence and for that matter surrounding circumstances evidence cannot be admitted to substitute or vary an entirely written contract, they can be admitted to prove the

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[86] *Ibid*. at para. 42.

commercial purpose which both parties sought by their contract to accomplish. For the latter purpose, it does not matter whether the contract is written or oral, since the interpretative process is entirely different from the determination of the datum.

Similar conclusions may be reached with respect to evidence of post-contractual declarations and conduct. Like pre-contractual negotiations, post-contractual declarations and conduct must usually be known or have been reasonably available to both parties to the contract[87] or it would be hard to see what relevance they could have as evidence. Again, post-contract conduct is not capable of definition for its relevance depends on what is to be proved, *i.e.*, of the purposes for which it is to be admitted in evidence. It may validly show that the parties made a new contract or varied some terms of the old one or that the conduct of one gave rise to a post-contract estoppel. These are matters of datum. Yet again, the post-contract conduct may show the nature of the contract made. For instance, in order to prove that the parties did not contemplate making their oral conversations subject to written contract, what could be more cogent for the purposes of construction than that the other party, at a time when no dispute was pending, refused to execute the contractual document sent to him for signature and execution.[88] These purposes which relate to datum are of no concern to the interpretative process.

In Singaporean terms, the admissibility of the evidence for the purposes identified under sections 93 and 94 is different from the relevance of post-contractual negotiations and conduct to the interpretative process. If the purpose of admitting evidence of post-contractual negotiations or conduct is to substitute for the entirely written contract, the evidence must be excluded under section 93 which does not say that the evidence must be that at the time of contract. The same reason that excludes pre-contractual negotiations which relate to the datum excludes post-contractual negotiations. "Otherwise one might have the result that a contract meant one thing the day it was signed, but by reason of subsequent events meant something different a month or a year later."[89] One can appreciate that these circumstances may have small cogency; in so far as they take the form of conduct, they may represent only the parties' view of the contract as distinct from the true contractual position.[90] They may also be self-interested postures, adopted for the manufacture of evidence in one's favour.[91] But in any case, they must be excluded because the parties have by their agreement to reduce their contract into writing agreed to do so. Such was the case

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87 The House of Lords in *Diana Prosperity*, *supra* note 68 rejected an attempt to refer to evidence of Japanese usages and practices in aid of construction of whether the description of a motor vessel to be built after it had been chartered was a condition precedent.

88 *Jayaar Impex Ltd. v. Toaken Group Ltd.* [1996] 2 Lloyd's Rep. 437 (Q.B.).

89 Lord Reid in *James Miller & Partners Ltd. v. Whitworth Street Estates (Manchester) Ltd.* [1970] 1 A.C. 583 at 603 (H.L.). Again in *Schuler*, *supra* note 33 at 252 and see Lord Simon of Glaisdale at 265-270. *Cf. Watcham v. A.G. of East Africa Protectorate* [1919] A.C. 533 (P.C.), described as "a refuge of the desperate" in *Schuler*, *ibid*. at 261. See also *Estate of Seow Khoon Seng v. Pacific Century Regional Developments Ltd.* [1997] 1 S.L.R. 509 (H.C.) on the relevance of the subsequent conduct, reversed on other grounds [1997] 3 S.L.R. 761 (C.A.).

90 As in *Schuler*, *ibid*..

91 The local courts have not been very strict about this. See *Yeo Kee How v. Container Warehousing & Transportation (Pte.) Ltd.* [1977] 1 M.L.J. 219 at 221 (Sing. H.C.) where the court speculates about the construction the plaintiff would have put on the clause had he been successful in securing better employment about 7 months into his period of employment with the defendants.

in *Khoo Chooi Sim v. The Radio & General Trading Co. Ltd.*,[92] where the defence counsel sought to rely on evidence of the defendant giving the plaintiff a credit note for the return of two Fridgette Refrigerators as proof of the fact that the property in the goods had passed to the defendant. As the contract of sale was entirely written, the attempted reliance was to be excluded. The intention as to when property in the goods sold should pass could only be ascertained from the agreement itself and not from any transaction (the giving of the credit note) that occurred subsequent to the execution of the agreement.

However, if the relevance of the conduct is that it reveals the commercial purpose, the case should be different since the conduct would be relevant to the interpretative process, not as evidence of the datum. In *Zurich Insurance*, the Court of Appeal apparently approved of an obiter decision of the High Court, namely *China Insurance Co. (Singapore) Pte. Ltd. v. Liberty Insurance Pte. Ltd.*,[93] in which unilateral post-contractual subjective declarations of intention were admitted in evidence in order to construe a contract between BT and the defendant insurers, which was first in chronology. If that contract also covered BT in respect of the risks which the plaintiff insurers had agreed to cover under their contract with BT, there would be a case of double insurance entitling the plaintiff insurers to contribution from the defendant insurers. In approving the decision, the Court of Appeal may have omitted to notice that the subjective intentions of the defendant insurers in *China Insurance* which were communicated to BT after the contract between BT and the defendant insurers had been made were unknown to the plaintiff insurers when they agreed to insure BT in respect of certain risks relating to work on certain vessels. The subjective declarations communicated to BT the defendant's opinion that the defendant's policy excluded risk relating to work on those vessels. Acting on them, BT had duly sought additional cover under another contract with the plaintiff insurers. Andrew Phang Boon Leong JC held that on a reasonable construction of the contract between BT and the defendant insurers the subject matter and the risk covered by the plaintiff's and the defendant's respective policies were not the same. He went on to hold obiter that section 94 of the *Evidence Act* did not apply as the plaintiff and the defendant were essentially strangers to each other's contracts or policies. However, section 93 of the Evidence Act was applicable; in particular the common law exceptions to section 93 were applicable. He proceeded therefore to apply "the well-established common law principle to the effect that extrinsic evidence is admissible to aid the court in establishing the factual matrix which, in turn, would help the court in construing the contract(s) concerned".[94]

It is important to appreciate that the contract being construed in *China Insurance* was the first contract between BT and the defendant insurers and the declarations were therefore post-contract declarations. Although the declarations were acted upon, the factual matrix could not possibly prove any estoppel as between the plaintiff insurers and the defendant insurers since the plaintiffs were a third party to the declarations. The contextual information was that BT felt they were not covered against certain risks by the first contract and entered into a second insurance contract for that specific coverage. It could not have been background knowledge in the datum sense so far as

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92 [1964] M.L.J. 101 (Ipoh C.A.).

93 [2005] 2 S.L.R. 509 (H.C.) [*China Insurance*].

94 *Ibid*. at para. 46. The court with respect was not very clear on datum and interpretative process.

the first contract was concerned. Assuming that the high Court decision was right, the only other remaining explanations for the admissibility of the information were that the information could be used to draw an inference as to the meaning of the first contract in view of the latent ambiguity in that contract or that it was used to shed light on the commercial purpose of the first contract. On either explanation, it would appear that there is no requirement that unilateral subjective declarations cannot be admitted to prove an inference or the commercial purpose. This would be consistent with what theories of interpretation say, namely the impossibility of restricting the contextual dependence of a text or discourse to any given set of data.

B. *Heuristics and the Commercial Purpose*

The final point to be made about the notion of surrounding circumstances relates to the heuristic element in the interpretative process and leads us to the notion of commercial purpose. Under the strong theory as was seen earlier the interpretative process is confined to resolving latent ambiguities. The interpretative process is straightforwardly a clarifying and usually deductive process; the court simply prefers the evidence that will resolve the ambiguity which is also the evidence which exposes it. Under a 'prediction and control' theory, a greater scope of interpretation is entailed since a wider context-dependency is recognised and as a result patent ambiguities may be, and indeed, even so-called plain sentences may be, construed. There is however a difference between interpreting latent ambiguities and interpreting patent ambiguities and plain sentences. As modern theories of pragmatics demonstrate, the interpretative process (as distinguished from datum) in the latter case will have to involve a heuristics,[95] namely the formulation of alternative hypotheses and the use of the contextual information to narrow the range of hypotheses before the selection of the best fitting hypothesis in terms of some comparative preference such as the greater simplicity of one hypothesis compared with the others.[96] The deductive and inductive reasoning involved in clarifying latent ambiguities will not do. Suppose the example given earlier of the contract to sell light sandals. No amount of deductive or inductive argument will enable the interpreter to decide whether the lightness is a reference to colour or weight. Instead, the task of the interpreter is to discover among the contextual information materials for an educated guess. The ascertainment of meaning will not be possible by merely referring to the contextual dependence of the communication. It will be necessary to ascertain which aspect of context-dependency is relevant to the ascertainment of the meaning. The interpreter needs a set of rules which suggest on which contextual features to focus, avoiding having to trawl through the "infinitely many faces of the 'context' ".[97]

If the analysis given above is correct (namely that the distinction between latent and patent ambiguity is inadequate and that the notion of surrounding circumstances must be carefully sorted out into those which relate to datum and those which relate to interpretative process), we should expect to see that the principle of commercial

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[95] Marcelo Dascal, *Interpretation and Understanding* (Amsterdam: John Benjamin Publishing Co., 2003) 45-47.

[96] See Sir Robert Goff, "Commercial Contracts and the Commercial Court" [1984] L.M.C.L.Q. 382 at 389.

[97] Dascal, *supra* note 95 at 46.

purposes is at least a heuristics to guide the interpreter in the search for the meaning of a contractual text or discourse.

It has been said that interpretation according to the principle of commercial purposes means that generally the courts will, avoiding "a detailed semantic and syntactical analysis",[98] attribute to the parties a reasonable and sensible businesslike intention,[99] especially when the quality of the drafting is very poor,[100] but not in any sense conditioned on the existence of any ambiguity or bad drafting.[101]

The benefits of a commercial-purpose-driven interpretation are considerable and in demonstrating this, preference is given to Singapore cases. There is no doubt that an interpretative process in which we ask whether the commercial purpose provides a good fit to the meaning claimed by one party will go a long way toward saving the parties from a wrong choice of word or an incorrect expression, especially when they use words that unknown to them have acquired a strong contrary flavour or complexion or a narrower legal signification than they might suppose, or when they have proceeded from the 'penchant' of choosing obsolete, dubious or archaic words.[102] For instance, the phrase 'on account of' is an expression bearing a narrower legal signification that some person is contracting as another's agent,[103] and there is a rule of construction to that effect. But parties not acting under legal advice may be lost to that legal signification. Of course, as we have seen, a party may show that as a matter of datum the parties to the contract have provided a private dictionary meaning or that the case is one of rule ignorance. Very often, however, all this will not be necessary if recourse is had to the commercial purpose of the contract. Even where there is no direct evidence of the parties' mutual ignorance, regard to the commercial purpose will swiftly resolve the problem, as in *Punjab National Bank v. de Boinville*.[104]

There is also little doubt that many latent ambiguities may be more efficiently disposed of by recourse to the commercial purpose principle. To take an example, the word 'stow' in a bill of lading has become archaic on account of radical changes in the shipping practice. Goods for carriage, instead of being loaded into ship holds, are nowadays packed into containers, which are then sealed (usually) and loaded onto the vessel. A latent ambiguity arises in the light of the existing practice. Does the obligation to stow now refer to the process of packing (or stuffing) or unpacking as well or merely to the stowage of the containers on board the vessel?[105] Again, regard

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98 *Antaios Cia Naviera S.A. v. Salen Rederierna A.B.* [1985] A.C. 191 at 201 (H.L.) [*Antaios Cia Naviera*]. See also *Miramar Maritime Corp. v. Holborn Oil Trading Ltd.* [1984] A.C. 676 at 682 (H.L.).

99 In *Antaios Cia Naviera*, *ibid*., Lord Diplock in fact envisaged a more limited and negative role for the principle as serving to reject a conclusion on meaning which flouts business commonsense.

100 *Mitsui Construction*, *supra* note 27.

101 See also *Antaios Cia Naviera*, *supra* note 98.

102 See *The Sounion* [1987] 1 Lloyd's Rep. 230 (EWCA Civ.); *The Holstencruiser* [1992] 2 Lloyd's Rep. 378 at 380 (Q.B.) [*Holstencruiser*].

103 In the legal sense. But the word 'agent' attracts no similar presumption. 'No word is more commonly and constantly abused than the word "agent"': *Kennedy v. de Trafford* [1897] A.C. 180 at 188 (H.L.). In *The Kilmun* [1988] 2 Lloyd's Rep. 1, the defendants were described as appointed by the plaintiffs "as its agent for the performance of the certain duties … described herein" but otherwise the wording of the contract and the price fixed for the alumina only made sense if the defendants were dealing as principals (*i.e*., as subcontractors).

104 [1992] 1 W.L.R. 1138 at 1155 where the phrase was held not to create an agency in the "context of determining entitlement to an indemnity under an insurance policy".

105 See also *Holstencruiser*, *supra* note 102.

to the commercial purpose will normally resolve this problem quite satisfactorily, without the need for detailed investigations into private dictionaries or other causal explanations.

Then, as an illustration of the commercial purpose principle providing a ready solution to the problem of clarity, we have the case of *Pacific Century Regional Developments Ltd v. Estate of Seow Khoon Seng*.[106] In that case, there was a contract to sell certain shares but in the event that public listing failed, the vendor was to have the option to re-purchase them at their net tangible value. The net tangible value was defined as "the net tangible value [NTV] of the company as at the end of the financial year immediately preceding the exercise date based on the audited financial statements of the company in accordance with generally accepted accounting principles and practices…" (insertion mine). The financial statements had since 1981 been drawn up without reflecting the revaluation of certain of the company's leasehold assets and the difference in NTV between a computation which ignored and one that took into account the revaluation was a sizeable 40 cents a share. The court upheld the larger NTV on two grounds. First, the definition of net tangible value, on true construction, did not make the audited financial statements the sole basis for computation but referred to the employment of those "statements in accordance with generally accepted accounting principles…"; and according to those principles, the revaluation had additionally to be taken into account. But this ground is controversial. The complete expression was "based on the audited financial statements of the company in accordance with generally accepted accounting principles and [practice]" and the latter expression beginning with 'in accordance with' could be qualifying the reference to the audited financial statements of the company, rather than referring to other information that might be taken into account. The second ground was the commercial purpose ground, that it would make no commercial sense, when the exercise of a buy-back option (conditional on failure of listing) could take place a considerable period of time from the date of the stipulated audited accounts, for the parties (who must have known of the absence of revaluation in the audited accounts) to intend to rely solely on the audited accounts. This with respect was a more convincing ground.[107]

The commercial purpose principle is also effective in dealing with patent ambiguities. If the parties issuing and taking out a policy to cover loss of life or disability due to accident agree that "[n]o accident benefit shall be payable if death injury or incapacity shall result directly or indirectly from … wilful exposure to needless peril",[108] what does "wilful exposure to needless peril" mean? There is a spectrum of activities apparently covered by the phrase, ranging from playing football at one end to courting death by standing on the narrow ledge of a high-rise building. But more significantly, this spectrum is divisible into two sets of mutually exclusive entities (for instance, those which are serious and those which are not). Suppose the deceased stepped onto the bumper of a moving car but then the inexperienced driver panicked and lost control of the car (an unforeseeable occurrence), with the result

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106 [1997] 3 S.L.R. 761 (C.A.).

107 Reference may also be made to the dissenting judgment of Chao Hick Tin J.A. in *MCST Plan No 1933*, *supra* note 80. See also McKendrick, *supra* note 80.

108 See for example *Morley and Morley v. United Friendly Insurance plc.* [1993] 1 Lloyd's Rep. 490 (EWCA Civ.).

that the deceased fell to his death. Regard to the commercial purpose will swiftly show whether the risk the deceased ran is an excluded risk. If the purpose of the policy was to provide cover for serious injury, the phrase "wilful exposure to needless peril" would connote exposure to what was foreseen as a risk of serious injury and the foreseeable risk of bruises and abrasions (from falling off the car) would not be an excluded risk.[109]

Once it is allowed that the contextual dependence of words used in contracting is more than an accidental and occasional feature, contrary to the assumptions of the strong theory of meaning, there will be a need to adopt a heuristics capable of narrowing down the contextual dependence to information that will provide the closest fit to what the words mean. If the principle of commercial purpose is a heuristics, the above examples show that it is capable of solving fairly both problems of patent ambiguities and clarity. It would moreover have the merit of obliterating any untenable distinction between the construction of written and oral contracts and ensuring that the process of interpretation is neutral, as it should be, and distinct from the determination of the datum. In *Maggs (trading as B.M. Builders) v. Marsh*,[110] Smith L.J. delivering the leading judgment says that the interpretation of an oral contract is dependent on recollections of the parties which must be tested according to post-contract conduct for the purposes of deciding whose account is correct. These remarks pertain to datum only and should not be understood as concerned with the interpretative process. As a matter of datum, this use of credibility evidence is seen also in the determination of whether the terms of a written contract are entirely written,[111] although once the court concludes that the contract is entirely written, there will be no further interest in whose account is more credible because the exclusion of extrinsic evidence to substitute for the writing entails the irrelevance of such credibility evidence.

III. Commercial Purpose as Rational Instrumentality

It remains only to argue that although the principle of commercial purposes offers a heuristics capable of furnishing satisfying solutions to the interpretative process, it is in fact more than that. It is a principle of rational instrumentality.

Modern theories of interpretation and pragmatics posit a stronger proposition that if communication is directed towards an avowed and shared goal (*i.e.*, it is part of a goal-oriented activity), the ascertainment of meaning will be governed by a principle of rationality, not merely assisted by a heuristic device.[112] There may in many cases of discourse be doubts as to whether in general the goal-orientation is sufficiently clear and whether some goal is shared. But there can be no doubt that the conditions of goal-orientation are satisfied where the making of a contract is concerned. The

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[109] "[Reasonable] means reasonable as between the insured and the insurer having regard to the commercial purpose of the contract, which is *inter alia* to indemnify the insured against liability for his personal negligence.": see *Fraser B. N. Furman (Productions) Ltd. v. Miller Smith & Partners* [1967] [1967] 1 W.L.R. 898 at 905 (EWCA Civ.).

[110] [2006] Build L.R. 395 (EWCA Civ.).

[111] *Moore v. Garwood* (1849) 4 Ex. 681 at 689-690; *Carmichael v. National Power plc.* [1999] 1 W.L.R. 2042 (H.L.).

[112] Otherwise, see David Lewis, "Radical Interpretation" (1974) 27 Synthese 331.

goal-orientation is in fact institutionalised. Parties who communicate with a view to achieving a contract establish a clear institutionalised goal for themselves under an institutionalised framework in which they confer on each other the right to have the judicial interpreter interpret their contract. It would not be wrong to say that the making of a contract is a kind of private quasi-legislative act. In that sense, a private act of interaction with a view to reaching a consensus is not that different from a public legislative act as a speaking language with authority to deprive and reward.

Dascal, in his investigations into the meaning of a legislative text, has demonstrated forcefully that the institutionalised and mediated legal text places relevance and importance on the functional context and the use of fuzzy language.[113] This means first that the text will have to be applied even to circumstances not foreseen or foreseeable by the parties at the time of the creation of it. Secondly, this means that there will be cases "where the meaning of a legislative text is undecidable by any amount of combined linguistic and factual knowledge including the contextual dependence of the sentences used".[114] When that is the case, the creators of the text expect and require the judicial interpreter to perform a genuine act of creative interpretation. This act must also be legitimate; that is why it must be performed in accordance with a principle of rationality, namely that the judicial interpreter shall assign the meaning of the text in accordance with the purposes for which the creators have uttered the text.

These demonstrations are equally applicable to the making of a contract, as a kind of private quasi-legislative act. One is that the contract, like the legislative act which mediates between morals and policies, mediates between private interests with a view to a particular goal. The second is that both take place in institutionalised frameworks which involve recourse to a judicial interpreter. As a result, a contract like the legislative text must be construed purposively, for that is both rational and impartial. The difference is that the principle of rationality in the case of the contract is an instrumental one, namely that the judicial interpreter will seek the advancement of the parties' commercial purpose.

The view that the principle of commercial purposes is entailed is not yet fully acknowledged. In *Antaios Compania S.A.* where the principle of commercial purposes was first broached before and accepted by the House of Lords, Lord Diplock deprecated the "extension of the use of the expression 'purposive construction' from the interpretation of statutes to the interpretation of private contracts".[115] We are also reminded that "[t]here are obvious differences between the process of interpretation in regard to private contracts and public statutes."[116] Again, where the problem has been identified as an application of the contract to events which the parties may not

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[113] Dascal, *supra* note 95 at ch. 15. In connection with the construction of a contract, see Lord Porter in *Yorkshire Dale Steamship Co. Ltd. v. Minister of War Transport* [1942] A.C. 691 at 714 where he said:

> The fact is that there is no form of words in which underwriters and insured can express themselves so as to convey with precision what they mean to include in war risks. Indeed, I do not think that they themselves know exactly what they desire to embrace in the cover furnished, and I fancy that they best convey their intention by using somewhat vague words in which this present clause is expressed, leaving it to the courts by a series of decisions to determine the line of demarcation between the two forms of risk.

[114] *Ibid.* at 334.

[115] *Antaios Cia Naviera*, *supra* note 98 at 201.

[116] *Mannai Investments*, *supra* note 9 at 770 per Lord Steyn.

have foreseen and the principle of commercial purposes is used to yield a solution, the courts say that they are engaged in an artificial process. In *Bromarin v. I.M.D. Investments*, Chadwick L.J. said:

> It is not, to my mind, an appropriate approach to construction to hold that, where the parties contemplated event 'A', and they did not contemplate event 'B', their agreement must be taken as applying only in event 'A' and cannot apply in event 'B'. The task of the court is to decide in the light of the agreement that the parties made, what they must have been taken to have intended to the event, event 'B', which they did not contemplate. That is of course an artificial exercise, because it requires there to be attributed to the parties an intention which they did not have (as a matter of fact) because they did not appreciate the problem which needed to be addressed. But it is an exercise which the courts have been willing to undertake for as long as commercial contracts have come before them for construction.[117]

With respect, so far from being an artificial exercise, the application of the principle of commercial purpose in these circumstances is entailed when the parties have employed fuzzy language in drawing up their contract.[118] When doing so, they appreciate that they may not have specific intentions regarding a particular event 'B' but intend, where the meaning of the contract is not decidable by reference to any amount of linguistic and factual knowledge which is true when they have had no specific intentions about event 'B', that it shall be decided by reference to their commercial purposes. There is nothing artificial about this process at all if the principle of commercial purposes is entailed.

For the avoidance of confusion, the principle of commercial purpose must not be taken as, or as a proxy for, the principle of collective rationality, for the reason that the latter is unattainable. Earlier mention was made of the view that the object of the interpretative process is to foster the collective intention, and thus the expectations aroused by it. While this explanation does in fact distinguish between language which is to order behaviour and language which expresses an experience, private or social, there is an insuperable problem with it. The common intention model simply fails in its premises. Common intention is of two kinds, deliberately collective and spontaneously collective. If we inquire into the formation of the common intention in either sense, we will be confronted by the Impossibility Theorem.[119] Arrow's analysis of the conditions under which collective intention is formed proves that it is impossible to constitute a collective intention out of individual intentions, or to

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[117] [1999] S.T.C. 301 at 310 (EWCA Civ.).

[118] There is no residual gap problem. Hoffman J. (as he then was) in *MFI Properties*, *supra* note 63 at 976 broached this residual prospect in these terms:

> But there will also be cases in which the language used by the parties show beyond doubt that they intended an assumption for which, to a third party who knows nothing of the negotiations, no commercial purpose can be discerned. In such circumstances the court has no option but to assume that it was a quid pro quo for some other concession in the course of negotiations, the court cannot reject it as absurd merely because it is counterfactual and has no outward commercial justification.

In these remarks, however, there is also suggestion that if more is known about the negotiations, much of the mystery about the commercial purpose may be dispelled. With respect, a term may have no outward commercial justification only because the opacity is due to lack of relevant information, which lack may have been due to reliance on a more restrictive notion of the surrounding circumstances than what has been argued for.

[119] Kenneth Arrow, *Social Choice and Individual Values*, 2d ed. (New Haven: Yale University Press, 1963).

put it another way, there is no rational way to construe a collective intention out of entrenched individual intentions. An expectations-based model is deceptive in its constitutive suggestion that collective integration is possible whereas this is only possible where there is unanimity. But the common intention with its objective slant is non-unanimous and the only instance where it can be so is where the collective intention is spontaneously generated without any prior intention to reach consensus being held by either of the two parties. Obviously, a spontaneous collective intention is ruled out as a contract and is of no concern to us here.

IV. A CODA

The need for a principle of rational instrumentality does not imply the redundancy of other heuristics. As was hinted at in the introduction and the discussion in this article, the cases on construction of contracts are now more consistent with presuming reliance on rules of construction, in particular the plain meaning rule, than applying rules of construction. The courts treat the rules as rebuttable and that is quite telling that the rules have transformed into heuristics. This is consistent with the courts regarding the presumed reliance as a distinct interpretative element outside the notion of surrounding circumstances and is not detracted from by the suggestion that the presumption may be stronger when the document entirely contains the contract between the parties.[120] This attitude is correct because when the strong theory is abandoned, rules of convention are merely heuristics for generating hypotheses as to meaning. When some contextual information is resorted to by a party as elucidating the meaning of the contract, the court recognises a possible hypothesis by comparing the meaning based on presumed reliance on rules of convention and the meaning based on the protagonist's contextual information before proceeding to eliminate one or the other by preferring the simpler to the more complex etc.

No interpretation by assistance of a heuristic device is called for where the parties show that they have actually relied on a rule of construction since as we have also seen there is only a matter of datum.[121] With printed standard forms, this reliance may be substantial; sometimes to the extent that "they become the subject of exegesis by the courts so that the way in which they will apply to the adventure contemplated by the charter-party will be understood in the same sense by both parties when they are negotiating its terms and carrying them out".[122] Thus, where there is actual proof that contracting parties have agreed to provide their own dictionary meaning, the datum is settled and no interpretation is necessary.[123] As Lord Hoffmann puts it in *Chartbrook*:

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[120] There are some local cases which take into account the character and degree of experience of a contracting party when deciding whether to apply a rule of construction or a technical meaning with which an experienced businessman might be expected to have become familiar but not a tyro.

[121] See also *Llanelli Railway and Dock Co. v. L.N.W.R.* [1875] 1 App. Cas. 550 at 560.

[122] *Federal Commerce and Navigation Co. Ltd. v. Tradax Export S.A.* [1978] A.C. 1 at 8 (H.L.); see also *The Nema*, *supra* note 19.

[123] An agreement to provide a dictionary meaning or to resolve differences over the meaning by reference to a third party whose determination shall be final will not be regarded as ousting the jurisdiction of the court. See Denning M.R. in *Re Tuck Settlement Trusts* [1978] 1 Ch. 49 at 61 (Ch.).

> [E]vidence may always be adduced that the parties habitually used words in an unconventional sense in order to support an argument that words in a contract should bear a similar unconventional meaning. This is the "private dictionary" principle, which is akin to the principle by which a linguistic usage in a trade or among a religious sect may be proved: compare *Shore v Wilson* (1842) 9 Cl & F 355. For this purpose it does not matter whether the evidence of usage by the parties was in the course of negotiations or on any other occasion. It is simply evidence of the linguistic usage which they had in common.[124]

However, where the parties do not express such an agreement, the question whether there is an implicit agreement to that effect is significant as a matter of heuristics. This, it is submitted, provides a truer explanation why the House of Lords in *Chartbrook* would reject the wider application of the private dictionary principle in *The Karen Oltmann*. In *Chartbrook*, the House of Lords rejected the sweeping application of the idea of an implied agreement to provide a dictionary meaning in *The Karen Oltmann*,[125] where the parties had not said that they agreed on a dictionary meaning. In his judgment in the Court of Appeal, Lawrence Collins L.J. was sceptical of the principle in *The Karen Oltmann* (in paragraph 121).[126] Lord Hoffmann agreed because the telexes in *The Karen Oltmann* did not evidence any unconventional usage. There was merely a choice "between two perfectly conventional meanings of the word "after" in a particular context".[127]

V. Conclusion

Contrary to the supposition that theories of interpretation and pragmatics have little to contribute to the construction of contracts,[128] this article argues that they shed invaluable light on the interpretative process. The conclusions of this article may be summarised as follows:

Rules of construction applied as rules are underpinned by a strong theory of meaning which recognises limited contextual dependence. As a consequence, interpretation is a narrow deductive process of eliminating latent ambiguities.

The surrounding circumstances cannot be defined conceptually because it is a parasitic notion. It takes its character from the purpose for which it is employed. Thus, it may be a matter of datum or the interpretative process.

In relation to the interpretative process, it may be relevant as a deductive or inductive argument or as a heuristic device, alongside the presumed reliance on the rules of construction or as revelatory of the commercial purpose.

The commercial purpose of a contract is not a heuristic device (although it can serve the function of a heuristic device).[129] It supplies a principle of instrumental

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[124] *Chartbrook*, *supra* note 83 at para. 45.

[125] *Supra* note 76. Cf. *Codelfa Construction Pty. Ltd. v. State Rail Authority of New South Wales* (1982) 149 CLR 337 at 352 (H.C.A.).

[126] He doubted whether it differed in any material respect from admitting evidence of prior negotiations in construing a contract. See also David McLauchlan, "Contract Interpretation: What is It About?" (2009) 31 Sydney L. Rev. 5.

[127] *Chartbrook*, *supra* note 83 at para. 45.

[128] See McMeel, *The Construction of Contracts*, *supra* note 12 at para. 2.08.

[129] The failure to appreciate this explains why despite the advantages just described, the commercial purposes approach has its share of detractors. McKendrick's article in the SAcLJ, *supra* note 80, mentions

rationality for deciding cases where the meaning cannot be determined by any amount of combined linguistic and factual knowledge.

If these conclusions are correct, the pre-eminence of rules of construction as endorsed in *Zurich Insurance* and *The Starsin* cannot be supported.[130] Statements as to how the courts construe contracts in accordance with the principle of commercial purposes should not be seen as exceptional although its applicability is not preconditioned by the existence of latent ambiguity in the language.

The attempt to force the principle of commercial purposes into the ill-fitting provisions of the *Evidence Act* is also impossible. The principle is of a substantive nature and the fact that it is produced by the context does not mean that the context which indicates its existence is evidentiary or that the principle is evidentiary.

uncertainty at numerous points and highlights that purposive construction can easily shade into creative construction, and judicial activism. That is why it must be pegged to the surrounding circumstances; it must be based on evidence. Without it there will be academic speculations and conjectures. With respect therefore, the dissenting judgment of Chao Hick Tin J.A. in *MCST Plan No 1933*, *supra* note 80 was correct.

[130] *Cf.* Goff, *supra* note 96 at 388.