
The old rule, the true rule and contract administration notices in construction

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Recently there has been a trend towards a non-technical or commercial approach to contract administration notices in construction. This trend appears driven by a similar approach to the interpretation of contracts, including the progressive creep away from the restriction on examining surrounding circumstances (the Codelfa "true rule"). The High Court of Australia recently breathed life into the true rule, creating an apparent re-divergence of the laws of England and Australia. What does this mean for the approach to contract administration notices in Australia? This article argues that a non-technical approach is still to be preferred, and in the process embarks on a critical analysis of the issues involved in the contract interpretation debate.

INTRODUCTION

Are time bars a necessary evil or a coward's castle?

So much has been written about time bars previously.¹ Suffice to say, it appears to currently be beyond doubt that non-compliance with a notice obligation, where that obligation – properly construed – is a condition precedent to the actual entitlement arising, can be fatal to a contractor's claim.²

Although this premise may be less clear in respect of owner-caused delay, and the related question of whether time bars can overcome the prevention principle (or vice versa),³ it is fair to suggest that a contractor disregards any notice requirement at its peril.⁴

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¹ A detailed analysis of time bars is outside the scope of this article. For further reading, see generally Morton C, "Time Bars and the Condition Precedent" (1995) 11 BCL 302; Bellemore A, "Time Bars and Condition Precedent" (1996) 12 BCL 78; Thomas T, "A Failure to Give Notice and the Defeasibility of Time Bars in Construction Contracts" (2006) 22 BCL 342; Bellemore A, "Variation Claims in the Absence of Required Writing" (2010) 26 BCL 150; Lal H, *The Rise and Rise of Time-Bar Clauses for Contractors' Claims: Issues for Construction Arbitrators*, Society of Construction Law UK Paper No 142 (September 2007); Champion R, *Variations. Time Limits and Unanticipated Consequences*, Society of Construction Law UK Paper No 138 (May 2007); Jones D, "Can Prevention Be Cured by Time Bars" (2009) 26 *International Construction Law Review* 57.

² For examples of where a failure to comply with a time bar defeated a contractor's entitlement, see *Jennings Construction Ltd v QH & M Birt Pty Ltd* (1986) 8 NSWLR 18; *Wormald Engineering Pty Ltd v Resources Conservations Co International* (1992) 8 BCL 158; *Opat Decorating Service (Aust) Pty Ltd v Hansen Yuncken (SA) Pty Ltd* (1995) 11 BCL 360; *John Goss Projects Leighton Contractors* (2006) 66 NSWLR 707.

³ See for example, Jones, n 1; Bailey I, "Concurrency, Causation, Commonsense and Compensation (Part 2)" (2010) 27 *International Construction Law Review* 197.

⁴ Recent discussion and debate over whether the penalties doctrine, as recently clarified in the High Court's decision in *Andrews v Australia and New Zealand Banking Group Ltd* (2012) 247 CLR 205, might apply to time bars is also outside the scope of this article. For suggestions that the penalties doctrine could apply to time bars, see Easton P, "Penalties percolating through the construction industry: *Andrews v Australia and New Zealand Banking Group Ltd*" (2013) 29 BCL 233; Davenport P, "Andrews v ANZ and Penalty Clauses", Presented at seminar of the Adjudication Forum (13 November 2012). For the counter argument that time bars do not attract the penalties doctrine, including that "unfortunately, Mr Davenport's enthusiasm in his own judgment is misplaced", see Bond J, *Message for Adjudicators: Contrary to What You Might Have Heard, a Properly Drafted Contractual Time Bar Will Not Attract the Penalty Doctrine*, Presented to Queensland Law Society/IAMA Annual BCIPA intensive (7 March 2013).

Against this backdrop, the question of whether or not a contractor has in fact complied with a time bar often provides fertile ground for disputes, and can lead to interesting and surprising outcomes.⁵

This article will consider two relatively recent cases where a non-technical approach to contractual notices was taken, and therefore time bars did not defeat the contractors' claims. These cases, *Etlis v New Age Constructions (NSW) Pty Ltd*⁶ and *BMD Major Projects Pty Ltd v Victorian Urban Development Authority*,⁷ both cited with approval the House of Lords decision of *Mannai Investment Co Ltd v Eagle Star Life Assurance Co Ltd*,⁸ in respect of the use of surrounding circumstances to assist in the interpretation of notice provisions and the actual notices themselves.

Mannai is commonly cited, among other cases,⁹ as authority for the broader, commercial approach to interpretation of contracts in England. Importantly, this approach included "quietly dropping" the "old rule" that ambiguity is required before a court can have regard to extrinsic evidence.¹⁰

In recent times, many judges and commentators considered that this broader approach had also become the law in Australia. In particular, it appeared to be understood that the "gateway" requirement for ambiguity, or Mason J's "true rule" laid down in *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales*,¹¹ had been superseded. At the very least, the position was not clear.

This state of flux was recently addressed when the High Court of Australia made its view clear that, in publishing reasons for refusing to grant special leave to appeal in *Western Export Services Inc v Jireh International Pty Ltd*,¹² the true rule is the law of Australia until the High Court – and only the High Court – says otherwise.

This recent development calls for a reconsideration of the approach to interpretation of notices given under construction contracts against the backdrop of time bars. Is reliance on *Mannai* and other English cases wrong, given the apparent re-divergence of the laws in England and Australia? Are *Etlis* and *BMD Major Projects* fruit from a tainted tree?

ETLIS

In *Etlis*, the contractor was engaged to carry out the construction of a house in Paddington, New South Wales, under a Housing Industry Association standard "Plain English Building Agreement". Shortly after commencing work in early September 1997, the contractor encountered an unexpected Telstra cable which stopped excavation. The cable was jointly inspected by the owner and the contractor.

Clause 6 of the contract provided, that in the event of an excusable delay occurring:

the Contractor is entitled to a fair and reasonable extension of time PROVIDED that the owner is notified in writing ... within ten working (10) days of the event.¹³

Ostensibly, the contractor had not provided a notification as required by cl 6 of the contract. However, the referee found that the owner had engaged in discussions with the contractor and

⁵ This article is focused on notices against the backdrop of time bars. Notices in other contexts (for example, notices to show cause or notices of breach) are outside the scope of this article. However, it appears that a non-technical approach also applies to such notices. For example, see *FPM Constructions Pty Ltd v Council of the City of Blue Mountains* [2005] NSWCA 340 at [151].

⁶ *Etlis v New Age Constructions (NSW) Pty Ltd* [2005] NSWCA 165.

⁷ *BMD Major Projects Pty Ltd v Victorian Urban Development Authority* [2007] VSC 409.

⁸ *Mannai Investment Co Ltd v Eagle Star Life Assurance Co Ltd* [1997] AC 749.

⁹ See, particularly *Investors Compensation Scheme Ltd v West Bromwich Building Society* [1998] 1 All ER 98 at [114]-[115] (Lord Hoffmann) including the famous "summary of principles".

¹⁰ *Mannai Investment Co Ltd v Eagle Star Life Assurance Co Ltd* [1997] AC 749 at 776, 779.

¹¹ *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337 at 352.

¹² *Western Export Services Inc v Jireh International Pty Ltd* (2011) 282 ALR 604.

¹³ *Etlis v New Age Constructions (NSW) Pty Ltd* [2005] NSWCA 165 at [12] (emphasis in original).

understood that the contractor would be entitled to extra time. On that basis, the referee concluded that the owners waived their right to rely on compliance with the time bar in cl 6 of the contract in relation to the claim for delay in relation to the Telstra cable. The trial judge accepted this conclusion.

In the New South Wales Court of Appeal, Handley JA (with whom Hodgson JA and Brownie AJA agreed) held that the findings of the referee, and the reasoning of the trial judge, on the waiver and estoppel issues could not be supported because, as a matter of law, there could be no waiver without a communication from the owner which contained a promise or representation that written notification was not required.¹⁴

This was when things got interesting. On appeal, counsel for the contractor relied upon a notice of contention which, among other things, contended that a quotation letter faxed by the contractor on 4 September 1997 was a notice which complied with the time bar in cl 6. That letter stated “we are pleased to submit the following quote for your consideration: Extra cost associated with Telstra cable, including labour and equipment \$27,450”.¹⁵

A further letter from the contractor on 16 September 1997 stated:

3) We also note that due to the Telstra cable the sewer has to be hand excavated, due to this work a lump sum price would not be fair for you or myself, I feel the best alternative is cost plus builder's margin ... Could you please confirm if you would like to proceed with the variations?¹⁶

There was nothing formal or “contractual” about these letters. On their face, the letters did not even suggest that the contractor needed extra time, although the owner in fact knew that the additional work would cause delay. However, the court held that the letters of 4 and 16 September 1997 amounted to sufficient compliance with the time bar in cl 6 of the contract.¹⁷ In doing so, Handley JA said:

Where to the knowledge of both parties the proprietors already have the information that cl 6 requires the builder to communicate the notification need not set this out at length. *In those circumstances the primary purpose of any written notification will be to provide objective evidence to facilitate contract administration and avoid disputes.*

The relevant question is whether the letter of 16 September would convey to a reasonable recipient, *with this background knowledge*, that the building work would be delayed because of the cable. There is no difficulty in so construing this letter. *A non-technical approach to its construction* is supported by *Mannai Investment Co Ltd v Eagle Star Life Assurance Co Ltd* [1997] UKHL 19; [1997] AC 749, 774 where Lord Hoffmann said that the clause in issue “does not require the tenant to use any particular form of words”. This can be said of cl 6. At 767-8 Lord Steyn said:

“The construction of the notices must be approached objectively. The issue is how a reasonable recipient would have understood [them] ... the notices must be construed taking into account the relevant objective contextual scene ... The real question is what evidence of surrounding circumstances may ultimately be allowed to influence the question of interpretation. That depends on what meanings the language read against the objective contextual scene will let in.”¹⁸

Etlis provides a somewhat surprising outcome in light of what the letters of 4 and 16 September 1997 actually said. On their face, the letters appeared to be nothing more than quotations. The letters were casual, not contractual. There is no overt suggestion that additional time was being notified or being claimed. However, the surrounding circumstances were that the owner in fact knew that the contractor was being delayed.¹⁹ A non-technical approach was adopted.

¹⁴ *Etlis v New Age Constructions (NSW) Pty Ltd* [2005] NSWCA 165 at [15]-[16].

¹⁵ *Etlis v New Age Constructions (NSW) Pty Ltd* [2005] NSWCA 165 at [17], [34].

¹⁶ *Etlis v New Age Constructions (NSW) Pty Ltd* [2005] NSWCA 165 at [34].

¹⁷ *Etlis v New Age Constructions (NSW) Pty Ltd* [2005] NSWCA 165 at [40]-[41].

¹⁸ *Etlis v New Age Constructions (NSW) Pty Ltd* [2005] NSWCA 165 at [38]-[39] (emphasis added).

¹⁹ *Etlis v New Age Constructions (NSW) Pty Ltd* [2005] NSWCA 165 at [32] (Handley JA).

The Victorian case of *BMD Major Projects* is a similar example of a business-like (and not overly technical) approach. The two cases illustrate a commonality in approach to notices and compliance with time bars in the construction industry, whether the contract is to build a small house or large scale public infrastructure.

BMD MAJOR PROJECTS

In *BMD Major Projects*, the contractor was engaged to develop a site formerly used as a quarry. The contractor encountered physical conditions on the site which it claimed differed materially from the conditions expected. The contractor's claim was primarily based on a latent conditions clause in the Australian Standard General Conditions of Contract (AS 2124-1992) but was also based on unjust enrichment, breach of contractual warranties and breach of the *Trade Practices Act 1974* (Cth) (as it was then).

The contractor became aware of the differing physical conditions in the last week of July 2002. The contractor's letter, which was argued to be a latent conditions notice under cl 12.2, and a notice of delay and claim for extension of time under cl 35.5, was dated 2 August 2002 but faxed and received on 6 August 2002. The owner contended that the contractor was time barred as it allegedly failed to give notice "forthwith" upon the contractor becoming aware of the latent condition (as required by cl 12.2 of the contract), and that the contractor failed to properly notify and claim for extensions of time (as required by cll 35.5 and 35.5A of the contract).²⁰

The notice

Pagone J considered:

- what was meant by the word "forthwith"; and
- whether the contractor had indeed given its notice forthwith.

In terms of the requirement for a notice to be given "forthwith", Pagone J said:

Provisions like clause 12.2 must be construed in accordance with business common sense: see *McCann v Switzerland Insurance Ltd*; *Pacific Carriers Ltd v BNP Paribas*; *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd*; *Maggbury Pty Ltd v Hafele Australia Pty Ltd*. A stricter construction would encourage, if not compel, contractors to be more concerned with anxiously satisfying a formal temporal requirement of notification rather than to explore the underlying needs and circumstances of the situation.²¹

The word "forthwith" was therefore construed as meaning "without delay" rather than "immediately".

It is important to note that, in considering the relevant issues in coming to his determination, Pagone J cited with approval the House of Lords decision of *Mannai*, just as Handley JA had in *Etlis*.

As to whether a notice given on 6 August 2002, following an event which became known in late July 2002, was "forthwith", Pagone J held that the question depended on the facts and context.²² In this case, the contractor became aware of the situation, gave prompt oral notification, invited the owner and superintendent to inspect the situation, and then sent the formal written notification. On this basis, Pagone J held at that the notice was given "forthwith" as contemplated by the contract and accordingly the contractor was not time barred.²³

Extent of the notice

Like *Etlis* and the quotation letters that were held to be notices of delay, Pagone J in *BMD Major Projects* also gave the letter of 2 August 2002 more breadth than appeared on its face.

A letter that made no mention of a "Quarry Floor Stockpile" (instead referring only to a "Southern

²⁰ *BMD Major Projects Pty Ltd v Victorian Urban Development Authority* [2007] VSC 409 at [10], [70].

²¹ *BMD Major Projects Pty Ltd v Victorian Urban Development Authority* [2007] VSC 409 at [11]. Although Pagone J did not expressly refer to the true rule in *Codelfa*, his Honour obviously decided that the word "forthwith" was capable of more than one meaning, in deciding to adopt one of two alternative meanings.

²² *BMD Major Projects Pty Ltd v Victorian Urban Development Authority* [2007] VSC 409 at [11].

²³ *BMD Major Projects Pty Ltd v Victorian Urban Development Authority* [2007] VSC 409 at [11].

Stockpile”) was held by Pagone J:

on its terms and in the context in which it was sent and received, may fairly be construed as notification not only of the condition in the location then worked on (namely, the Southern Stockpile) but, more broadly, as notification that the natural surface levels were lower on the site at least in the areas proximate or contiguous to the Southern Stockpile.²⁴

Pagone J appeared to draw support for his conclusion from the parties’ conduct after notification, as being consistent with them having seen the notification as broader than the terms of the formal notification. It must be said that it is difficult to reconcile this conclusion with the long-standing principle that post-contractual conduct is not admissible as an aid to construction of a document.²⁵ Nevertheless, it does demonstrate a non-technical, business-like and fair approach.

Pagone J also gave the 2 August 2002 letter more breadth than appeared on its face in determining the contractor’s entitlement to an extension of time. The letter, while mentioning delay and effects on the critical path, did not appear to expressly seek an extension of time. Despite this absence of express reference to a claim, Pagone J held that:

It seems to me that it was clear from the letter dated 2 August 2002 that an extension of time was being claimed. Neither clause 35.5 nor any other clause in the contract requires any particular form of words by which to convey to a reasonable reader that a written claim for an extension of time was being made. In my view a reasonable reader reading the letter dated 2 August 2002 would have been on notice that an extension of time for practical completion was being sought having regard to the then notification that latent conditions had been encountered on “the critical path” and that a delay was anticipated of some four weeks if not longer. Such a construction of the contract, and of the documents which are sought to be relied upon pursuant to the terms of the contract, is consistent with what a reasonable person would understand a document to mean having regard to the purpose and the object of the transaction: see *Pacific Carriers Ltd v BNP Paribas, Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd*.²⁶

Accordingly, the contractor was held to have also complied with the time bars with respect to extensions of time.

This approach was consistent with the approach taken by the New South Wales Court of Appeal in *Ellis*.

It would appear that *Ellis* and *BMD Major Projects* are fruit from the same tree – “Mannai from Heaven” – for those who prefer a modern, commercial, and common sense approach to the interpretation of notices and compliance with time bars under construction contracts. But where does *Mannai* come from, and can it really be relied on in Australia?

MANNAI

Mannai is not a construction law decision. It concerns the construction of a notice to terminate a lease that,²⁷ on its face, had considerable difficulties.

The relevant lease provided that the tenant could terminate the lease, on the third anniversary of the term commencement date, by serving not less than six months notice. The lease commencement date was 13 January 1992. The notice dated 24 June 1994 purported to terminate the lease on 12 January 1995. The third anniversary of the term commencement date was in fact 13 January 1995. There was an inaccuracy in the notice.

²⁴ *BMD Major Projects Pty Ltd v Victorian Urban Development Authority* [2007] VSC 409 at [16].

²⁵ *Agricultural and Rural Finance Pty Ltd v Gardiner* (2008) 238 CLR 570 at [35] (Gummow, Hayne and Kiefel JJ). See also Douglas F, “Modern Approaches to the Construction and Interpretation of Contracts” (2009) 32(2) *Australian Bar Review* 158 at 165.

²⁶ *BMD Major Projects Pty Ltd v Victorian Urban Development Authority* [2007] VSC 409 at [73].

²⁷ There were in fact two leases – one for the office premises and one for a car park. The leases were entered into on the same date and contained identical termination clauses. There were also two identical termination notices given. For convenience, this discussion will assume that there was only one lease and one notice.

The House of Lords reversed the decision of the Court of Appeal,²⁸ and held (by Lord Steyn, Lord Hoffmann and Lord Clyde agreeing, Lord Goff of Chieveley and Lord Jauncey of Tullichettle dissenting) that the notice was effective to terminate the lease.

The Court of Appeal and dissenting judgments – a strict approach

The Court of Appeal had held that the notice was ineffective and relied on the 1942 Court of Appeal decision of *Hankey v Clavering*.²⁹ In *Hankey v Clavering*, a notice was held to be ineffective because it incorrectly specified the date of termination of a lease (as was the case in *Mannai*). The point was considered to be so clear that the judgment was delivered *ex tempore*,³⁰ where Lord Greene MR said:

The whole thing was obviously a slip, and there is a natural temptation to put a strained construction in language in aid of people who have been unfortunate enough to make slips. That, however, is a temptation which must be resisted, because documents are not to be strained and principles of construction are not to be outraged in order to do what may appear to be fair in a particular case.³¹

In dissent in the House of Lords, Lord Goff of Chieveley and Lord Jauncey of Tullichettle took a strict approach, relying on the authority of *Hankey v Clavering*, notwithstanding the apparent unreasonableness of the result. Lord Goff of Chieveley said:

At first sight it seems unreasonable that the notice should not have been effective. It was obvious that the tenant was trying to give an effective notice under that clause ... It is tempting therefore to assist the tenant who has made a mistake of this kind, when it must have been obvious to the landlord that the tenant intended to give an effective notice under the clause. But the difficulty in the way of adopting this approach is that, on the authorities, it is inconsistent with the agreement of the parties as expressed in the clause ... The simple fact is that the tenant has failed to use the right key which alone is capable of turning the lock.³²

It must be said the strict approach adopted in dissent in *Mannai* has parallels with the Australian approach to the limits of business common sense,³³ and most prominently the well-known passage in *Australian Broadcasting Commission v Australian Performing Right Association Ltd* where Gibbs J said (in dissent):

If the words used are unambiguous the court must give effect to them, notwithstanding that the result may appear capricious or unreasonable, and notwithstanding that it may be guessed or suspected that the parties intended something different. The court has no power to remake or amend a contract for the purpose of avoiding a result which is considered to be inconvenient or unjust.³⁴

The majority – a commercial approach

For the majority of the House of Lords (Lord Steyn, Lord Hoffmann and Lord Clyde), the obvious defect in the notice was no impediment to its effect.

The modern commercial approach was adopted; an approach that had already been foreshadowed in earlier English decisions such as *Prenn v Simmonds*³⁵ and *Reardon Smith Line Ltd v Hansen-Tangen*.³⁶ For example, in *Prenn v Simmonds*, Lord Wilberforce said:

²⁸ *Mannai Investment Co Ltd v Eagle Star Life Assurance Co Ltd* [1996] 1 All ER 55.

²⁹ *Hankey v Clavering* [1942] 2 All ER 311.

³⁰ *Mannai Investment Co Ltd v Eagle Star Life Assurance Co Ltd* [1997] AC 749 at 754.

³¹ *Hankey v Clavering* [1942] 2 All ER 311 at 328 cited in *Mannai Investment Co Ltd v Eagle Star Life Assurance Co Ltd* [1997] AC 749 at 754 (Lord Goff).

³² *Hankey v Clavering* [1942] 2 All ER 311 at 753-754.

³³ Lewison K and Hughes D. *The Interpretation of Contracts in Australia* (4th ed, Thomson Reuters, 2012) pp 40-43.

³⁴ *Australian Broadcasting Commission v Australasian Performing Right Association Ltd* (1973) 129 CLR 99 at 109.

³⁵ *Prenn v Simmonds* [1971] 3 All ER 237.

³⁶ *Reardon Smith Line Ltd v Hansen-Tangen* [1976] 1 WLR 989.

The time has long since passed when agreements, even those under seal, were isolated from the matrix of facts in which they were set and interpreted purely on internal linguistic considerations.³⁷

Five years later, in *Reardon Smith*, Lord Wilberforce went further in saying:

In a commercial contract it is certainly right that the court should know the commercial purpose of the contract and this in turn presupposes knowledge of the genesis of the transaction, the background, the context, the market in which the parties are operating.³⁸

In a much shorter judgment, Lord Clyde did not explicitly refer to *Prenn v Simmonds* and *Reardon Smith* but simply found that, on a “fair and reasonable construction of the notice”, the notice satisfied the technical requirements of the clause.³⁹ Lord Clyde did, however, adopt the same principles as expressed in those cases when he said “the standard of reference is that of a reasonable man exercising his common sense in the context and in the circumstances of the particular case”.⁴⁰

Lord Steyn and Lord Hoffmann were more explicit in their adoption of the principles expressed by Lord Wilberforce in *Prenn v Simmonds* and *Reardon Smith*.

Lord Steyn

Lord Steyn said that the construction of such notices should, by analogy, be the same as the construction of commercial contracts. On that basis, Lord Steyn formulated three propositions, including that “in respect of contracts and contractual notices the contextual scene is always relevant”.⁴¹ Lord Steyn said:

The construction of the notices must be approached objectively. The issue is how a reasonable recipient would have understood the notices. And in considering this question the notices must be construed taking into account the relevant contextual scene.⁴²

In considering the strict approach in *Hankey v Clavering*, and whether that approach should be followed in *Mannai*, Lord Steyn said, among other things:

Hankey v Clavering was decided more than half a century ago. Since then there has been a shift from strict construction of commercial instruments to what is sometimes called purposive construction of such documents. ...

It is better to speak of a shift towards commercial interpretation. About the fact of this change to construction there is no doubt. One illustration will be sufficient. In *Antaios Compania Naviera SA v Salen Rederierna AB* [1985] AC 191, 201, Lord Diplock said in a speech concurred in by his fellow Law Lords observed:

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

... the law therefore generally favours a commercially sensible construction. The reason for this approach is that a commercial construction is more likely to give effect to the intention of the parties ... Nowadays, one must substitute for the rigid rule in *Hankey v Clavering* the standard of commercial construction.⁴³

Lord Hoffmann

Lord Hoffmann, considered to be a champion of the modern approach to commercial construction,⁴⁴ adopted a similar approach to Lord Steyn. His starting point was also that the rules for construing

³⁷ *Prenn v Simmonds* [1971] 3 All ER 237 at 239.

³⁸ *Reardon Smith Line Ltd v Hansen-Tangen* [1976] 1 WLR 989 at 995.

³⁹ *Mannai Investment Co Ltd v Eagle Star Life Assurance Co Ltd* [1997] AC 749 at 781.

⁴⁰ *Mannai Investment Co Ltd v Eagle Star Life Assurance Co Ltd* [1997] AC 749 at 782.

⁴¹ *Mannai Investment Co Ltd v Eagle Star Life Assurance Co Ltd* [1997] AC 749 at 768.

⁴² *Mannai Investment Co Ltd v Eagle Star Life Assurance Co Ltd* [1997] AC 749 at 767.

⁴³ *Mannai Investment Co Ltd v Eagle Star Life Assurance Co Ltd* [1997] AC 749 at 770-771.

⁴⁴ Spigelman J, “From Text to Context: Contemporary Contractual Interpretation” (2007) 81 ALJ 322 at 326; Lewison and Hughes, n 33, p 10.

notices given under contracts are the same for construing contracts proper. At least, Lord Hoffmann said that there was no answer to the question of why the rules for the construction of notices should be any different to the rules for the construction of contracts. Accordingly, Lord Hoffmann said:

Commercial contracts are construed in light of all the background which could reasonably have been expected to have been available to the parties in order to ascertain what would objectively have been understood to be their intention: *Prenn v Simmonds* [1971] 1 WLR 1381, 1383. The fact that the words are capable of a literal application is no obstacle to evidence which demonstrates what a reasonable person with knowledge of the background would have understood the parties to mean, even if this compels one to say that they used the wrong words.⁴⁵

This part of Lord Hoffmann's decision was a portent of things to come. One year later Lord Hoffmann went even further in his famous and often-cited summary of principles in *Investors Compensation Scheme Ltd v West Bromwich Building Society*,⁴⁶ which is discussed further below.

Turning to the Court of Appeal's decision, Lord Hoffmann held that the court was bound to, and therefore was correct to follow, *Hankey v Clavering* but that *Hankey v Clavering* should no longer be followed.⁴⁷ In a lengthy consideration of the grounds upon which *Hankey v Clavering* appeared to have been decided, Lord Hoffmann found a "promising clue" in Lord Greene's statement that the notice must "on its face" comply with the terms of the lease.⁴⁸ Lord Hoffmann then considered that this reference to a document "on its face" must be based on:

an *old rule* about the admissibility of extrinsic evidence to construe legal documents. In its pure form, the rule was said to be that if the words of the document were capable of referring *unambiguously* to a person or thing, no extrinsic evidence was admissible to show that the author was using them to refer to something or someone else.⁴⁹

Lord Hoffman said "this extraordinary rule of construction is, as it seems to me, the only explanation for the decision in *Hankey v Clavering*", and that the rule was "highly artificial and capable of producing results which offend against common sense".⁵⁰ There appeared to be no doubt at all to Lord Hoffmann that "in the case of commercial contracts, the restriction on the use of background has been quietly dropped".⁵¹

THE OLD RULE AND THE TRUE RULE

The old rule, as described by Lord Hoffmann in *Mannai*, will be strikingly familiar to those interpreting contracts in Australia, although it is known by a different name, the true rule.

In Australia, the true rule as to the admissibility of evidence of surrounding circumstances to aid contract interpretation was set out by Mason J in *Codelfa*:

The true rule is that evidence of surrounding circumstances is admissible to assist in the interpretation of the contract if the language is ambiguous or susceptible of more than one meaning. But it is not admissible to contradict the language of the contract when it has a plain meaning.⁵²

Codelfa has not been overruled by the High Court of Australia.

Lord Hoffmann could not have made his opinion on this rule – whether it is called a true rule or an old rule – any clearer.

Theory and practice

The practical challenges of applying the true rule are stark.

⁴⁵ *Mannai Investment Co Ltd v Eagle Star Life Assurance Co Ltd* [1997] AC 749 at 779.

⁴⁶ *Investors Compensation Scheme Ltd v West Bromwich Building Society* [1998] 1 All ER 98 at 114-115.

⁴⁷ *Mannai Investment Co Ltd v Eagle Star Life Assurance Co Ltd* [1997] AC 749 at 773, 780.

⁴⁸ *Mannai Investment Co Ltd v Eagle Star Life Assurance Co Ltd* [1997] AC 749 at 776.

⁴⁹ *Mannai Investment Co Ltd v Eagle Star Life Assurance Co Ltd* [1997] AC 749 at 776 (emphasis added).

⁵⁰ *Mannai Investment Co Ltd v Eagle Star Life Assurance Co Ltd* [1997] AC 749 at 777-778.

⁵¹ *Mannai Investment Co Ltd v Eagle Star Life Assurance Co Ltd* [1997] AC 749 at 779.

⁵² *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* (1982) 149 CLR 337 at 352.

For starters, “few, if any, English words are unambiguous or not susceptible of more than one meaning or have a plain meaning”.⁵³ The richness of the English language itself means that, although it is helpful for pursuits such as literature and poetry, the language is difficult to express precisely in order to control future conduct in a legal document.⁵⁴

In addition, it has also been said that, due to the strictness of the true rule, Australian courts have been “generally quite generous” in finding the existence of ambiguity as a gateway to admit evidence of the relevant background.⁵⁵

Even if there is no ambiguity, at a practical level the courts are rarely divorced from the surrounding circumstances. In reality, it is rare to see a case pursued solely based on construction of the written instrument; more common is for alternative bases such as implied terms, rectification and/or estoppel also to be plead, all of which contain no such restriction on admission of extrinsic evidence. When life closes a door, it opens a window. This tension has not gone unnoticed:

Obviously, the principles excluding parol evidence of subjective intention ... have as their aim the exclusion of evidence which may unduly interfere with the construction of a written document against its relevant background.

The question as yet unresolved at the highest level in this area is how to achieve that objective without excluding what would otherwise be thought to be relevant and persuasive evidence. After all, prior drafts of written agreements would be admissible in a rectification suit as would oral evidence of what the parties intended. Courts generally manage to quickly sort out what is relevant and irrelevant in such circumstances.⁵⁶

Therefore, given all of these challenges, it is fair to question whether rigid adherence to the true rule is even practical or necessary. In modern times, the true rule appears to be an artificial construct where, at least at a practical level, there are more “exceptions that prove the rule” than there are clean applications of the rule.

HAS AUSTRALIA ALSO “QUIETLY DROPPED” THE TRUE RULE?

Investors Compensation Scheme

The year after the judgment in *Mannai* was delivered, Lord Hoffmann gave his well-known “restatement of principles”⁵⁷ in *Investors Compensation Scheme*. Lord Hoffmann said that the fundamental move towards commercial construction, particularly as a result of Lord Wilberforce’s speeches in *Prenn v Simmonds* and *Reardon Smith*, was not always sufficiently appreciated and that “almost all the old intellectual baggage of ‘legal’ interpretation has been discarded”.⁵⁸

Consistent with *Mannai* and the English cases preceding it, the admissibility of background in Lord Hoffmann’s restatement of principles in *Investors Compensation Scheme* was not subject to any old rule in respect of ambiguity. Among other things, Lord Hoffmann’s restatement also significantly expanded the scope of admissible background as including “absolutely anything which would have affected the way in which the language of the document would have been understood by a reasonable man”.⁵⁹

Australian application

The High Court has cited *Investors Compensation Scheme*, and examined surrounding circumstances without first identifying ambiguity in the language of the contract, in *Maggbury Pty Ltd v Hafele*

⁵³ *Manufacturers’ Mutual Insurance Ltd v Withers* (1988) 5 ANZ Ins Cases 60-853 at 75,343 (McHugh JA) cited in Lewison and Hughes, n 33, p 113.

⁵⁴ Kirby M, “Towards a Grand Theory of Interpretation: The Case of Statutes and Contracts” (2003) 24(2) *Statute Law Review* 95.

⁵⁵ Lewison and Hughes, n 33, p 113.

⁵⁶ Douglas, n 25 at 164.

⁵⁷ Lewison and Hughes, n 33, p 10.

⁵⁸ *Investors Compensation Scheme Ltd v West Bromwich Building Society* [1998] 1 All ER 98 at 114.

⁵⁹ *Investors Compensation Scheme Ltd v West Bromwich Building Society* [1998] 1 All ER 98 at 114.

*Australia Pty Ltd*⁶⁰ and *Pacific Carriers Ltd v BNP Paribas*.⁶¹ The High Court then cited its decision in *Pacific Carriers*, and again examined surrounding circumstances without first finding ambiguity, in *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd*⁶² and *International Air Transport Association v Ansett Australia Holdings Ltd*.⁶³

Australia appeared to be left with a strange situation where English decisions such as *Investors Compensation Scheme* were cited with approval, but not distinguished from the Australian approach. This approach has been confusing.⁶⁴ Where did this leave the true rule?

The resulting confusion

In 2007, the Hon Jim Spigelman AC, then Chief Justice of New South Wales, writing extra-judicially, said:

One of the problems that arise from time to time is that the High Court does not always tell you that it is in fact departing from its earlier judgments. This may well have occurred in this context with respect to [the true rule in] *Codelfa*. In any event, I remain of the view that Mason J was not intending to use “ambiguity” in a narrow sense.⁶⁵

After considering the development of the law of contractual interpretation in England led by Lord Hoffmann, and the extent to which those same English cases have been cited in Australia, Spigelman said that “the High Court has either abandoned that part of *Codelfa* [the true rule] or acknowledged that it should never have been understood as so confined” and that the true rule “has been superseded, without being overruled”.⁶⁶

This conclusion was consistent with that of Francis Douglas QC, who said:

The shift from a strict construction of contracts, particularly commercial contracts to a more purposive construction is now an accepted development in the law of the United Kingdom and Australia.⁶⁷

Having said that, the position was not – and is not – clear cut. Lewison and Hughes, in their leading text, *The Interpretation of Contracts in Australia*, identified that although the position in Australian law appeared to be moving in the direction of the English approach, there remained significant authority to the contrary and that “the question is unlikely to be resolved until it is settled by the High Court”.⁶⁸

The approach of the intermediate appellate courts has been mixed. The Full Court of the Federal Court, in *Lion Nathan Australia Pty Ltd v Coopers Brewery Ltd*, held that ambiguity was no longer a precondition to the consideration of surrounding circumstances, based on a consideration of the High Court’s reasons in *Pacific Carriers* and *Toll v Alphapharm*.⁶⁹

⁶⁰ *Magbury Pty Ltd v Hafele Australia Pty Ltd* (2001) 210 CLR 181 at [11] (Gleeson CJ, Gummow and Hayne JJ).

⁶¹ *Pacific Carriers Ltd v BNP Paribas* (2004) 218 CLR 451 at [22] (Gleeson CJ, Gummow, Hayne, Callinan and Heydon JJ).

⁶² *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* (2004) 219 CLR 165 at [40] (Gleeson CJ, Gummow, Hayne, Callinan and Heydon JJ).

⁶³ *International Air Transport Association v Ansett Australia Holdings Ltd* (2008) 234 CLR 151 at [53] (Gummow, Hayne, Heydon, Crennan and Kiefel JJ).

⁶⁴ See generally Cleary S and Radojevic S, “Surrounding Circumstances: What is the ‘True’ True Rule?” (2012) *Australian Construction Law Bulletin* 80.

⁶⁵ Spigelman, n 44 at 330.

⁶⁶ Spigelman, n 44 at 328-329.

⁶⁷ Douglas, n 25 at 158.

⁶⁸ Lewison and Hughes, n 33, pp 7-10.

⁶⁹ *Lion Nathan Australia Pty Ltd v Coopers Brewery Ltd* (2006) 236 ALR 561 at [45]-[61] (Weinberg J), [101] (Kenny J), [250]-[251] (Lander J).

The New South Wales Court of Appeal, in *Masterton Homes Pty Ltd v Palm Assets Pty Ltd*⁷⁰ and *Franklins Pty Ltd v Metcash Trading Ltd*⁷¹ reached a similar, even “stronger”,⁷² position on the issue. For example, in *Masterton Homes*, President Allsop (with whom Basten J agreed) said:

Unless and until the High Court identifies and corrects any perceived error in the approach taken by intermediate courts of appeal ... the position should be taken that the identification of ambiguity is not a precondition for examining contextual and background material otherwise legitimate to examine in furtherance of the construction and interpretation of a written contract.⁷³

His Honour was even more strident in *Franklins* where he said:

The state of the law in this respect is to be ascertained from a number of High Court cases: *Maggbury Pty Limited v Hafele Australia Pty Limited* [2001] HCA 70; 210 CLR 181 at 188 [11]; *Pacific Carriers v BNP Paribas* at 461-462 [22]; *Zhu v Treasurer of the State of New South Wales* [2004] HCA 56; 218 CLR 530 at 559 [82]; *Toll (FGCT) v Alphapharm* at 179 [40] and *International Air Transport Association v Ansett Australia Holdings Limited* [2008] HCA 3; 234 CLR 151 at 160 [8] and 174 [53]. *These cases are clear. ... There is no place in that structure, so expressed, for a requirement to discern textual, or any other, ambiguity in the words of the document before any resort can be made to such evidence of surrounding circumstances.*⁷⁴

The adoption of *Investors Compensation Scheme* by the High Court in the decisions identified above, and relied upon in *Lion Nathan*, *Masterton Homes* and *Franklins*, can be contrasted with the High Court’s warning given in *Royal Botanic Gardens and Domain Trust v South Sydney City Council* that other Australian courts, if they discern any inconsistency between *Investors Compensation Scheme* and *Codelfa*, should continue to follow *Codelfa*.⁷⁵ This warning was reiterated in a footnote by Heydon and Crennan JJ in *Byrnes v Kendle*.⁷⁶

Clearly, some Australian courts did not heed these warnings. On the other hand, the Queensland Court of Appeal did. For example, in *Velvet Glove Holdings Pty Ltd v Mount Isa Mines Ltd*, Philippides J (with whom Fraser and White JJA agreed), held that:

Although that statement [in *Toll v Alphapharm*] involves an endorsement of the first principle summarised by Lord Hoffman in *Investors Compensation Scheme Ltd*, this Court must bear in mind the caution issued by the High Court in *Royal Botanic Gardens*. That warning was reiterated in *Byrnes v Kendle* [2011] HCA 26 by Heydon and Crennan JJ (at fn 135) who observed in particular that the opinions stated in *Masterton Homes Pty Ltd v Palm Assets Pty Ltd* [2009] NSWCA 234; (2009) 261 ALR 382 at 384-385 [1]-[4] and 406-407 [112]-[113] and *Franklins Pty Ltd v Metcash Trading Ltd* [2009] NSWCA 407; (2009) 76 NSWLR 603 at 616-618 [14]-[18], 621-622 [42], 626 [63] and 663-678 [239]-[305] must be read in the light of the High Court’s caution in *Royal Botanic Gardens*.⁷⁷

In *Velvet Glove*, the Queensland Court of Appeal applied the true rule by not permitting resort to extrinsic evidence. The language in the contract, when looked at in its entirety, was not ambiguous or capable of more than one meaning.⁷⁸

The inconsistency between the various Australian courts’ approaches to the true rule is not satisfactory. The late Lord Chief Justice of England and Wales, Thomas Bingham, set out seven

⁷⁰ *Masterton Homes Pty Ltd v Palm Assets Pty Ltd* (2009) 261 ALR 382.

⁷¹ *Franklins Pty Ltd v Metcash Trading Ltd* (2009) NSWLR 603.

⁷² Lewison and Hughes, n 33, pp 114-116.

⁷³ *Masterton Homes Pty Ltd v Palm Assets Pty Ltd* (2009) 261 ALR 382 at [3].

⁷⁴ *Franklins Pty Ltd v Metcash Trading Ltd* (2009) NSWLR 603 at [14] (emphasis added).

⁷⁵ *Royal Botanic Gardens and Domain Trust v South Sydney City Council* (2002) 240 CLR 45 at [39] (Gleeson CJ, Gaudron, McHugh, Gummow and Hayne JJ).

⁷⁶ *Byrnes v Kendle* (2011) 243 CLR 253 at footnote 155.

⁷⁷ *Velvet Glove Holdings Pty Ltd v Mount Isa Mines Ltd* (2012) 28 BCL 351 at [96].

⁷⁸ *Velvet Glove Holdings Pty Ltd v Mount Isa Mines Ltd* (2012) 28 BCL 351 at [103].

criteria by which a legal system should be assessed.⁷⁹ The first was that the law should be accessible, intelligible, clear and predictable. The various Australian courts' approaches have been anything but intelligible, clear and predictable.

Ironically, given some of the issues identified above, it is at least arguable that the existence of the true rule itself creates more confusion and risk of disagreement, the very "mischief" that the rule is intended to limit.⁸⁰

An urgent need has even been identified for the High Court to issue its own summary of principles of contract interpretation for the guidance of lower courts.⁸¹ Very shortly thereafter, the High Court did indeed make its views clear, although not in the form of binding precedent.

RESURRECTION OF THE TRUE RULE

Western Export Services

In *Western Export Services*,⁸² the High Court considered a special leave application against the decision of the New South Wales Court of Appeal. Counsel for the applicants said:

[The High Court's general statements, post-*Codelfa*] stand as, obviously in themselves, authoritative statements for what they say. In our submission, on their face, what they say is inconsistent with the rigid notion of a gateway through which the matter should pass ...

The very importan[t], not quite talismanic, but approaching it, quality of Justice Mason's reasons in *Codelfa*, in our submission, add to rather than detract from the desirability of a grant of special leave in this case.⁸³

The High Court (Gummow, Heydon and Bell JJ) refused to grant special leave.

A refusal to grant special leave "creates no precedent and is binding on no one".⁸⁴ Nevertheless, the High Court in *Western Export Services* took the unusual step of publishing its reasons, and in doing so made its current position on the true rule very clear, including where the court said:

Acceptance of the applicant's submission, clearly would require reconsideration by this Court of what was said in *Codelfa Construction Pty Ltd v State Rail Authority (NSW)* by Mason J, with the concurrence of Stephen J and Wilson J, to be the "true rule" as to the admission of evidence of surrounding circumstances. Until this Court embarks upon that exercise and disapproves or revises what was said in *Codelfa*, intermediate appellate courts are bound to follow that precedent. The same is true of primary judges, notwithstanding what may appear to have been said by intermediate appellate courts.

The position of *Codelfa*, as a binding authority, was made clear in the joint reasons of five Justices in *Royal Botanic Gardens and Domain Trust v South Sydney City Council* and it should not have been necessary to reiterate the point here.⁸⁵

The High Court's displeasure with intermediate appellate courts' judgments to the contrary was palpable.

⁷⁹ Bingham T, *The Rule of Law* (Allen Lane, 2010) cited in Ferguson N, *The Great Degeneration: How Institutions Decay and Economies Die* (Allen Lane, 2012) p 79.

⁸⁰ For example, in *Western Export Services Inc v Jireh International Pty Ltd* [2011] HCATrans 297 Gummow J said, defending the true rule at [80]-[95]: "In this activity there is great mischief because the wider this net is thrown the greater the possibility of litigation and disagreement and expense in circumstances where ordinary contracts pass into the hands of all sorts of third parties who are expected to be able, on the faith of *Codelfa*, because they think that words mean what they say."

⁸¹ McLauchlan D and Lees M, "Construction Controversy" (2011) 28 *Journal of Contract Law* 101 at 119.

⁸² *Western Export Services Inc v Jireh International Pty Ltd* (2011) 282 ALR 604.

⁸³ *Western Export Services Inc v Jireh International Pty Ltd* [2011] HCATrans 297 at [225]-[240].

⁸⁴ *North Ganalanja Aboriginal Corp v Queensland* (1996) 185 CLR 595 at 643 (McHugh J).

⁸⁵ *Western Export Services Inc v Jireh International Pty Ltd* (2011) 282 ALR 604 at [3]-[4] (emphasis added).

Since *Western Export Services*

The intermediate appellate courts' reaction since *Western Export Services* has been interesting. A strict return to the true rule has been acknowledged in some cases, whereas two recent decisions from the New South Wales Court of Appeal may have gone too far in disregarding the High Court's firm views that *Codelfa* remains binding precedent.

In *Hancock Prospecting Pty Ltd v Wright Prospecting Pty Ltd*, the Western Australian Court of Appeal (McClure P, with whom Newnes JA and Le Miere J agreed) expressly noted *Western Export Services*. The court applied *Codelfa* in finding that an agreement was "unambiguously clear".⁸⁶

Similarly, in *Current Images Pty Ltd v Dupack Pty Ltd*,⁸⁷ the New South Wales Court of Appeal (Bathurst CJ, with whom Macfarlan JA and Sackville AJA agreed) also expressly noted *Western Export Services* and the true rule in *Codelfa*. However, in this case the court found that the ambiguities and internal inconsistencies in the agreement permitted consideration of the surrounding circumstances objectively known to the parties at the time of entry into the agreement.⁸⁸

The faithful adoption of the High Court's dicta in *Western Export Services* in those cases, almost as though a High Court decision to refuse special leave carried the weight of binding precedent, contrasts powerfully with the more recent New South Wales Court of Appeal decisions of *OneSteel Manufacturing Pty Ltd v BlueScope Steel (AIS) Pty Ltd*⁸⁹ and *Schwartz v Hadid*.⁹⁰

In *OneSteel v Bluescope*, neither the decision in *Western Export Services* nor the true rule rated a single mention. Allsop P (with whom Macfarlan and Meagher JJA agreed) referred to the "proper approach to the construction of commercial contracts" as his Honour had previously discussed in *Franklins v Metcash*.⁹¹ This reference was made notwithstanding, and without any acknowledgement of the High Court's disapproval of *Franklins* in *Western Export Services*. Allsop P referred to the decision of *Codelfa*, but only in respect of Mason J's endorsement of Lord Wilberforce's famous statement in *Reardon Smith* that it is essential to understand the "genesis of the transaction, the background, the context, the market in which the parties are operating".⁹² No mention is made that Mason J's endorsement of the English approach was subject to the true rule so expressed. Indeed, Allsop P conducted a lengthy consideration of the factual background to the agreements and the dispute without having expressly identified that the language in the agreements was ambiguous. However, and to be fair, it is submitted that the language in the agreements was in fact ambiguous. The gateway requirement in *Codelfa* may well have been easily satisfied in that case, had Allsop P expressly turned his mind to the question.⁹³

In *Schwartz v Hadid*, the decision of *Western Export Services* is cited, but only to suggest that the Court of Appeal has not decided whether or not it should be bound by it.

Macfarlan and Meagher JJA held that, due to the facts in that case, it was unnecessary to consider the authority of *Western Export Services*,⁹⁴ and whether the court was correct to conclude in *Franklins* that the identification of ambiguity is not a precondition to examining evidence of surrounding

⁸⁶ *Hancock Prospecting Pty Ltd v Wright Prospecting Pty Ltd* (2012) 294 ALR 550 at [82] (McClure P).

⁸⁷ *Current Images Pty Ltd v Dupack Pty Ltd* [2012] NSWCA 99.

⁸⁸ *Current Images Pty Ltd v Dupack Pty Ltd* [2012] NSWCA 99 at [32], [48] (Bathurst CJ).

⁸⁹ *OneSteel Manufacturing Pty Ltd v BlueScope Steel (AIS) Pty Ltd* [2013] NSWCA 27.

⁹⁰ *Schwartz v Hadid* [2013] NSWCA 89.

⁹¹ *OneSteel Manufacturing Pty Ltd v BlueScope Steel (AIS) Pty Ltd* [2013] NSWCA 27 at [13].

⁹² *OneSteel Manufacturing Pty Ltd v BlueScope Steel (AIS) Pty Ltd* [2013] NSWCA 27 at [13].

⁹³ *OneSteel Manufacturing Pty Ltd v BlueScope Steel (AIS) Pty Ltd* [2013] NSWCA 27 at [61]. Allsop P noted "that there is one true meaning does not detract from the pervasive reality that a contract will often have potentially more than one meaning, that words are inherently contextual in their meaning and that reasonable minds often differ about what is the true meaning". This is the closest his Honour came to identifying expressly any ambiguity, and he did not appear to feel the need to do so before his detailed analysis of the factual background at [6]-[38].

⁹⁴ *Schwartz v Hadid* [2013] NSWCA 89 at [37].

circumstances.⁹⁵ Although Basten JA took a different view on the application of principles to the facts of the case, and therefore delivered a dissenting judgment, his Honour expressly agreed with the statement of principles expressed by Meagher JA.⁹⁶

Although *Western Export Services* is not binding precedent, the High Court could not have been any clearer in its reasons as to the approach it expects intermediate appellate courts to adopt. *Schwartz v Hadid* is a fairly clear, but polite, refusal by the New South Wales Court of Appeal to immediately follow *Western Export Services*.

It is difficult to predict whether *OneSteel v Bluescope* and *Schwartz v Hadid* are rogue decisions. The High Court might not have been impressed, particularly given how vehemently its views were expressed in *Western Export Services*. However, the decisions at least highlight that the application of the true rule in Australia remains unpredictable and turbulent.

What if the background was different?

One particularly interesting aspect of the High Court's refusal to grant special leave to appeal in *Western Export Services* was its final statement:

However, the result reached by the Court of Appeal in this case was correct. Further, even if, as the applicant contends, cl 3 in the Letter of Agreement should be construed as understood by a reasonable person in the position of the parties, with knowledge of the surrounding circumstances and the object of the transaction, the result would have been no different.⁹⁷

It is strange that the High Court appears to have considered the surrounding circumstances anyway, albeit in passing, notwithstanding the restriction from doing so due to the binding true rule that the court so vehemently defended. This appears to support the observation above that, at a practical level, it is nearly impossible to divorce the courts from surrounding circumstances.

The court's election to essentially vindicate its decision by referring to the surrounding circumstances is similar to the comment of Baroness Hale in *Charbrook v Persimmon Homes*, although the outcome was different in that case:

But I have to confess that I would not have found it quite so easy to reach this conclusion had we not been made aware of the agreement which the parties had reached on this aspect of their bargain during the negotiations which led up to the formal contract. On any objective view, that made the matter crystal clear.⁹⁸

Therefore, the final statement by the High Court in *Western Export Services* provides some hope that the court may have been inclined to properly reconsider the true rule in an appropriate case. Until then, the application of the true rule in Australia remains, in many respects, unintelligible, unclear and unpredictable, offending the first test of Thomas Bingham's criteria for the assessment of a legal system.

COMMERCIAL APPROACH TO NOTICES RECONSIDERED

Where does all of this analysis take us with respect to notices?

The rules for interpreting contract administration notices appear not to be different from the rules for interpreting contracts proper. *Mannai* is one of a family of English cases that has "quietly dropped" the old rule against admitting extrinsic evidence to construe documents. In Australia, the position is far less clear but the High Court recently in *Western Export Services*, albeit not as binding precedent, very loudly picked the same true rule back up again.

The result is confusing.

Australian reliance on *Mannai*, and indeed any English case adopting a broader commercial approach, appears to be under threat when, at least based on the divergence highlighted above, *Mannai*

⁹⁵ *Schwartz v Hadid* [2013] NSWCA 89 at [85].

⁹⁶ *Schwartz v Hadid* [2013] NSWCA 89 at [3].

⁹⁷ *Western Export Services Inc v Jireh International Pty Ltd* (2011) 282 ALR 604 at [6] (Gummow, Heydon and Bell JJ).

⁹⁸ *Charbrook v Persimmon Homes* [2009] 1 AC 1101 at [33].

may have had a different outcome if it was decided in Australia. Recall that there was nothing ambiguous about the notice to terminate the lease. The date of “12 January 1995” is not capable of more than one meaning.

This analysis is analogous to the suggestion by Professor David McLauchlan that *Investors Compensation Scheme*, although widely cited in Australia, may itself have been decided differently in Australia.⁹⁹

However, it might not be as simple as that, at least insofar as notices are concerned.

The decision in *Mannai* appears to be based, at least partly, on the premise that the rules for interpreting notices given under commercial contracts should not be different to the rules for interpreting commercial contracts.¹⁰⁰ But notices given under contracts, at least construction contracts, are different. There is no compelling reason for the true rule to apply to such notices.

Does the true rule even apply for administration notices?

The rationale for the true rule “gateway” from *Codelfa* appears to be predominantly grounded on the needs for certainty and to reduce the cost of litigation.

The Hon Jim Spigelman AC said that the drive from text to context in contractual interpretation might explain why counsels’ briefs that were once delivered tied in pink ribbon now come in multiple trolleys.¹⁰¹ The interests of third parties in a commercial contract, and the reliance of third parties on the language of the text of a contract, are matters entitled to significant weight.¹⁰² Indeed, the interests of third parties appeared to be at the forefront of the Justices’ minds in their stinging rebuke of the applicant’s attempt at “white-anting *Codelfa*”¹⁰³ in the *Western Export Services* special leave to appeal:

In this activity there is great mischief because the wider this net is thrown the greater the possibility of litigation and disagreement and expense in circumstances where ordinary contracts pass into the hands of all sorts of third parties who are expected to be able, on the faith of *Codelfa*, because they think that words mean what they say... [contracts] have to be shown to bankers, they have to be shown to revenue authorities, they have to be shown to subcontractors, so on and so forth.¹⁰⁴

Fair enough. But do any of these considerations even apply to a contract administration notice in construction, particularly where a time bar is involved?

In considering the policy reasons which supported the old rule, Lord Hoffmann in *Mannai* said:

There are documents in which the need for certainty is paramount and which admissible background is restricted to avoid the possibility that the same document may have different meanings for different people according to their knowledge of the background... But the reasons of policy which require the restriction on background ... do not apply to notices given pursuant to clauses in leases.¹⁰⁵

Similarly, policy reasons that support the true rule can hardly be said to apply to notices given under construction contracts in compliance with a time bar.

In construction contracts, the notice, although often a condition precedent to an entitlement arising, is not itself determinative of the entitlement. It might be described as a different type of “gateway”. The heavy contract administration begins after the giving of the notice. The notice highlights the existence of the issue so that the proper and considered contract administration can take place. For example, take a notice of delay or claim for extension of time. The contractor may assert that it is entitled to 50 days extension of time. It is a matter for the owner or superintendent – or

⁹⁹ McLauchlan D, “Plain Meaning and Commercial Construction: Has Australia Adopted the ICS Principles?” (2009) 25 *Journal of Contract Law* 7.

¹⁰⁰ *Mannai Investment Co Ltd v Eagle Star Life Assurance Co Ltd* [1997] AC 749 at 767 (Lord Steyn), 779 (Lord Hoffmann).

¹⁰¹ Spigelman, n 44 at 334.

¹⁰² Spigelman, n 44 at 334-335.

¹⁰³ *Western Export Services Inc v Jireh International Pty Ltd* [2011] HCATrans 297 at [70] (Gummow J).

¹⁰⁴ *Western Export Services Inc v Jireh International Pty Ltd* [2011] HCATrans 297 at [80]-[95] (Gummow J).

¹⁰⁵ *Mannai Investment Co Ltd v Eagle Star Life Assurance Co Ltd* [1997] AC 749 at 767, 779.

ultimately an arbitrator or a court – to determine whether the delaying event in fact occurred and, if so, the effect that the delay in fact had. The quantum of the extension on the face of the claim, and indeed anything on the face of the claim at that time, is arguably not relevant.

In those circumstances, the notice (on its face) is not important, other than to satisfy a gateway requirement. Issues of cost and the interests of third parties can hardly be said to come into the equation. Therefore, the requirement for ambiguity on the face of a notice before one may have regard to surrounding circumstances appears to simply not be required. Ambiguity or otherwise, surrounding circumstances are absolutely essential to the determination of the claim and a proper consideration of whether the notice in fact complied with the contract.

Surrounding circumstances and purpose and object

The purpose of a notice in construction contract administration is essentially to promote timely attention to the issue raised. Notices provide an opportunity for the parties to consider how best to proceed, enable the contractor to claim in an orderly manner, and promote early issue resolution and dispute avoidance.¹⁰⁶

Having said that, notices are not given in a vacuum. The owner or superintendent knows – or at least ought to know – a lot more than what is written on a piece of paper. For example, in relation to delay notices:

The objective ... is to inform the owner of the possible consequences of a delay event so that appropriate action might be taken. Where the delay event is within the knowledge of the owner, this imperative is at least partially satisfied. Other communications, emails and site minutes, for example, might add to the owner's knowledge and understanding of the consequences. In these circumstances it is at least arguable that a degree of "business common sense" should be applied when consideration is given to whether the totality of the information provided by the contractor satisfies the notice provision.¹⁰⁷

Similarly, in *Brewarrina Shire Council v Beckhaus Civil Pty Ltd*, the dissenting reasons of Young CJ highlighted the superintendent's role, albeit in the context of a clause relating to progress payments:

One must also consider the context in which the clause occurs. The contract gives to the Superintendent quite copious rights to be informed of what is to be occurring on the site. To cite a selection of clauses in the contract, although the Contractor has position of the site, the Superintendent has ample rights of access under clause 27.2, he has the power to direct the Contractor to supply details of the source of the materials it is employing in the works (clause 29.3), he may direct the Contractor to remove what he considers to be defective work (clause 30.3), he may order tests to be carried out (clause 31.1). Furthermore, under clause 33.1 the Superintendent may direct in what order the work is to be performed, he has considerable input into the construction program (clause 33.3) and he is in control of the variations to be affected (clause 40.1).¹⁰⁸

This analysis can be extended to all matters of contract administration concerning an owner or superintendent. The conclusion of Young CJ is consistent with the common sense, and not overly technical, approach in *Etlis*. There are two parties to a contract. The objective intention of the parties must be that the owner or superintendent, not just the contractor, should know what is going on:

To me, these provisions show the parties contractual intent that the Superintendent is able to be and expected to be au fait with the works and their progress at all times.¹⁰⁹

Unfortunately, the majority decision in *Brewarrina* is authority for the proposition that if the superintendent cannot issue a progress certificate due to lack of information, he should not issue one at

¹⁰⁶ Jones, n 1 at 63.

¹⁰⁷ Bailey, n 3 at 205.

¹⁰⁸ *Brewarrina Shire Council v Beckhaus Civil Pty Ltd* (2003) 56 NSWLR 576 at [72]-[73].

¹⁰⁹ *Brewarrina Shire Council v Beckhaus Civil Pty Ltd* (2003) 56 NSWLR 576 at [74].

all. This has been the subject of some criticism.¹¹⁰ Nevertheless, it is argued that the dissenting judgment of Young CJ is a useful summary of the context in which contract administration notices are given and received and “the market in which the parties are operating”.¹¹¹ The owner’s or superintendent’s actual knowledge form part of the surrounding circumstances against which a contractual notice should be interpreted in determining whether a time bar has been complied with.

Etlis and BMD Major Projects reconsidered

It is submitted that the outcomes in *Etlis* and *BMD Major Projects* would not have played out any differently without reliance on *Mannai*, despite the doubt that has now been cast on the underlying basis for that reliance.

First, even if the true rule applies to the interpretation of administration notices given under construction contracts – which, it is submitted, it should not – the author’s view is that *Etlis* and *BMD Major Projects* would still have had the same outcome. Put simply, the notices considered in those cases were ambiguous on their face. Adopting the broader characterisation of “ambiguity”,¹¹² the scope and applicability of the relevant notices were doubtful. The gateway requirement – if indeed there is such a requirement for notices – was satisfied in any event.

Secondly, one should perhaps not read too much into the citation of *Mannai* in *BMD Major Projects*. Although *Mannai* was squarely relied upon in *Etlis*, it was not the only decision relied upon in *BMD Major Projects* to support the commercial approach to interpretation of the relevant notice provisions and the notices themselves.

More germane to Pagone J’s decision in *BMD Major Projects* appeared to be the High Court authorities of *Pacific Carriers*, and *Toll v Alphapharm*. In *Western Export Services*, the High Court, after re-affirming that the true rule remains binding precedent in Australia, said:

We do not read anything said in this Court in *Pacific Carriers Ltd v BNP Paribas*; *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd*; *Wilkie v Gordian Runoff Ltd* and *International Air Transport Association v Ansett Australia Holdings Ltd* as operating inconsistently with what was said by Mason J in the passage in *Codelfa* to which we have referred.¹¹³

The decisions of *Pacific Carriers* and *Toll v Alphapharm* squarely support the consideration of surrounding circumstances in the same way as was the surrounding circumstances were considered in *Etlis* and *BMD Major Projects*. The High Court itself sees no inconsistency between those decisions and *Codelfa*.

In *Pacific Carriers*, the seller of legumes provided a letter of indemnity to its sea carrier to facilitate delivery without the production of a bill of lading. The letter of indemnity was signed by the seller and was signed and stamped by an officer of the seller’s bank. The bank argued that the letter, properly construed, did not provide an indemnity from the bank and that, in any event, the officer did not have the authority to bind the bank.¹¹⁴ The High Court held:

The case provides a good example of the reason why the meaning of commercial documents is determined objectively: it was only the documents that spoke to Pacific. The construction of the letters of indemnity is to be determined by what a reasonable person in the position of Pacific would have understood them to mean. That requires consideration, not only of the text of the documents, but also the surrounding circumstances known to Pacific and BNP, and the purpose and object of the transaction.¹¹⁵

¹¹⁰ For a more thorough analysis of *Brewarrina* and indeed the criticisms of the majority decision, see Baron A “Progress Claims, Progress Certificates and Legal Stability” (2003) 19 BCL 271; Rodighiero D “Responsibility for Failure to Certify Progress Payments: Where Are We Now?” (2008) 24 BCL 29.

¹¹¹ *Reardon Smith Line Ltd v Hansen-Tangen* [1976] 1 WLR 989 at 995 (Lord Wilberforce).

¹¹² Spigelman, n 44 at 326.

¹¹³ *Western Export Services Inc v Jireh International Pty Ltd* (2011) 282 ALR 604 at [5] (Gummow, Heydon and Bell JJ).

¹¹⁴ *Pacific Carriers Ltd v BNP Paribas* (2004) 218 CLR 451 at [4] (Gleeson CJ, Gummow, Hayne, Callinan and Heydon JJ).

¹¹⁵ *Pacific Carriers Ltd v BNP Paribas* (2004) 218 CLR 451 at [22].

After considering the terms of the document, the surrounding circumstances, and the purpose and object of the transaction (including a consideration of standard commercial practice),¹¹⁶ the court held that the bank was undertaking an obligation of indemnity.¹¹⁷

In *Toll v Alphapharm*, conditions of credit for the transportation of expensive and temperature-sensitive vaccines were signed by a representative of the consignor without that representative having read the terms of the contract. The vaccines were ruined in transit, causing significant losses, but the conditions of credit contained a wide exclusion of liability clause.¹¹⁸ The court endorsed its recent reaffirmation of the principle of objectivity and the above passage in *Pacific Carriers*,¹¹⁹ and held that the conditions of credit governed the transaction.¹²⁰

Extending these principles to contract administration notices in construction, there appears to be no doubt that the interpretation of notices includes what a reasonable person would understand a document to mean having regard to the purpose and the object of the transaction. The purpose and object of construction contract notices are as described above – to identify an issue in broad terms so that appropriate action can be taken by the parties. Therefore, consideration of surrounding circumstances is essential to interpret the notices. This brings us full circle to what were arguably the correct findings in *Etlis* and *BMD Major Projects*.

Risks – undermining the commercial approach

This article has sought to demonstrate that a non-technical approach to interpretation of contract administration notices is still to be preferred, notwithstanding the resurrection and residual uncertainty of the true rule. However, and unfortunately, it might not take much at all to undermine this approach.

The decisions of *Etlis*, *BMD Major Projects* and *Mannai* all appear to emphasise that a non-technical approach is allowed because the relevant clauses in those cases did not require the party to use a particular form of words in its notice.¹²¹ What if the relevant clauses are more prescriptive?

In *Mannai*, Lord Hoffmann said:

If the clause had said that the notice had to be on blue paper, it would have been no good serving a notice on pink paper, however clear it might have been that the tenant wanted to terminate the lease.¹²²

Although the provisions of some onerous, “owner-friendly” construction contracts do not literally require a notice to be communicated on blue paper, some come close enough. For example, extension of time clauses that might require the contractor to provide, within an extremely tight timeframe after commencement of a delay, the following prescribed information:

- all documentation relevant to the delay;
- evidence that the contractor has taken all reasonable steps to mitigate the delay;
- a detailed critical path analysis to demonstrate the effect of the delay (even if the delay has not ceased);
- a fully documented claim for delay costs (even if the delay has not ceased and the costs cannot properly be ascertained); and
- updated claims every, say, five business days.

Putting aside one’s views of such a tyrannical and antiquated notification regime, it may be difficult to interpret such a clause – and indeed the notice purportedly given under the clause – in a

¹¹⁶ *Pacific Carriers Ltd v BNP Paribas* (2004) 218 CLR 451 at [7].

¹¹⁷ *Pacific Carriers Ltd v BNP Paribas* (2004) 218 CLR 451 at [25].

¹¹⁸ *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* (2004) 219 CLR 165 at [19]–[20].

¹¹⁹ *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* (2004) 219 CLR 165 at [40].

¹²⁰ *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* (2004) 219 CLR 165 at [50].

¹²¹ *Etlis v New Age Constructions (NSW) Pty Ltd* [2005] NSWCA 165 at [29]; *BMD Major Projects Pty Ltd v Victorian Urban Development Authority* [2007] VSC 409 at [73]; *Mannai Investment Co Ltd v Eagle Star Life Assurance Co Ltd* [1997] AC 749 at 774 (Lord Hoffmann), 881 (Lord Clyde).

¹²² *Mannai Investment Co Ltd v Eagle Star Life Assurance Co Ltd* [1997] AC 749 at 776.

non-technical way. Given the accepted enforceability of time bars,¹²³ this is where the coward's castle really might trump the reasonable and commercial approach, despite the known purpose and objects of such a notice and the owner's own knowledge of the situation.

The absurdity of this strict approach is illuminated when one considers the modern technological framework in which the construction industry is now operating. Reliance on email communications, project databases (such as Aconex), cloud computing, and complex systems such as Building Information Modeling (BIM), all necessarily require a level of collaboration and – dare it be said – informality to work properly.

Charles Fournier has suggested that the natural consequence of this technological framework is that time bar regimes are likely to be marginalised over time.¹²⁴ Whether this will be the case remains to be seen. It is certainly a challenge that construction lawyers will need to consider and resolve in the near future.

In the meantime, the obvious answer is that contractors should refuse to sign draconian contracts containing such rigid and repressive requirements. In theory this makes sense but, unfortunately, in practice there is a difference between theory and practice.¹²⁵ Contractors (particularly subcontractors) often do not have the bargaining power to seek changes, and the principle of voluntary assumption of risk prevails (subject to any other form of relief such as waiver, estoppel or statutory unconscionability).¹²⁶

Spot the vicious cycle and the unintended consequences: the answer for an administratively burdened contractor may well be to wear that burden and then attempt to manage the contract accordingly with a plethora of formal notices. An owner may then respond to the flood of letters it receives by alleging that the contractor has become too "contractual". The parties may become "more concerned with anxiously satisfying a formal temporal requirement of notification rather than to explore the underlying needs and circumstances of the situation".¹²⁷ Relationships deteriorate and the project suffers.

This basic hypothetical is intended to illustrate that rigid technical notification obligations are not the answer. Contract administration should help the parties to deliver a quality project on time and on budget – not hinder them in a cumbersome and distracting paper war. Hopefully, sooner or later, the construction industry will come to realise the existence of this new pragmatic and commercial "true rule".

¹²³ As briefly described in the introduction to this article, including the footnoted references.

¹²⁴ Fournier C, *iNotice – Contractual Notices in the Era of Field Communication Systems*, Presented at 2013 Society of Construction Law Australia Conference (4 August 2013).

¹²⁵ A mangled version of a quote commonly credited to Lawrence Peter "Yogi" Berra, former American baseball player and manager.

¹²⁶ Douglas, n 25 at 171-172.

¹²⁷ *BMD Major Projects Pty Ltd v Victorian Urban Development Authority* [2007] VSC 409 at [11] (Pagone J).