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Subjective intention in the law of contract – its role and limits

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Introduction

When I was at the Bar I travelled very little, but a highlight was a five day trial in Brisbane, exactly twenty years ago, as a junior against David Logan, also then a junior, before Justice Richard Cooper sitting in the Federal Court here in Brisbane.[1] I consider myself very fortunate to have appeared before that very distinguished judge. My other memory of that trial is the generous hospitality of my opponent and of other local practitioners, which made me think of how some Sydney barristers, including me, did so little to welcome interstate colleagues. I would like to think that thereafter I tried a little harder to welcome my visiting opponents. Now, if you are thinking that is a none-too-subtle request not to treat me too harshly when the time comes for questions, you would be perfectly correct!

I shall start with a famous passage on the significance of signing documents:

> In the absence of fraud or some other of the special circumstances of the character mentioned, a man cannot escape the consequences of signing a document by saying, and proving, that he did not understand it. Unless he was prepared to take the chance of being bound by the terms of the document, whatever they might be, it was for him to protect himself by abstaining from signing the document until he

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1 *Dixon Projects Pty Ltd v Hallmark Homes Pty Ltd* [2004] FCA 118; 60 IPR 8.

> understood it and was satisfied with it. Any weakening of these principles would make chaos of every-day business transactions.

Its gender-specific language betrays its age. Putting that to one side, it may strike most of you as an unexceptionally correct statement of the law of contract. But (to anticipate one of the topics to which I shall return) that depends on what we both mean by "the law of contract". The occasion for Sir John Latham's statement was to contrast the law applicable to business contracts with the position when William Farnworth – described as a man of "no education, small intelligence and a history of curious conduct"[2] – gave over the entirety of his assets by way of purported gift to his step son.[3] The High Court had no difficulty upholding the trial judge's finding that this had occurred in circumstances making it what we would now describe as unconscionable for the stepson to rely on the deed.

My point is not that the law of contract excludes the law of deeds, even though the latter is some half a millennium older than the modern law deriving from assumpsit.[4] What is now called the law of contract would once have been regarded as comprising, within the common law, of the areas of covenant, plus a deal of debt, detinue and assumpsit,[5] and extending outside common law to a great deal of the law of the staple, the law of the fair, and the law merchant which was not incorporated into common law until the 18th century.[6] To this day there are occasions where those differences matter. An example is the enforcement of deeds by non-parties, where there is no need to identify an exception to the "rules" of privity.[7] Normally it does not matter if a document is a deed or an agreement, but sometimes it does. As Windeyer J said half a century ago:[8]

> That our law should still treat covenants by deed differently from other promises in writing may seem to be today a regrettable historical survival – a relic of a very distant past, and of the distinction in somewhat later times between covenant, or debt, and assumpsit as forms of action. ... But it is not for any court administering

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2 (1948) 76 CLR 646 at 655.

3 The deed was very poorly drafted but was treated as effective to do so.

4 See the first two chapters of AWB Simpson, *A History of the Common Law of Contract* (Clarendon Press, Oxford, 1975).

5 See G Lindsay, "Building a Nation: The Doctrine of Precedent in Australian Legal History" in J Gleeson et al (eds), *Historical Foundations of Australian Law* (Federation Press, 2013) 267 at 294.

6 See M Leeming, "The Enduring Qualities of Commercial Law", Third Bathurst Lecture on Commercial Law, 22 April 2021, pp 7-16.

7 See for example *Morgan v Pike* (1854) 14 CB 473; 139 ER 195, Jervis CJ concluded that "the covenantor may be sued upon his covenants, although the deed may not have been executed by the covenantee", as did Cresswell and Williams JJ. Later authorities are reviewed in *Mirzikinian v Tom & Bill Waterhouse Pty Ltd* [2009] NSWCA 296 at [50]-[53].

8 *Brooks v Burns Philp Trustee Co Ltd* (1969) 121 CLR 432 at 464.

> the common law to shut its eyes to a seal and in impatience to treat words of covenant as if they were promises which, in the absence of consideration, the law would not enforce.

That remains true to this day. It is one reason why "the law of contract" may be more complex than it seems.

As it happens, there is complete, or virtually complete, overlap between the law of deeds and the law of simple contracts in relation to the subject of this address, which concerns the role of subjective intention. The solemnity of a deed, which not only must be written but most also be "signed, sealed and delivered" – although those words certainly don't bear their ordinary meaning but instead bear quite different, and highly diluted, meanings by reason of New South Wales and Queensland statutes[9] – makes it a paradigm case where evidence of a party's subjective intention is inadmissible, except, at least arguably, the special case of a deed of release (to anticipate another topic to which I shall return).

Another aspect of my point is that the "law of contract" is *not* the law governing the large majority of legality binding agreements which parties enter into. I am not talking about the humdrum contracts of daily existence (such as contracts to buy a cup of coffee, or a meal at a restaurant, or contracts for carriage by taxi or public transport). None of those contracts is written. And while there may be a written contract between banker and customer, and insured and insurer, should there be a dispute, our respective contractual rights will be but a small component of its resolution, and at least one party may prefer to rely upon non-contractual rights (such as a statutory obligation to provide "responsible lending") or non-curial remedies (such as the Australian Financial Complaints Authority (the successor of, inter alia, the Financial Ombudsman Service)). These contracts are numerous, but they are never, or almost never, litigated, because it is not worth anyone's trouble to do so. I am also not talking about "domestic contracts", which are often informal but which tend to concern ownership of the family home or farm. But while I am mentioning these topics about which I am *not* talking, might I note that there is nothing closely resembling offer and acceptance in most of the most frequently encountered classes of contract. All this reflects what Lord Wilberforce had observed of the difficulties caused by English law having committed itself to a "rather technical and schematic doctrine of contract" which caused "many situations of daily life" to "fit uneasily into the marked slots of offer, acceptance and consideration".[10]

[9] Contrast *Conveyancing Act 1919* (NSW), s 38 and *Property Law Act 1974* (Qld), Part 6, Subdiv 2.

[10] *New Zealand Shipping Co Ltd v AM Satterthwaite & Co Ltd* [1975] AC 154 at 167. See also *Integrated*

The topic of this presentation concerns the law of bespoke negotiated written agreements, normally between commercial parties. The law of contract that is of interest to me and, I hope, to you, is the *litigated* law of contract. In large measure, that means contracts separate from "consumer" contracts which are moderately heavily regulated by statute. They are important, both in terms of the economic activity they reflect, and as a proportion of the litigation that occupies court time. As the English Court of Appeal noted in 2021, it is far from clear that all of the rules and principles governing the interpretation of negotiated agreements apply more broadly throughout the law of contract.[11]

In truth, the fact that the subject matter is the *litigated* law of contract has direct consequences for the rules and exceptions to be discussed. For completely understandable reasons, a large concern of the scope of the rules bearing upon the construction of negotiated, bespoke, written contracts is the avoidance of the time and cost of preparing, and responding to, evidence outside the scope of the contract.

The importance of signature

The position was well put in a decision which was one of the successes of the Chair of this presentation, just a year before he was appointed to the Court of Appeal, and at the same time two junior counsel were spending a week before Justice Cooper. In *Equuscorp Pty Ltd v Glengallan Investments Pty Ltd* the joint judgment said:[12]

> The respondents each having executed a loan agreement, each is bound by it. Having executed the document, and not having been induced to do so by fraud, mistake, or misrepresentation, the respondents cannot now be heard to say that they are not bound by the agreement recorded in it. The parol evidence rule, the limited operation of the defence of non est factum and the development of the equitable remedy of rectification, all proceed from the premise that a party executing a written agreement is bound by it.

The same point was made in *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* by reference to the passage from Sir John Latham's judgment in *Wilton v Farnworth*.[13] This is not confined to the law of contract. It certainly extends to deeds poll and conveyances and other signed instruments. But in its application to the law of contract, it is closely linked to the objective

Computer Services Pty Ltd v Digital Equipment Corp (Aust) Pty Ltd (1988) 5 BPR 11,110 at 11,117 and *Branir Pty Ltd v Owston Nominees (No 2) Pty Ltd* (2001) 117 FCR 424; [2001] FCA 1833 at [369].

11 See *Ralph v Ralph* [2021] EWCA Civ 1106; [2022] 2 All ER 325 at [26]-[31].

12 (2004) 218 CLR 471; [2004] HCA 55 at [33] (footnotes omitted).

13 *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* (2004) 219 CLR 165; [2004] HCA 52 at [46]-[47].

theory of construction, and the "fundamental rule" of contractual interpretation, which as stated in *Byrnes v Kendle,* is to be found in answer to the question, "What is the meaning of what the parties have said?", not to the question, "What did the parties mean to say?"[14] (Imagine by the way how difficult it would be to translate that distinction into a foreign language, or, alternatively, how difficult it would be for lawyers for whom English is a second language to apprehend the distinction drawn by the High Court. Legal language can be very complex and very subtle.)

The High Court said that the parol evidence rule proceeded from the significance of a signature. As you all know, the joint judgment in *Con-Stan Industries of Australia Pty Ltd v Norwich Winterthur Insurance (Australia) Ltd* said that the rule was "extrinsic evidence is generally inadmissible to add to, vary or contradict the express terms of a contract which has been reduced to writing".[15] The rule admits of exceptions; hence "generally". That makes it no different from just about every other rule or principle in law that there is. It has always been thus. Year books from the 15th century establish that non est factum was even then regarded as a good plea to a deed.[16] The rule in its modern formulation[17] is also expressed in terms of a particular proscribed use, namely, to prevent additions, variations or contradictions of express terms.

Two preliminary points should be noted about the use of evidence of subjective intention.

First, the doctrines where legal meaning is given to a document by reference to a subjective intention "must necessarily be kept within narrow limits" for they go against that accepted objective theory of contractual interpretation.[18]

Secondly, "[i]n all these cases, strong evidence is required in order to displace the orthodox approach to construction."[19] A variety of language has been used to capture that

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[14] *Byrnes v Kendle* (2011) 243 CLR 253; [2011] HCA 26 at [53].
[15] (1986) 160 CLR 226 at 287.
[16] See YB 8 Hen VI pl 15, cited in W Holdsworth, *A History of English Law* (Methuen & Co, 3rd ed, 1944) Vol IX, p 177.
[17] Interestingly, the rule did not exist in earliest times, but came to be recognised in its modern form in the 17th century, associated with the *Statute of Frauds*. See J Wigmore, "A Brief History of the Parol Evidence Rule" 4 *Columbia LR* 338 at 350ff (1904), and W Holdsworth, *A History of English Law* (Methuen & Co, 3rd ed, 1944) Vol IX, pp 173-177.
[18] See *Toll v Alphapharm* at [46]-[47].
[19] *Lewis v Condon* (2013) 85 NSWLR 99; [2013] NSWCA 204 at [62], referring to *Petelin v Cullen* (1975) 132 CLR 355 at 359-360 (as to the "heavy onus" to be discharged by the plaintiff in a non est factum case) and *Franklins Pty Ltd v Metcash Trading Ltd* (2009) 76 NSWLR 603; [2009] NSWCA 407 at [451]-[460] (as to the requirement of "clear and convincing proof" in a rectification suit).

concept – most famously in the context of equitable rectification, "clear and convincing proof", but also "the strongest proof possible", "strong irrefragable evidence", "the very clearest evidence", and others, as Campbell JA explained.[20]

This is an example of the need to accommodate the significance attributed to executing a legal document.

The existence of those cases where evidence of subjective intention is admitted gives rise to a practical difficulty. Very few trials involve a single issue. It is not unlikely – in my experience it is the norm – for rectification and construction to be propounded in the alternative, in a single trial (this is quite modern; it may be doubted it occurred before the Judicature legislation). If evidence is admitted for one reason (say, rectification in equity), that does not make it permissible to use it for another (say, construction of a written agreement). Kirby P once referred to the judge taking care to maintain a "dichotomy of the mind" in dealing with each issue, and (as I read the judgment) was sceptical of judges' ability to do so.[21] Of course the same judges rule on evidentiary objections and go on to decide the cases every day – notably in a growing number of cases, in judge-alone criminal trials, where it may be impossible to forget the excluded evidence, especially if its prejudice outweighs its probative value.[22] I don't see insuperable difficulty in judges deciding questions of construction confining themselves to the evidence which is properly available to be used for that purpose.

Five "exceptions" to the parol evidence rule involving subjective intention

But there are exceptions to the parol evidence rule. Indeed, one topic I wish to explore is what follows from their status as "exceptions". I want to mention five topics where evidence of subjective intention is admissible (although some are controversial). They are Sir Anthony Mason's "united in rejecting" exception, the "private dictionary" principle, evidence of surrounding circumstances, rectification in equity, and the construction of releases. I am not being exhaustive – to that list might be added the defences of duress and non est factum, the doctrine of sham, and a large number of other equitable defences. But there are limits to our time and your patience. The point of addressing those examples is to consider how each inter-relates with the other. Aspects of all of them are

[20] *Franklins Pty Ltd v Metcash Trading Ltd* at [451]-[461].

[21] *B&B Constructions (Aust) Pty Ltd v Brain A Cheeseman & Associates Pty Ltd* (1994) 35 NSWLR 227 at 233, referring to doubts expressed by psychologists as to whether judges can assert a dichotomy of the mind and a faithful disregard for evidence inadmissible to the task of construction.

[22] In extreme cases, the parties may of course apply for the admissibility to be determined by another judge.

controversial, although that may merely be a consequence of the fact that the interaction between interpretation and rectification is just about the most controversial subject in the law of Australia and England and Wales right now. Indeed, the Privy Council – not a body known for unnecessary hyperbole – said six weeks ago that "the previously placid waters of English law about rectification may fairly be said to have been stirred up into a veritable storm".[23] Much of the debate centres around the limits of each doctrine. The point is that rational debate on the wisdom or unwisdom of each area is informed by asking what is its purpose, is it an exception to the parol evidence rule or is it some other rule or principle. In short, the topics need to be considered in context.

1. The "united in rejecting" exception

In *Codelfa Construction Pty Ltd v State Rail Authority of NSW*, Mason J said that:[24]

> There may perhaps be one situation in which evidence of the actual intention of the parties should be allowed to prevail over their presumed intention. If it transpires that the parties have refused to include in the contract a provision which would give effect to the presumed intention of persons in their position it may be proper to receive evidence of that refusal. After all, the court is interpreting the contract which the parties have made and in that exercise the court takes into account what reasonable men in that situation would have intended to convey by the words chosen. But is it right to carry that exercise to the point of placing on the words of the contract a meaning which the parties have united in rejecting? It is possible that evidence of mutual intention, if amounting to concurrence, is receivable so as to negative an inference sought to be drawn from surrounding circumstances.

The effect is that evidence of the subjective intentions of the parties may be admissible to show that a particular interpretation or meaning was rejected by the parties. One way in which this has arisen is where parts of a standard form have been deleted.[25] Now although Mason J raised this exception merely as a possibility, it was applied in the Queensland Court of Appeal by Fryberg JA, as confirmatory of a result already reached on the construction of a lease, although significantly both McMurdo P and Holmes JA refrained from expressing views on the point.[26] In the New South Wales Court of Appeal,

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[23] *Porter v Stokes* [2023] UKPC 11 at [37].

[24] *Codelfa Construction Pty Ltd v State Rail Authority of NSW* (1982) 149 CLR 337 at 352-353.

[25] See *NZI Capital Corporation v Child* (1991) 23 NSWLR 481 at 490-494; *Esso Australia Ltd v Australian Petroleum Agents' & Distributors' Association* [1993] 3 VR 642 at [19]; *Walker Group Constructions Pty Ltd v Tzaneros Investments Pty Ltd* (2017) 94 NSWLR 108; [2017] NSWCA 27 at [117]-[118].

[26] *Elesanar Constructions Pty Ltd v State of Queensland* [2007] QCA 208 at [45]-[48]; cf at [5] and [7].

Sheller JA, writing for the Court, treated the exception as an example of where evidence of surrounding circumstances was available to construe an ambiguous provision.[27]

Mason J's exception has been subject of criticism. Indeed, Lord Nicholls once described this evening's commentator's criticism of the exception as both "penetrating" and "unanswerable".[28] The criticism was the conceptual difficulty in an exception which permits *negative* evidence to be adduced, but leaves *positive* evidence that the parties intended a word or provision to bear a particular reason to be determined by some other rule (such as rectification in equity where a different standard of proof applies). However, more recently, there has been acceptance of Mason J's proposition, albeit in the absence of argument on the point, by the High Court of Australia in *Ecosse Property Holdings Pty Ltd v Gee Dee Nominees Pty Ltd*.[29] For practical purposes, the exception is available in all trials in New South Wales and probably also throughout Australia.

2. The private dictionary principle

After referring to doctrines such as rectification and estoppel which his Lordship viewed as operating "outside" of the exclusionary rule, Lord Hoffman noted in *Chartbrook Ltd v Persimmon Homes Ltd* that there is "however a group of cases in which judges have found an exception to the exclusionary rule".[30] The leading case reflecting this exception is Kerr J's judgment in *Partenreederei MS Karen Oltmann v Scarsdale Shipping Co Ltd*.[31] Sir Michael Kerr – the trial judge in *The Siskina* who was appointed to lead the Commercial Court the following year – had to deal with a time charter for 2 years which contained a break clause: "Charterers to have the option to redeliver the vessel after 12 months' trading subject to giving three months' notice". The issue was whether "after 12 months' trading" meant that the break clause could be operated only at the end of the first year or at any time during the second year. His Lordship looked at telexes between the parties which discussed various lengths of break and were clearly using the word "after" to mean "on the expiring of" rather than "at any time after the expiry of". His Lordship justified the admissibility of this evidence:[32]

27 *Aberdeen Asset Management Ltd v Challenger Wealthlink Management Ltd* [2002] NSWCA 245 at [24].

28 D Nicholls, "My Kingdom for a Horse: The Meaning of Words" (2005) 121 *LQR* 577 at 584, referring to D McLauchlan, "Common Assumption and Contract Interpretation" (1997) 113 *LQR* 237 at 242.

29 (2017) 261 CLR 544; [2017] HCA 12 at [9] ("it was not disputed that in the circumstances it is open to the court to take account of the words crossed out of the standard form as an aid to the proper construction of the clause. The deletions do not evidence a prior intent, which could have changed, but rather they identify a matter which, on the face of the document, was rejected by both parties"). Nettle J made the same point at [73].

30 [2009] 1 AC 1101; [2009] UKHL 38 at [43].

31 [1976] 2 Lloyd's Rep 708.

32 [1976] 2 Lloyd's Rep 708 at 712.

> If a contract contains words which, in their context, are fairly capable of bearing more than one meaning, and if it is alleged that the parties have in effect negotiated on an agreed basis that the words bore only one of the two possible meanings, then it is permissible for the court to examine the extrinsic evidence relied upon to see whether the parties have in fact used the words in question in one sense only, so that they have in effect given their own dictionary meaning to the words as the result of their common intention. Such cases would not support a claim for rectification of the contract, because the choice of words in the contract did not result from any mistake. The words used in the contract would ex hypothesi reflect the meaning which both parties intended.

I shall come back to this point, which is problematic. One criticism is that, as others have pointed out, it is far from clear that rectification would not be available in those circumstances. A second criticism is that the reasoning seems to be that because of a perceived limitation of an equitable remedy, a common law exception should be created. Some might think that that tends to reverse that natural order of things!

The effect of this reasoning is that evidence may be admissible to show that the parties negotiated on the basis of a common understanding or agreement that a word or phrase bore a particular meaning. There is a deal of hostility to this decision, especially in the United Kingdom.[33] However, it should be noted that Kerr J's exception has been cited with approval by Courts of Appeal in New South Wales[34] and Queensland,[35] and was regarded as uncontroversial by the New Zealand Supreme Court's recent, important judgment in *Bathurst Resources Ltd v L&M Coal Holdings Ltd*.[36] It is always difficult to judge how foreign legal systems work, but I suspect that businesspeople and litigators in the United States would regard the debate about this exception as peculiar as the clothes judges and counsel wear when hearing cases. Under §201 of the Second Restatement on Contracts, it is provided that "Where the parties have attached the same meaning to a promise or

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[33] Lord Steyn wrote that it has the potential to "swallow up" the exclusionary rule: J Steyn, "Written Contracts: To What Extent May Evidence Control Language" (1988) 41 *Curr Leg Prob* 23 at 29. In *Chartbrook*, Lord Hoffman considered at [45] that the admission of evidence in *The Karen Oltmann* did in fact infringe the exclusionary rule, viewing it as an "illegitimate extension of the 'private dictionary' principle which, taken to its logical conclusion, would destroy the exclusionary rule and any practical advantages which it may have": at [47]. See also D McLauchlan, "Contract Interpretation: What is it About?" (2009) 31(1) *Syd LR* 5.

[34] *Commonwealth Steel Company Ltd v BHP Billiton Marine & General Insurance Ltd* [2018] NSWCA 242 at [1], [6] and [36].

[35] *Australasian Medical Insurance Ltd v CGU Insurance Ltd* [2010] QCA 189; 271 ALR 142 at [1], [62] and [93].

[36] [2021] 1 NZLR 696; [2021] NZSC 85 at [81].

agreement or a term thereof, it is interpreted in accordance with that meaning", and the account in *Corbin on Contracts* suggests it is uncontroversial.[37] I cannot resist mentioning one of my favourite opening lines of one of my favourite and best named New York judges. The decision is *Frigaliment Importing Co Ltd v RNS International Sales Corp*,[38] the subject matter is a written contract for the sale of 150,000 pounds of chicken, the judge was the inaptly named Judge Friendly (who by all accounts was a forbidding, austere, man for whom both Merrick Garland and John Roberts clerked)[39] and the opening line, which accurately captures the essence of the trial, was "The issue is, what is chicken?" The plaintiff had bought an enormous quantity of frozen chicken, and complained that it meant young birds suitable for broiling and frying. The subjective belief of the defendant, which was that older, less succulent chickens suitable only for stewing would suffice, was relevant and probably dispositive.[40]

Some of the criticism concerns identifying the pigeon-hole into which these cases fall. Thus, in "private dictionary" cases, it has been suggested that estoppel by convention and rectification should instead be considered.[41] It has also been suggested that the exception applies only to cases where the parties have used a word "unconventionally".[42] Against this, Professor McLachlan has written that:[43]

> It is difficult to understand why the court should be able to admit evidence that the parties always, or for a particular transaction, used a word in an unconventional sense, for example, they used 'apples' to mean 'pears' or 'sell' to mean 'buy', but not evidence that they used a word in one of two conventional senses, such as the

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37 See *Corbin on Contracts* §24.5.

38 190 F Supp 116 (1960).

39 See, generally, D Dorsen, *Henry Friendly – Greatest Judge of his Era* (Harvard University Press, 2012).

40 "When all the evidence is reviewed, it is clear that defendant believed it could comply with the contracts by delivering stewing chicken in the 2½-3 lbs size. Defendant's subjective intent would not be significant if this did not coincide with an objective meaning of 'chicken'. Here it did coincide with one of the dictionary meanings ...": at 121.

41 *Chartbrook* at [47]. Briggs J, sitting at first instance, had noted in [2007] EWHC 409 (Ch) at [42] that if he were free to do so, he would re-analyse the *Karen Oltmann* line of cases as rectification cases, as he felt that that rectification cases precisely encapsulated those cases dealing with the private dictionary principle; see especially at [41]-[43] (of course, his Lordship is now free to do precisely that).

42 *Chartbrook* at [45] ("It is true that evidence 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. But the telexes in *the Karen Oltmann* did not evidence any unconventional usage. There was no private dictionary. The case involved a choice between two perfectly conventional meanings of the word "after" in a particular context. In my opinion Lawrence Collins LJ was right in saying that the admission of the evidence infringed the exclusionary rule").

43 "The Continuing Confusion and Uncertainty over the Relevance of Actual Mutual Intention in Contractual Interpretation" (2021) 37 *JCL* 25.

word 'after' in *The Karen Oltmann*. One would have thought that, if anything were to be excluded, it would be the evidence of the unconventional meaning!

To that might be added the proposition that whether or not a usage is "conventional" or "unconventional" is scarcely a clearly defined element of a rule. Language is much more subtle than that. Meaning turns on context, as does whether a use is "conventional" or otherwise; I hope the examples I have mentioned (including but not limited to "after 12 months" and "chicken") confirm as much.

One notable "private dictionary" case is *Proforce Recruit Ltd v Rugby Group Ltd*,[44] where the Court of Appeal of England and Wales concluded that a strike out on an otherwise unarguable case on construction could be saved by reference to the meaning that it was alleged that the parties had in their negotiations placed on that phrase. Mummery LJ observed that evidence of the parties' pre-contractual negotiations would have influenced the notional reasonable person in his understanding of the meaning the parties intended to convey by the words used. It is also worth pausing on the concurrence of Arden LJ, which exposes an important distinction:[45]

> [T]hose words bear the meaning that the parties in common gave to them in their communications leading up to the signing of the agreement. In admitting evidence as to those communications, the court would be hearing that evidence not with a view to taking the parties' subjective intent into account for the purposes of interpretation (a purpose precluded by the principles laid down by Lord Hoffman [in *Investors Compensation Scheme Ltd v Westbromich Building Society* [1988] 1 All ER 98; 1 WLR 896]) but for the purpose of identifying the meaning that the parties in effect incorporated into their agreement in circumstances where the court was satisfied that on their true interpretation the terms of the agreement were to have this effect.

3. Surrounding circumstances

As Arden LJ indicated, the "private dictionary" exception is an instance of evidence which bears directly upon the objective meaning to which the parties are taken to have agreed. The "united in rejecting" exception is no different. The meaning of the words used in the written contract is informed by the facts known to both parties that they used language in a particular way, and if they were united in rejecting a particular construction. They are

[44] [2006] EWCA Civ 69; [2006] All ER (D) 247.
[45] [2006] EWCA Civ 69; [2006] All ER (D) 247 at [55].

separate exceptions because (a) the situation recurs and (b) the force of the evidence of the known understanding of language of the parties in those cases is especially probative. I do not regard what is occurring as adding to, or varying, or contradicting the written contractual text; instead, these doctrines supply an objectively demonstrable meaning to the parties' chosen words. At least one aspect of the problems with the exceptions is delineating them (confining them to meanings which have been *rejected* or usage which is *unconventional*).

In my view, there is much to be said for both "exceptions" to be an aspect of a broader rule of the admissibility of surrounding circumstances. Take for example *Macdonald v Longbottom*.[46] That was a case where a pre-contractual conversation between the parties showed that a contract for the sale of "your wool" was intended to include both wool produced on the seller's farm and the wool that the seller had brought in from other farms. All members of the Court of Queen's Bench held that the conversation was admissible to identify the subject matter of the contract. In *Prenn v Simmonds*,[47] Lord Wilberforce treated this as an example of a case where "evidence of mutually known facts may be admitted to identify the meaning of a descriptive term". These decisions were referred to by Mason J in *Codelfa* when formulating the exception to the parol evidence rule. It is easy to see how this more general approach can subsume the particular exceptions I have mentioned above.

Evidence of prior negotiations being admitted for the purpose of establishing the objective background is not the same as those negotiations being admitted for the purpose of demonstrating the parties' actual intentions. The distinction is quite fine. It has been said that "[t]he main difficulty lies in deciding whether evidence of pre-contractual negotiations [are] being adduced to prove a fact which is objectively known to the parties, or to establish what the contract means".[48] As I understand it, that is the force of Professor McLauchlan's criticism:[49]

> It is obvious that neither [Lord Hoffman or Mason J] had in mind objective evidence of the meaning that the parties actually attached to the language in dispute, but that is precisely the effect of a long line of authority applying such an objective background facts exception.

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[46] (1859) 1 El & El 977; 120 ER 1177.
[47] [1971] 1 WLR 1381 at 1384.
[48] P S Davies, "Negotiating the Boundaries of Inadmissibility" [2011] *CLJ* 24 at 26.
[49] (2021) 37 *JCL* 25 at 30; and see the discussion of cases in (2009) 31 *Syd LR* 5 at 26-29.

Further, it has been noted that this exception can undermine the exclusionary rule altogether as "the content of pre-contract discussions is [itself] a background fact".[50] I completely agree that the content of pre-contract discussions and negotiations are background facts. The fact that they are pre-contractual negotiations does not make them inadmissible. They may be used if they inform the meaning the parties ascribed to the contractual language, although they may not be used simplistically on the basis that they inform the result which either or both party understood to have been agreed.

The distinction is quite fine, and if the construction of the contract were determined by a jury, one might doubt the wisdom of rules which result in such fine distinctions. However, the proper construction of the contract will be determined by a judge (or a panel of appellate judges) who will give reasons for the construction. Those reasons ought to make it clear whether and if so how the evidence of surrounding circumstances has been used.

How does this affect the advocate? The decisions mentioned above illustrate that there are available at least three bases upon which evidence external to a written negotiated contract may be tendered. More than one basis may be available, and there is seldom harm in mentioning that if the tender is opposed. The time to articulate the basis upon which such evidence is tendered is the time it is tendered, not closing address – especially if the judge, who may be concerned about the size of the "agreed tender bundle", wants to know why each document is to be tendered. The time to determine whether to adduce such evidence is when the case is being prepared. For of course there is a cost in attempting to identify useful evidence bearing upon the construction of a contract, and it may be substantial, and the utility of doing so needs to be assessed in light of the strength of the purely textual arguments available to the party.

In particular, when evidence is tendered which is said to be of surrounding circumstances, it ought to be possible for the litigator to answer, in twenty words or less, what is the particular circumstances to which the evidence is relevant and how that bears upon a contested question of construction. It seems to me that an approach which is focussed on the particular issues arising in the particular litigation is most likely to accommodate the legitimate concerns of unnecessary cost and delay in litigation.

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[50] D Nicholls, "My Kingdom for a Horse: the Meaning of Words" (2005) 121 *LQR* 577 at 582.

Now what I have said about the breadth of the rule permitting evidence of surrounding circumstances to be tendered, and the running of trials, may well be controversial, and there may be scope for an exchange of views on those issues later this evening. My point is that if one takes a broad view of the admissibility of surrounding circumstances, then it may be seen that the "united in rejecting" exception and the "private dictionary" principle are just aspects of evidence of surrounding circumstances which are especially probative. There is no need to regard them as separate exceptions, but instead they are aspects of the same rule, which permits the tender of relevant evidence.

4. Rectification in equity

The foregoing is completely different from rectification in equity. In such cases, evidence of the parties' subjective understanding is admissible and indeed determinative; the suit will fail unless the Court is satisfied that the written instrument does not reflect the parties' subjective intention. The doctrine transcends the law of contract – it applies to all instruments, including voluntary settlements, deeds poll and conveyances. It is also different in its operation. There may be large questions whether as a matter of construction the evidence of a private dictionary, or the parties being united in opposing, or the evidence of surrounding circumstances, suffices to give meaning to the contractual language – but if they are sufficient, then the contract is construed in that way and that is the end of the analysis. In contrast, even if a claim for rectification is made out, relief may be refused for discretionary reasons (for example, delay or the intervention of third parties) or only granted on terms.[51] Moreover, as previously mentioned, equity imposes an elevated standard of proof – traditionally, "clear and convincing proof" – before a claim for rectification is made out. I mentioned that this is a very controversial area right now, although you are fortunate in having probably the leading academic commentator in the common law world on this topic speaking after me.[52] That suggests I should be careful and concise.

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[51] See for example *Sargeant v Reece* [2007] EWHC 2663 (Ch) at [86]-[88], *Konica Minolta Business Solutions (UK) Ltd v Applegate* [2012] EWHC 3242 (Ch) at [121]-[123] and [2013] EWHC (Ch) 2536 (Ch) at [49]-[53], *CMG Equity Investments Pty Ltd v Australia and New Zealand Banking Group Ltd* [2008] FCA 455; 65 ACSR 650 at [28] and *Re Premier Bay Pty Ltd* [2018] VSC 168 at [743].

[52] See for example D McLauchlan, "*Chartbrook Ltd v Persimmon Homes Ltd*: Common-sense Principles of Interpretation and Rectification?" (2010) 126 *LQR* 8; D McLauchlan, "Refining Rectification" (2014) 130 *LQR* 83; D McLauchlan, "The Many Versions of Rectification for Common Mistake" in S Degeling, J Edelman and J Goudkamp (eds), *Contract in Commercial Law* (Thomson Reuters, 2016); D McLauchlan, "Rectification Rectified?" (2020) 36 *JCL* 131; D McLauchlan, "The Continuing Confusion and Uncertainty over the Relevance of Actual Mutual Intention in Contractual Interpretation" (2021) 37 *JCL* 25.

I only wish to make one point. That is that no question arises here as to how to reconcile the doctrine with the parol evidence rule. Equitable rectification is in the teeth of the parol evidence rule. The evidence which is excluded by the parol evidence is *precisely* the evidence which is critical to a claim for rectification. The limits on the doctrine are found elsewhere, and when it applies, it trumps the construction reached at law, ultimately by reason of the operation of the local equivalent of s 25(11) of the *Judicature Act 1873* (UK), s 7(3) of the *Civil Proceedings Act 2011* (Qld): if there is a conflict between the rules at common law and in equity, the latter prevail.

None of this is to deny that it makes sense to consider the inter-relationship between the separate roles of interpretation and rectification. But it is very different from a consideration of the overlapping scope of the exceptions to the parol evidence act encapsulated in the "united in rejecting", the "private dictionary" principle and the surrounding circumstances exception, all of which are aspects of the common law and which may be expected to live harmoniously with each other.

5. Construction of releases in equity

The last example concerns how a release is to be construed in equity. There is a deal of authority to the effect that the subjective understanding of a releasor is admissible and may be used to construe the document, being a different approach from that taken at common law. I attempted to describe the position in *Reid v Commonwealth Bank of Australia*,[53] to which reference may be made if you are interested. In short, there are a series of passages in judgments, including 19th century English decisions, and contemporary decisions of intermediate appellate courts, which treat the construction of a release as outside the parol evidence rule.[54] Most recently, in *Burness v Hill* a unanimous Victorian Court of Appeal explicitly upheld the decision at first instance that a party's subjective intention was relevant, saying:[55]

> The trustees' second contention challenges that finding, on the basis that the trial judge erred in taking Hill's subjective intention into account in construing the words of the release. The emphasised words in the summary of the equitable principle in *Grant*, which we have set out at paragraph above, are directly inconsistent with the

[53] (2022) 109 NSWLR 149; [2022] NSWCA 134 at [38]-[48].

[54] See *Torrens Aloha Pty Ltd v Citibank NA* (1997) 72 FCR 581 at 600, where a Full Court of the Federal Court referred to a statement by Sir Frederick Pollock which had also been endorsed in *Grant v John Grant & Sons Pty Ltd* (1954) 91 CLR 112, namely, that "in equity 'a release shall not be construed as applying to something of which the party executing it was ignorant'".

[55] *Burness v Hill* [2019] VSCA 94 at [78].

second contention; which must therefore fail. Specifically, the trial judge was justified in referring both to Hill's subjective intention and the fact that Hill was ignorant of his marshalling claim at the time he entered into the terms of settlement.

The passage in the joint judgment of the High Court in *Grant v John Grant & Sons Pty Ltd* upon which reliance was placed was:[56]

> From the authorities which have already been cited it will be seen that equity proceeded upon the principle that a releasee must not use the general words of a release as a means of escaping the fulfilment of obligations falling outside the true purpose of the transaction as ascertained from the nature of the instrument and the surrounding circumstances including the state of knowledge of the respective parties concerning the existence, character and extent of the liability in question **and the actual intention of the releasor**.

There is a debate about how the authorities are to be read,[57] when regard is had to clear English authority that "there is no room today for the application of any special 'rules' of interpretation in the case of general releases".[58] Everyone accepts that it is possible to release an unknown claim, and that merely because a releasor is unaware of the claim does not stand in the way of such a construction being upheld. Everyone accepts that, separately from construction, it may be unconscionable for a releasee to rely upon a release (which in fact was an aspect of what occurred in *Wilton v Farnworth*).[59] What is contested is whether the approach stated in the passages reproduced above should be regarded as distinct from the orthodox objective approach to construction. In light of the existing state of authorities, I incline to the view that that is a matter for the High Court and the High Court alone (it was not necessary to decide this definitively in *Reid v Commonwealth Bank of Australia*). But were that not so, I would treat considerations of coherence in relation to the approach taken in equity to the construction of releases quite differently from the interaction between the "united in rejecting", the "private dictionary" and the "surrounding circumstances" exceptions to the parol evidence rule. The question is quite different. It is whether there may still in 2023 be said to be a rule of equity that in construing a release, regard may be had to the releasor's subjective intention. If so, then s 7(3) of the *Civil Proceedings Act 2011* (Qld) applies and the evidence will be admissible

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[56] (1954) 91 CLR 112 at 129-130 (emphasis added).
[57] See P Herzfeld and T Prince, *Interpretation* (Lawbook Co, 2nd ed, 2020), p 632 and cf *Reid* at [42]-[45].
[58] *Bank of Credit and Commerce International SA v Ali* [2002] 1 AC 251; [2001] UKHL 8 at [26].
[59] See the release in the deed of Mr Wilton from all claims and demands to which Rich J referred at 653.

and available for use.

Consequences

Let me try to bring together six points out of that very brief tour through the uses of evidence of subjective intention.

First, subjective intention has a limited role in the law of contract, by which I mean, the law of litigated, negotiated contracts. That is necessary in order to preserve the objective theory of contractual construction, and the significance attributed to executing a written document. The exceptions where subjective intention is relevant as a matter of construction are curtailed in a number of ways.

Secondly, the parol evidence rule is a rule with a purpose, namely, to prevent evidence which adds to or varies or contradicts the parties' express terms when they have been reduced to writing. The rule has always been subject to "exceptions". On any view there are occasions when extrinsic evidence is admissible to identify the meaning of the parties' express language. Whether or not they are exceptions which add to, vary or contradict the contractual language is a topic not without interest, as is how they interact with each other. I have suggested that there is a case which can be made for the first and second being instances of the third.

Thirdly, the parol evidence rule is informed, in part, by policy concerns directed to the cost of litigation. There is to my mind much to be said for the appropriate constraint against misuse being one deriving from the rules of evidence. For, after all, the general rule in much of Australia is that, except as otherwise provided by the *Evidence Act*, "evidence that is relevant in a proceeding is admissible in the proceeding" and "evidence that is not relevant in the proceeding is not admissible".[60] In the important New Zealand decision of 2021 in *Bathurst Resources*,[61] there was a clarification of all of these issues in light of the *Evidence Act 2006* (NZ), although to be clear that legislation in some respects goes further than its Australian ancestors,[62] and thus some care must be taken if it is to be transplanted across the Tasman.

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60 *Evidence Act 1995* (NSW), s 56;

61 [2021] NZSC 85; [2021] 1 NZLR 696 see esp at [49]-[50].

62 In particular, the New Zealand statute displaces common law rules to the extent they are inconsistent with its provisions and purposes (s 10); cf s 9 of the New South Wales and Commonwealth Acts which are directed to preserving common law rules.

Fourthly, I have sought to illustrate that, rather than debating the width or narrowness of the rules and exceptions at common law, which have to apply to a wide range of cases, an alternative solution may be to descend to the particular. It is surely good discipline for the litigator who wishes to adduce evidence said to bear upon the construction of a negotiated written contract to be able to identify with some precision the basis on which it is said to be admissible – because it shows the parties had a particular purpose, or used language in a particular way – and the issue in the litigation to which that evidence is directed (for example, the dispute over the meaning of a particular clause). As the none-too-subtle references to the need for contextual construction mentioned above might suggest, I favour courts knowing more, rather than less, of the contextual background in order to fix a legal meaning to the negotiated contractual language, and I am sceptical of both the practicality and the correctness of any so-called "ambiguity gateway". I have sought to indicate, *en passant*, that the words "the law of contract" are ambiguous and context dependent, and the words "signed, sealed and delivered" are ambiguous and context dependent, as well as referring to decisions holding that the words "after 12 months" and "chicken" and "your wool" are ambiguous and context dependent. However, I am also acutely conscious that much of the contextual background will only peripherally, if at all, bear upon the resolution of a dispute. I have in mind the distinction drawn by the Supreme Court of New Zealand in *Bathurst Resources*:[63]

> Often the prior negotiations will not have addressed (even by necessary implication) the issue that has arisen in the proceedings, because that was an issue not identified by the parties prior to contract formation. Often they will also reveal no more than a negotiating stance adopted by one party that is not agreed to by the other.
>
> However, if evidence shows what a party intended the words to mean, and that this was communicated, it may tend to show a common mutual understanding as to the meaning of the contract. Logically, the party who claims to have communicated their intention would have to be able to point to something – even if just silence (in circumstances where a reply might be expected) – on the part of the other party to bring that intention into the realm of mutual understanding. Such an understanding is relevant to the objective search for meaning. The evidence will be relevant and, subject to the s 8 assessment, admissible.

What I have said may be controversial, especially insofar as applicable to those courts in

[63] [2021] NZSC 85; [2021] 1 NZLR 696 at [75]-[76].

Queensland to which the *Evidence Act 1995* (Cth) does not apply. If nothing else, if these words have caused some critical thought about a fundamental aspect of commercial litigation, they will not have been entirely in vain.

Fifthly, I have maintained that the position in equity is different. The motivating principles are different, the historical lineage is different, and the way in which relief may be obtained is different. If the issue is how to reconcile the various ways in which the parol evidence rule is qualified, then it is important to bear in mind the nature of the qualification. I hope I may be forgiven for citing from a leading decision of the High Court hearing a Queensland appeal:[64]

> The jurisdiction of a court of equity to set aside a gift or other disposition of property as, actually or presumptively, resulting from undue influence, abuse of confidence or other circumstances affecting the conscience of the donee is governed by principles the application of which calls for a precise examination of the particular facts, a scrutiny of the exact relations established between the parties and a consideration of the mental capacities, processes and idiosyncrasies of the donor. Such cases do not depend upon legal categories susceptible of clear definition and giving rise to definite issues of fact readily formulated which, when found, automatically determine the validity of the disposition. Indeed no better illustration could be found of Lord Stowell's generalisation concerning the administration of equity: "A court of law works its way to short issues, and confines its views to them. A court of equity takes a more comprehensive view, and looks to every connected circumstance that ought to influence its determination upon the real justice of the case."

The quest for coherence within the common law rules applicable to evidence admissible on construction is quite different from the way within the legal system the distinct principles of common law rules of construction and equitable rectification are reconciled.

Sixthly, even if you find aspects of that somewhat controversial, perhaps my words will serve to remind you, as I have been reminded in the course of preparing this presentation, of the profoundness of an observation made by Felix Frankfurter. He said that "Words are clumsy tools", and unquestionably that is borne out by much of the litigated law of contract, but he also added that "they are the only tools we have".[65]

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[64] *Jenyns v Public Curator (Qld)* (1953) 90 CLR 113 at 119, citing *The Juliana* (1822) 2 Dods 504 at 522; 165 ER 1560 at 1567.

[65] F Frankfurter, "Some reflections on the reading of statutes" 47 *Columbia LR* 527 at 546 (1947).

Subjective Intention in the Law of Contract: Its Role and Limits

Commentary by David McLauchlan

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In 2015 I was in England on sabbatical leave and I was asked by University College London to provide a commentary on a paper to be delivered by another leading judge. The judge on that occasion was Sir Terence Etherton, then Chancellor of the High Court of England and Wales and shortly afterwards Master of the Rolls. Sir Terence delivered a paper aptly entitled "Contract Formation and the Fog of Rectification".[1] My commentary was naturally very respectful but I did take issue with some of his observations, particularly those concerned with my writings in the area. Afterwards in the course of a very pleasant dinner I asked the Judge what he thought when he learned that I was to be the commentator. He looked me in the eye and, with only the hint of a smile, he said: "Well, you know, you agree to do a good deed, and what happens, you get punished!" I don't know what Justice Leeming will think of my comments this evening, but I very much hope that he won't think he has been punished. Certainly there is little that I disagree with in his comprehensive and insightful paper.

What I want to do is to suggest a way forward from the fine distinctions that the judge has highlighted – distinctions that make the law hard to understand or more complicated than it need be.

In my view two of the most troublesome terms in the law of contract are "subjective intention" and "objective intention". We are routinely told by judges who are faced with issues concerning the formation or interpretation of contracts that their task is to determine the parties' *objective* intention, not their *subjective* intention. It is said that evidence of subjective intention is irrelevant and inadmissible, and such evidence is often understood to embrace anything that points to the parties' *actual* intention. I have been arguing for years that this is an oversimplification. Of course, no-one has ever suggested that a court should be able to inquire into the parties' states of mind and hence allow them to testify as to what they each intended at the time of the alleged contract. However, the situation is entirely different where there is reliable evidence that, *as a result of communications between the parties*, they reached an agreement that was intended to be binding or, as the case may be, they formed a common understanding as to the meaning of language in dispute. What I am saying is that too often the dirty words "subjective intention" are used to rule out *any* evidence pointing to the parties' actual mutual intention on the basis that the sole task of the court is to determine their presumed (objective) intention. In fact, accepting and giving effect to evidence of the kind I have mentioned is not in any way inconsistent with an objective approach. One is still ascertaining the parties' intentions through objective evidence.

I have read judgments that in effect say to the parties "don't you tell me what you intended, it's my job to decide what you intended"! I also recall one New Zealand case[2] which included a

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1 Later published in (2015) 68 CLP 367.

2 *Brierley Investments Ltd v Shortland Securities Ltd* (1994) 5 TCLR 615.

finding by a very good High Court judge that the parties actually intended to be bound by an informal commercial property agreement. He said that their "actual belief at the time was that a binding deal had been concluded" and that "anything which remained was drafting detail". However, he then concluded that this was irrelevant. The question of intention to be bound was "not to be approached subjectively". It was "to be approached on an objective basis". The test was whether a reasonable person in the position of the promisee would have inferred that the promisor intended to be bound. I call this "objectivity gone mad"! How reasonable persons would have understood the transaction was irrelevant in this case. While the presence of actual consensus ad idem and intention to be bound is not *necessary* for formation of a binding contract, it is surely *sufficient*.

Difficulties also arise in relation to the term "objective intention". It is routinely said that it is a basic principle that the law is only concerned with the intention of the parties as *objectively ascertained*. So, in an interpretation dispute the judge must try to ascertain what a reasonable person would have understood the parties to have meant. But who is this reasonable person and what does he or she know about the background to the contract and the parties' dealings? It is widely thought that the common law depersonalises contracting parties and asks what a detached or outside observer would have taken their intention to be. On one view, this observer is imbued with business common sense and has knowledge of the all the terms of the contract and the surrounding circumstances, but apparently he or she is unaware of, or wholly unconcerned with, their actual intention, even if it is shared and manifested in communications between them.

However, it is equally common to refer to the objective test as requiring a determination of what the reasonable person *in the position of the parties* would have inferred. Numerous statements to like effect are to be found in the judgments of the High Court of Australia. For example, the Court said in *Toll v Alphapharm*[3] that "[w]hat matters is what each party by words and conduct would have led a reasonable person in the position of the other party to believe". On this version of objectivity, a reasonable person, who is asked to determine what the parties appeared to mean by the relevant language, would surely give decisive weight to communications between the parties establishing *either* a shared actual understanding of the meaning of the language *or* the understanding of one party where that party was led reasonably to believe that its understanding was also shared by the other party. In this context there is no sensible distinction between meaning and *what the parties meant* because what the parties meant IS the meaning!

Nevertheless, at the same time the High Court continues to adhere to rules that evidence of the parties' prior negotiations and subsequent conduct reflecting their actual intentions is inadmissible as an aid to interpretation. However, despite this, as Justice Leeming has explained, the courts are able, by one mechanism or another, to ensure that contractual terms are given a meaning that is consistent with a proven actual mutual intention of the parties. Well-informed counsel, and sympathetic judges who believe that it would be unjust to deny the parties' true bargain, have at their disposal various methods of achieving this. Justice Leeming has highlighted Justice Mason's "united in rejecting" principle, the "private dictionary" principle, the "objective background facts" exception, and of course the equitable remedy of rectification. All I will say about these is that, although their scope is to varying extents uncertain or contentious and they are sometimes overlooked, they do demonstrate that the law has no settled policy against enforcing a commonly understood or agreed meaning that is

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[3] (2004) 219 CLR 165 at [40].

apparent from the parties' negotiations. Indeed, given that the very purpose of the law of contract is to give effect to the parties' true intention or bargain, any such policy seems counter-intuitive.

I would add two other possible exceptions to Justice Leeming's list. The first is estoppel by convention. Not surprisingly, his Honour did not highlight this because the Australian authorities, at least when I last looked, are conflicting.[4] However, there is now substantial authority from other jurisdictions for the view that the doctrine of estoppel by convention may be invoked to avoid the rule excluding evidence of prior negotiations As Lord Hoffmann explained in the *Chartbrook* case, "if the parties have negotiated an agreement upon some common assumption, which may include an assumption that certain words will bear a certain meaning, they may be estopped from contending that the words should be given a different meaning".[5] This has precisely the same effect as if the evidence had been admitted as an aid to determining meaning in the first place. So, instead of saying that the objectively determined actual mutual intention of the parties is the meaning of the contract, it is said that, where both parties have proceeded on the basis that the contract did mean what they intended it to mean, the party denying that meaning is estopped from doing so. No wonder this whole area of the law makes our heads spin!

Turning now to my other addition, depending on the circumstances it may also be possible to argue that a common understanding or agreement gave rise to a collateral contract or that it was a term of a partly written and partly oral contract. I mention this because the very existence of these well-established "exceptions" to the parol evidence rule leads me to question why it should make a difference that the oral agreement concerns the meaning of a term contained in a written document as opposed to an agreement on a matter not covered in the document. In other words, why should the admissibility of extrinsic evidence depend on whether the evidence concerns the meaning the parties gave to the contractual language or the existence of a collateral contract or an independent oral term?

This brings me to what is perhaps the main reason why Australian law in this area is particularly difficult. It concerns the continuing belief that there is a meaningful parol evidence rule. As Justice Leeming has mentioned, the rule states that evidence is inadmissible to add to, vary or contradict the terms of a written contract. However, none of the leading Commonwealth jurisdictions, apart from Australia, take the rule seriously nowadays because it is riddled with so many exceptions or qualifications. Certainly it no longer has the stringent effects that it once had. The English Law Commission was surely correct in its 1986 report on the subject when it said that "no parol evidence rule today requires a court to exclude or ignore evidence which should be admitted or acted upon if the true contractual intention of the parties is to be ascertained and effect given to it".[6]

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4 *Johnson Matthey Ltd v AC Rochester Overseas Corp* (1990) 23 NSWLR 190 SC at 195 and *Australian Co-operative Foods Ltd v Norco Co-operative Ltd* (1999) 46 NSWLR 267 at [52]. However, *Johnson* was not followed in *Whittet v State Bank of New South Wales* (1991) 24 NSWLR 146 SC at 153 where Rolfe J said that "[i]t would be strange ... if matters arising out of pre-contractual negotiations, which could be proved to the extent necessary to justify rectification, namely, by clear and convincing proof, could not be relied upon to found an estoppel by convention because of the source from which they arose". The conflict was noted but left unresolved by the New South Wales Court of Appeal in *Ryledar Pty Ltd v Euphoric Pty Ltd* (2007) 69 NSWLR 603 at [227] and *Franklins Pty Ltd v Metcash Trading Ltd* (2009) 76 NSWLR 603 at [34] and [577].

5 *Chartbrook Ltd v Persimmon Homes Ltd* [2009] AC 1101 at [47]

6 *The Parol Evidence Rule* (Law Com. No.154, 1986), para 1.7. The Commission later concluded (para 2.45) that the rule, "in so far as [it] can be said to have an independent existence", no longer has "the effect of excluding evidence which ought to be admitted if justice is to be done between the parties".

In the USA the rule has been described as a "treacherous bog in the field of contract law"[7] and as "a positive menace to the due administration of justice".[8] One leading commentator has said that "[i]n virtually every jurisdiction [of the USA], one finds irreconcilable cases, frequent changes in doctrine, confusion, and cries of despair",[9] and this might equally be regarded as a description of the position across the states of Australia. Actually, I feel sorry for Australian counsel and judges who regularly have to grapple with the rule. However, a solution is at hand. They can escape this "treacherous bog" by emigrating to New Zealand! Our judges have fewer constraints on finding and enforcing the parties' true bargain, and of course they have good rugby union teams to support!

Let me finish with three points. First, the scope of the parol evidence rule is most commonly raised in Australian cases when the issue is one of contract interpretation. Indeed, the rule is commonly understood as *either* a synonym for a plain meaning rule *or* the basis for excluding evidence of prior negotiations. Yet the rule as classically formulated has no application in such cases. As the greatest Contract lawyer of them all, Yale law professor Arthur Corbin, argued, "the terms of any contract must be given a meaning by interpretation before it can be determined whether an attempt is being made to 'vary or contradict' them".[10]

Secondly, the judgment of the New Zealand Supreme Court in the *Bathurst* case that Justice Leeming has mentioned repays careful study if one is seeking to bring about much-needed coherence in the law of contract interpretation. Well, I would say that, wouldn't I, given that the Court accepted arguments I have been harping on about for many years concerning both interpretation and implication of terms!

However, I have one caveat. Although I think the Court was right to jettison the rules forbidding resort to prior negotiations and subsequent conduct as aids to interpretation, I think it was wrong to hold that the issue is one of evidence and therefore governed by the provisions of our Evidence Act stating that all relevant evidence should ordinarily be admissible. This is because the meaning of a written contract has long been regarded as a question of law and, as a corollary, the permissible aids to determining that meaning have also been regarded as embodying rules or principles of the substantive law of contract. It is one thing to say that all relevant evidence is admissible in determining a question of fact – for example, did the defendant say anything to the plaintiff before the contract was formed about the matter in dispute and, if so, did it indicate assent to the plaintiff's understanding of that matter. It is quite another to say that, once these facts are proven, they can be determinative of the objective intention of the parties and hence the true meaning of the contract.

Finally, we must not lose sight of the fact that the great majority of interpretation disputes that come before the courts concern situations where the parties did not, at the time of formation, contemplate the issue that has arisen. Since there is no question, therefore, of their having formed an actual intention as to the meaning of the term in dispute, the law that we have talked about today won't be relevant. The task of the court will be to ascertain the meaning that the document would convey to a reasonable person with knowledge of the background. And any attempt by counsel in such cases to burden the court with a large volume of evidence

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7 *Chase Manhattan Bank v First Marion Bank* 437 F 2d 1040 (1971) at 1045.

8 WG Hale, "The Parol Evidence Rule" (1925) 4 Or L Rev 91 at 91.

9 EA Posner, "The Parol Evidence Rule, the Plain Meaning Rule, and the Principles of Contractual Interpretation" (1998) 146 U Pa L. Rev 533 at 540.

10 AL Corbin, *Corbin on Contracts* (rev ed, 1960) Vol 3, at §543 (pp 130–131).

concerning the parties' negotiations in an endeavour to establish an actual mutual intention that in reality simply did not exist ought to be stopped at the case management stage or lead to an adverse costs order.