The use of extrinsic evidence in aid of construction: a plea for pragmatism [1]

Introduction

1 Under the objective theory of contract the meaning of a contract is to be decided in accordance with what the terms of the contract would convey to a reasonable person in the position of the parties, rather than by reference to the subjective intentions of one, or even both, parties to the contract.[2]

2 The process of deciding the meaning of a written contractual term ordinarily involves objective consideration of –

(a) the text of the contractual term;

(b) the context within which the term exists (namely, the entire text of the contract and any other contract, document or statutory provision referred to in the text); and

(c) the commercial purpose or objects evidently intended to be secured by the contract.[3]

3 This process ordinarily occurs by reference to the contract alone, namely to the contractual text and contextual matters to which it has referred. Notably, there is no ambiguity threshold which must be crossed before it is legitimate to look to context in this way.[4]

4 But, in the process of deciding the meaning of a contractual term, the question often arises whether a party should be permitted to refer to contextual matters which are extrinsic to the language of the parties' agreement or what might be evident from it.

5 Traditionally the starting point to answering that question has been a statement of the operation of the parol evidence rule[5] and a consideration of the exceptions to it.[6] It is more common now simply to say that the ordinary course is that the process of construction occurs by reference to the contract alone (in the sense described above), but that sometimes recourse to events, circumstances and things external to the contract is necessary.

6 Of course, that begs the question as to how one can determine when recourse to events, circumstances and things external to the contract has become necessary. The famous *Codelfa* "true rule",[7] suggests that an ambiguity threshold must first be passed. The first task essayed by this paper is the identification of the current state of Australian appellate authorities on this question. It will become apparent that the law is not yet in

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1 Paper delivered for the Current Legal Issues Seminar Series 2016. The paper is a development of a paper initially delivered to the annual conference of the Bar Association of Queensland in February 2015. I acknowledge the valuable assistance in that task provided by my associate, Mr Tristan Pagliano.

2 See *Pacific Carriers Ltd v BNP Paribas* (2004) 218 CLR 451 at [22] per Gleeson CJ, Gummow, Hayne, Callinan and Heydon JJ; *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* (2004) 219 CLR 165 at [40] per Gleeson CJ, Gummow, Hayne, Callinan and Heydon JJ; *Wilkie v Gordian Runoff Ltd* (2005) 221 CLR 522 at [15] per Gleeson CJ, McHugh, Gummow and Kirby JJ; *International Air Transport Association v Ansett Australia Holdings Ltd* (2008) 234 CLR 151 at [8] per Gleeson CJ and at [53] per Gummow, Hayne, Heydon, Crennan and Kiefel JJ; *Electricity Generation Corporation v Woodside Energy Ltd* (2014) 251 CLR 640 at [35]; *Mount Bruce Mining Pty Ltd v Wright Prospecting Pty Ltd* (2015) 89 ALJR 990 at [46] per French CJ, Nettle and Gordon JJ.

3 *Mount Bruce Mining Pty Ltd v Wright Prospecting Pty Ltd* (2015) 89 ALJR 990 at [47] per French CJ, Nettle and Gordon JJ.

4 *Eureka Operations Pty Ltd v Viva Energy Australia Ltd* [2016] VSCA 95 at [45] per Santamaria, Ferguson, McLeish JJA.

5 See at [15] below.

6 See at [16] and [47] to [48] below.

7 See at [16] below.

a satisfactory state and that there is still a division of approach between intermediate courts of appeal.

7 The second task essayed by this paper is a brief summary of the law concerning the use to which extrinsic evidence may be put once any ambiguity threshold is met (if there is one). Although the law seeks to draw a clear line between the legitimate and illegitimate uses of such evidence, it is readily apparent that the line is sometimes difficult to draw. And there are still some areas in which an approach is taken which seems anomalous.

8 In view of these difficulties, one might speculate whether the law is in need of reform.

9 Indeed, serious suggestions have been made that there should be no exclusionary rules at all. Rather the law should simply let everything in. For example, in a 2014 working paper entitled "A Draft Australian Law of Contract" prepared in response to the Commonwealth Attorney General's discussion paper concerning reform to Australian contract law, Ellinghaus, Kelly and Wright recommended the abolition of the parol evidence rule. The learned authors would reform the law so that "[a]ll evidence that is relevant to identifying and interpreting the terms of a contract is admissible, including evidence of each party's actual intention".[8] The meaning of a contractual term would be that "intended by the parties, having regard to", amongst other things, "the parties' statements and other conduct before and after the contract was made".[9] If a party intends a term to have a particular meaning, and the other party is or should reasonably be aware of that intention, that is its meaning.[10]

10 I recoil with horror from the breadth of these suggested reforms of the law and reject the notion that they reflect a proper policy setting for the law of contract in this country. The plea for pragmatism made in the title of this paper reflects a concern that the pursuit of theoretical purity can sometimes occur with insufficient attention to feasibility and practical consequences.

11 The third task essayed by this paper is the development of an explanation of why, in circumstances in which the parol evidence rule would have applied, the proper policy setting of the law must continue to be one in which admissibility in aid of construction of events, circumstances and things external to the contract is exceptional rather than usual.

12 My hypothesis is that one way or the other, and whether by developments in substantive or procedural law, or both, our system of justice must manage the question of admissibility of extrinsic evidence in aid of construction in such a way as will permit of its occurrence only where it is of real utility and must hold the evidence out if it is not.

13 The final task essayed by this paper is to suggest some procedural strategies which may improve the efficient management of the reception and use of such evidence in cases in which its use is proposed. I will leave the task of development of the substantive law to others.

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8 Proposed article 36 of a draft Australian Contract Law.

9 Proposed article 42 of a draft Australian Contract Law.

10 Proposed article 43 of a draft Australian Contract Law.

The substantive law

Is there still an ambiguity threshold?

14 The standard articulation of the objective theory of contract bears repetition. The meaning of a contract is to be decided in accordance with what the terms of the contract would convey to a reasonable person in the position of the parties, rather than by reference to the subjective intentions of one, or even both, parties to the contract.

15 Where the revealed contractual intention is that the whole of the parties' agreement is contained in a written contract document, the parol evidence rule applies to exclude the use of extrinsic evidence in determining the meaning of the words used in the contract document.[11] Usually such an intention is sufficiently revealed by the production of a signed written instrument which appears on its face to be the final written expression of the full consensus of the parties.[12]

16 Of course, the Courts have long since recognised that there is more to the task of construction than simply working out the plain and ordinary meaning of the words used in the contractual text. The strict operation of the parol evidence rule has been the subject of a number of exceptions, the principal amongst which was Sir Anthony Mason's famous statement in *Codelfa Construction Pty Ltd v State Rail Authority (NSW)*[13] of the true rule. He wrote:

> 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.

17 This statement of the rule had been widely regarded as authority for the proposition that "ambiguity" (in the sense that the language is ambiguous or susceptible of more than one meaning) was a threshold issue on which the admissibility of extrinsic evidence turned. (The threshold is fairly low: the Western Australian Court of Appeal has recently treated the concept as encompassing not only where a term is open to more than one meaning but also where it is merely difficult to understand;[14] and also any situation in which the scope or applicability of a contract to the circumstances concerned is doubtful and not merely cases involving lexical, grammatical or syntactical ambiguity.[15])

18 However, it was not too long after the articulation of the "true rule" that suggestions emerged that it was inappropriate to think of an "ambiguity threshold" to the admissibility of extrinsic evidence because language always needs to be interpreted in context. In *Investors Compensation Scheme Ltd v West Bromwich Building Society*,[16] Lord Hoffman famously summarised relevant principles in a way which rejected any notion of an ambiguity threshold, stating, amongst other things, that:

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11 *State Rail Authority of New South Wales v Heath Outdoor Pty Ltd* (1986) 7 NSWLR 170 at 191 per McHugh JA and *Nemeth v Bayswater Road Pty Ltd* [1988] 2 Qd R 406 at 413 per McPherson J.

12 The production of such a document will give rise to a prima facie presumption that the intention of the parties is that the terms of the contract are wholly contained in the writing, the force of which will vary according to a variety of circumstances: *IPN Medical Centres Pty Ltd v Van Houten & Anor* [2015] QSC 204 at [45] per Jackson J citing *Nemeth v Bayswater Road Pty Ltd* [1988] 2 Qd R 406 at 414. The presumption is often supported by the fact of an entire agreement clause within the signed contractual document.

13 (1982) 149 CLR 337 at 352.

14 *McCourt v Cranston* [2012] WASCA 60 at [24] per Pullin JA with whom Newnes JA agreed.

15 *Hancock Prospecting Pty Ltd v Wright Prospecting Pty Ltd* (2012) 45 WAR 29 at [76] per McClure P with whom Newnes JA and Le Miere J agreed. See also the discussion by Sloss J in *Bisognin v Hera Project Pty Ltd* [2016] VSC 75 at [146] to [157].

16 [1998] 1 All ER 98 at 114 to 115.

> … Subject to the requirement that it should have been reasonably available to the parties and to the exception [that previous negotiations and declarations of subjective intent are excluded], [the background knowledge which the reasonable person is assumed to have had] includes absolutely anything which would have affected the way in which the language of the document would have been understood by a reasonable man.

19 In *Bank of Credit and Commerce International SA v Ali*,[17] Lord Hoffman clarified that in making that statement he was suggesting that there was "no conceptual limit to what can be regarded as background".

20 In a paper delivered in 2009, Sir Anthony Mason himself retreated from the notion of an ambiguity threshold.[18] Relevantly:

(a) He thought that the favoured approach was that ambiguity should not be regarded as a necessary threshold. In this regard he observed (emphasis added):

> It was that idea that I was endeavouring to express in *Codelfa*, albeit imperfectly, because I recognised that ambiguity may not be a sufficient gateway; the gateway **should be wide enough to admit extrinsic material which is capable of influencing the meaning of the words of the contract**. The modern point of criticism is that one should not have been thinking in terms of gateway. At the time, however, it was natural to do so because it stressed the importance of the natural and ordinary meaning of the words used by the parties in their written instrument and it respected the difference between interpretation and rectification.

(b) He generally supported Lord Hoffmann's restatement of principles or guidelines and thought that the High Court of Australia had endorsed them in *Pacific Carriers Ltd v BNP Paribas*,[19] and in *Toll (FGCT) Pty Ltd v Alphafarm Pty Ltd*.[20]

(c) He did sound one word of caution, namely that he doubted that the Hoffmann restatement promoted cost-efficient litigation and thought it might lead to attempts to achieve rectification through interpretation.

21 Nevertheless, by early 2011 it seemed clear that it was a corollary of the objective theory of contract itself that identification of ambiguity in the terms of an agreement was not a necessary precursor to the examination of surrounding circumstances. This proposition had the support of multiple intermediate appellate courts:

(a) New South Wales:

(i) *Franklins Pty Ltd v Metcash Trading Ltd*;[21]

(ii) *Synergy Protection Agency Pty Ltd v North Sydney Leagues' Club Ltd*;[22]

(iii) *Masterton Homes Pty Ltd v Palm Assets Pty Ltd*;[23] and

(iv) *Movie Network Channels Pty Ltd v Optus Vision Pty Ltd*.[24]

(b) Federal Court:

(i) *Lion Nathan Australia Pty Ltd v Coopers Brewery Ltd*;[25] and

(ii) *Ralph v Diakyne Pty Ltd*.[26]

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17 [2002] 1 AC 251 at 269.

18 Sir Anthony Mason, "Opening Address" (2009) 25 Journal of Contract Law 1 at 3.

19 (2004) 218 CLR 451 at 462.

20 (2004) 219 CLR 165 at 179.

21 (2009) 76 NSWLR 603 at [14] to [18] per Allsop P, at [49] per Giles JA and at [239] to [305] per Campbell JA.

22 [2009] NSWCA 140 at [22] per Allsop P (with which Tobias and Basten JJA agreed).

23 (2009) 261 ALR 382 at [3] per Allsop P (with whom Basten JA agreed).

24 [2010] NSWCA 111 at [68] per Macfarlan JA (with whom Young JA and Sackville AJA agreed).

25 (2006) 156 FCR 1 at [51] per Weinberg J, at [100] per Kenny J and at [238] per Lander J.

(c) Victoria: *MBF Investments Pty Ltd v Nolan*.[27]

22 The judges in these cases had discerned in the High Court decisions which established the orthodoxy of the objective theory of contract[28] departure from the *Codelfa* rule which required ambiguity as a prerequisite for admissibility. They had noted that in stating the objective theory of contract, the High Court had done so in absolute terms and with no reference to any qualifications concerning the need to discern ambiguity. That proposition was certainly true and it was at least arguable that by so doing the High Court was favouring Lord Hoffman's approach. Even Sir Anthony Mason thought that was the position. It suffices merely to refer to the following passage from *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* (citations omitted, emphasis added):[29]

> This Court, in *Pacific Carriers Ltd v BNP Paribas*, has recently reaffirmed the principle of objectivity by which the rights and liabilities of the parties to a contract are determined. It is not the subjective beliefs or understandings of the parties about their rights and liabilities that govern their contractual relations. What matters is what each party by words and conduct would have led a reasonable person in the position of the other party to believe. **References to the common intention of the parties to a contract are to be understood as referring to what a reasonable person would understand by the language in which the parties have expressed their agreement. The meaning of the terms of a contractual document is to be determined by what a reasonable person would have understood them to mean. That, normally, requires consideration not only of the text, but also of the surrounding circumstances known to the parties, and the purpose and object of the transaction**.

23 In 2011, however, the notion that intermediate courts of appeal had correctly identified that the High Court intended to depart from the *Codelfa* rule was the subject of trenchant criticism by the High Court. The following observations may be made:

(a) In *Byrnes v Kendle*,[30] Heydon and Crennan JJ emphasised that the observations in relevant intermediate courts of appeal which suggested a relaxation of the *Codelfa* approach must be read in the light of the fact that in *Royal Botanic Gardens and Domain Trust v South Sydney City Council*[31] a plurality comprising Gleeson CJ, Gaudron, McHugh, Gummow and Hayne JJ had said[32] that until the High Court had decided on whether there were differences between the arguably more liberal British approach and the approach authorised by *Codelfa*, and if so which should be preferred, *Codelfa* should be followed in Australia.

(b) *Royal Botanic Gardens* was a case in which the Court was construing a deed between the "Trustees of the Domain" called "the Lessors" and, on the other part, the Council of the City of Sydney called "the Lessee", which governed the construction by the latter of the parking station beneath the Domain in Sydney. The Royal Botanic Gardens was the statutory successor of the Lessors. At issue was a clause concerning the determination of rent and whether the Lessors were bound by the words "in making any such determination the Trustees may have regard to additional costs and expenses which they may incur in regard to the surface of the Domain above or in the vicinity of the parking station" to take into account only such additional costs or could take wider considerations into account. Gleeson CJ, Gaudron, McHugh, Gummow and Hayne JJ found –

(i) the relevant clause was ambiguous;

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26 [2010] FCAFC 18 at [46] to [47] per Finn, Sundberg and Jacobson JJ.
27 (2011) 37 VR 116 at [197] to [203] per Neave, Redlich and Weinberg JJA.
28 See footnote 2 above.
29 (2004) 219 CLR 165 at [40] per Gleeson CJ, Gummow, Hayne, Callinan and Heydon JJ.
30 (2011) 243 CLR 253 at footnote 135.
31 (2002) 240 CLR 45.
32 (2002) 240 CLR 45 at [39].

(ii) it was appropriate to take into account the following surrounding circumstances:

A. the parties to the transaction were two public authorities;

B. the primary purpose of the transaction was to provide a public facility, not a profit;

C. the lessee was responsible for the substantial cost of construction of the facility;

D. the facility was to be constructed under the lessors' land and would not interfere with the continued public enjoyment of that land for its primary object, recreation;

E. the parties' concern was to protect the lessor from financial disadvantage from the transaction; and

F. the only financial disadvantage to the lessor which the parties identified related to additional expense which it would or might incur immediately or in the future; and

(iii) the clause was to be interpreted as exhaustively stating the considerations which could be taken into account in making a rental determination.

(c) Given that the clause had been found to be ambiguous, the observation made about *Codelfa* was necessarily obiter, but it was made in a joint judgment of five High Court justices and then re-emphasised by two further High Court justices in *Byrnes v Kendle*. Without more, the two cases would be a powerful reminder to courts below to keep following *Codelfa* until the High Court said the contrary.

(d) The point was then re-made in robust observations made in a decision made on a special leave application by Gummow, Heydon and Bell JJ in *Western Export Services Inc v Jireh International Pty Ltd*.[33] Although decisions on special leave applications do not carry the weight of precedent, they may nevertheless be thought to be a strong indication of the approach of the High Court. Their Honours wrote:

> [2] The primary judge had referred to what he described as "the summary of principles" in *Franklins Pty Ltd v Metcash Trading Ltd*. The applicant in this court refers to that decision and to *MBF Investments Pty Ltd v Nolan* as authority rejecting the requirement that it is essential to identify ambiguity in the language of the contract before the court may have regard to the surrounding circumstances and object of the transaction. The applicant also refers to statements in England said to be to the same effect, including that by Lord Steyn in *R (Westminster City Council) v National Asylum Support Service*.
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> [3] 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 and Wilson JJ, 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.
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> [4] 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.

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[33] (2011) 282 ALR 604.

24 In light of that trilogy of High Court reminders that overruling *Codelfa* was a matter for the High Court, and not intermediate courts of appeal, one would have expected to find a degree of circumspection in subsequent cases in those Courts when dealing with the question whether the law required an ambiguity threshold to be met. It seemed that the High Court had deliberately pressed the brake on the developments which had been occurring in the Courts below.

25 To an extent, that is what happened and some decisions in intermediate courts of appeal appeared to retreat from the full flourish of the "ambiguity is unnecessary" proposition (or at least to treat the proposition with some reserve):

(a) In New South Wales: see *Rinehart v Welker*,[34] *Cordon Investments Pty Ltd v Lesdor Properties Pty Ltd*,[35] and *Moorebank Recyclers Pty Ltd v Tanlane Pty Ltd*.[36]

(b) In Victoria: see *Reading Properties Pty Ltd v Mackie Group Pty Ltd*,[37] and *Retirement Services Australia (RSA) Pty Ltd v 3143 Victoria St Doncaster Pty Ltd*.[38]

(c) In Western Australia: see *McCourt v Cranston*,[39] *Hancock Prospecting Pty Ltd v Wright Prospecting Pty Ltd*,[40] *MacKinlay v Derry Dew Pty Ltd*,[41] *Director General, Department of Education v United Voice (WA)*,[42] and *Cape Lambert Resources Ltd v MCC Australia Sanjin Mining Pty Ltd*.[43]

(d) In Queensland, the Court of Appeal seemed still to adhere to the *Codelfa* orthodoxy: see *Velvet Glove Holdings Pty Ltd v Mount Isa Mines Ltd*.[44] In that case Justice Philippides specifically noted the *Byrnes v Kendle* warning about *Codelfa*.

26 The next significant step was the decision of the High Court in *Electricity Generation Corporation v Woodside Energy Ltd*.[45] It must first be noted that there was no dispute between the parties and therefore no dispute before the Court concerning the admissibility of extrinsic evidence and no mention made of the issue in the judgment. In relation to the construction of a "reasonable endeavours" clause in a commercial contract, French CJ, Hayne, Crennan and Kiefel JJ made the following statement:[46]

> The meaning of the terms of a commercial contract is to be determined by what a reasonable businessperson would have understood those terms to mean. That approach is not unfamiliar. As reaffirmed, it will require consideration of the language used by the parties, the surrounding circumstances known to them and the commercial purpose or objects to be secured by the contract. Appreciation of the commercial purpose or objects is facilitated by an understanding "of the genesis of the transaction, the background, the context [and] the market in which the parties are operating."

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34 [2012] NSWCA 95 at [116] per Bathurst CJ with whom Young JA agreed.
35 [2012] NSWCA 184 at [52] per Bathurst CJ with whom Macfarlan and Meagher JJA agreed.
36 [2012] NSWCA 445 at [174] per Bathurst CJ, Beazley and Meagher JJA.
37 (2012) 37 VR 194 at [21] to [23] per Warren CJ, Mandie JA and Judd AJA.
38 (2012) 37 VR 486 at [50] per Warren CJ and Harper JA and Robson AJA.
39 [2012] WASCA 60 at [20] to [23] per Pullin JA with whom Newnes JA agreed.
40 (2012) 45 WAR 29 at [76] per McClure P with whom Newnes JA and Le Miere J agreed.
41 [2014] WASCA 24 per Pullin JA at [54] with whom Newnes JA agreed.
42 [2013] WASCA 287 at [19] per Pullin J with whom Le Miere J agreed.
43 (2013) 298 ALR 666 at [107] per McLure P.
44 [2011] QCA 312 at [93] to [97] per Philippides J with whom Fraser and White JJA agreed.
45 (2014) 251 CLR 640.
46 *Electricity Generation Corporation v Woodside Energy Ltd* (2014) 251 CLR 640 at [35].

27 This reaffirmation of the objective theory of contract without articulating any reference to ambiguity as a threshold question was seen by some intermediate courts of appeal as articulating a position contrary to that stated in *Jireh*.

28 Thus:

(a) In *Mainteck Services Pty Ltd v Stein Heurtey SA*,[47] the New South Wales Court of Appeal held that *Woodside* was inconsistent with *Jireh*. Leeming JA (with whom Ward JA and Emmett AJA agreed) went on to explain why he held the view that the question whether ambiguity exists could never be evaluated without regard to surrounding circumstances and commercial purpose or objects. His Honour thought that was not inconsistent with *Codelfa* because the conclusion that language had a plain meaning was itself a conclusion which could not be reached until one had regard to context.

(b) In *Stratton Finance Pty Ltd v Webb*,[48] the Full Court of the Federal Court (Allsop CJ, Siopis and Flick JJ) agreed with that view.

(c) In *Newey v Westpac Banking Corporation*,[49] Basten, Meagher and Gleeson JJA took a similar view.

29 On the other hand:

(a) In *Technomin Australia Pty Ltd v Xstrata Nickel Australasia Operations Pty Ltd*,[50] the Western Australia Court of Appeal (McLure P, Newnes and Murphy JJA) carried out what might be thought to be a more orthodox analysis of the post-*Codelfa* cases and concluded that the *Jireh* injunction should be followed until the High Court decided otherwise.[51] Murphy JA observed:[52]

> Also, the following observations might be made about the law post-*Codelfa*. First, the passage in *Codelfa* (352) does not appear to have been subject of express consideration in the High Court since *Royal Botanic* [39]. Secondly, it might be thought that the authorities up to the time of [*Woodside*] are not necessarily inconsistent with a requirement of ambiguity. Thirdly, a case as significant as *Codelfa* in the operation of the commercial law in Australia for over 30 years is unlikely to have been impliedly overruled. Fourthly, in [*Woodside*], French CJ, Hayne, Crennan and Kiefel JJ 'reaffirmed' the High Court's earlier decisions. [*Woodside*] does not appear to provide a departure from them. Fifthly, the question of whether evidence of surrounding circumstances is inadmissible in the absence of ambiguity does not appear to have been canvassed in argument in [*Woodside*], nor isolated for determination.

(b) In *State of Victoria v R*,[53] the Victorian Court of Appeal seems to adhere to the *Codelfa* rule, but a differently constituted Court in *Leon Mancini & Sons Pty Ltd v Tallowate Pty Ltd*[54] had earlier referred to but not engaged with the controversy.

(c) In Queensland the Court of Appeal had noted the existence of the debate but expressly not yet decided the point: see footnote 2 in *Jakeman Constructions Pty Ltd v Boshoff*.[55] In *Watson v Scott*,[56] McMurdo P (with whom Morrison and

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47 (2014) 89 NSWLR 633 at [72] to [86] per Leeming JA with whom Ward JA and Emmett AJA agreed.
48 (2014) 314 ALR 166 at [36] to [40].
49 [2014] NSWCA 319 at [86] to [90].
50 (2014) 48 WAR 261.
51 See eg *Technomin Australia Pty Ltd v Xstrata Nickel Australasia Operations Pty Ltd* (2014) 48 WAR 261 at [35] to [45] per McLure P (with whom Newnes JA agreed) and at [190] to [216] per Murphy JA.
52 *Technomin Australia Pty Ltd v Xstrata Nickel Australasia Operations Pty Ltd* (2014) 48 WAR 261 at [215].
53 [2014] VSCA 311 at [92] per Nettle, Osborn, Whelan JJA.
54 [2014] VSCA 306 at [45] per Neave and Kyrou JJA and Ginnane AJA.
55 [2014] QCA 354 per Fraser JA with whom Mullins and Henry JJ agreed.

Philippides JJA agreed) summarised relevant principle in a traditional way.[57] As to this:

(i) Her Honour's summary was in these terms (citations omitted, emphasis added):

> In construing the terms of the agreement, this Court must discover the objective intention of the parties as embodied in the words used in the agreement. The parties' subjective intentions are irrelevant. The meaning of the agreement is to be determined by what a reasonable person would have understood the terms to mean; evidence of pre-contractual negotiations is only admissible if it provides knowledge of surrounding circumstances and relates to objective facts known directly or inferentially to both parties: *Byrnes v Kendle*. The agreement should be construed in a commercially sensible way although minds may differ as to what equates to "business commonsense": *Maggbury Pty Ltd v Hafele Australia Pty Ltd*. In construing a commercial contract a court should know the commercial purpose of the contract. This will usually require knowledge of the background and the context to the transaction. The apparent purpose or object can be inferred from the express and implied terms of the contract and from any admissible evidence of surrounding circumstances. **But evidence of surrounding circumstances is admissible to assist in the interpretation of a contract only if the language is ambiguous or susceptible of more than one interpretation; it is not admissible to contradict the language of the contract when it has a plain meaning: *Codelfa Construction Pty Ltd v State Rail Authority (NSW)* and *Western Export Services Inc v Jireh International Pty Ltd*. Where the terms of the agreement are unambiguous, extrinsic evidence may inform but cannot contradict the meaning of the contract.** Courts in construing an agreement must find the objective meaning of what the parties agreed to, not what they meant to agree to.

(ii) It should be observed that, taken at face value, the second of the two sentences emphasised seems to be inconsistent with the first. The two sentences literally would suggest that, if the terms are unambiguous, on the one hand extrinsic evidence is not admissible to assist in interpretation, but on the other hand extrinsic evidence may be permitted to inform without contradicting. It is to be doubted that that represents her Honour's intention. The case cited for the proposition in the second sentence does not support it and in the immediately following part of the judgment her Honour characterises the principles as requiring a decision whether text is susceptible of more than one meaning so that extrinsic evidence is admissible in aid of construction.

30 To my mind, at least before October 2015 when the High Court published their reasons in *Mount Bruce Mining Pty Ltd v Wright Prospecting Pty Ltd*,[58] the most influential articulations on either side of the debate, at least in Australia were, on the one hand, the New South Wales Court of Appeal decisions of *Franklins* (pre-*Woodside*) and *Mainteck* (post-*Woodside*), and on the other hand, the Western Australia Court of Appeal in *Techomin*, itself the culmination of a line of Western Australian authorities adhering to a more traditional view.

31 What then of *Mount Bruce*? It was a case involving the construction of a 1970 agreement in which a party agreed to pay a royalty in respect of iron ore mined from "MBM area" in the Pilbara and agreed that the royalty would be payable by "all persons or corporations deriving title through or under [MBM]". The Court regarded the questions of the proper meaning of "MBM area" and what was necessary to derive title "through or under" as ambiguous. Thus the observations which they made

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56 [2015] QCA 267.

57 *Watson v Scott* [2015] QCA 267 at [30].

58 (2015) 89 ALJR 990.

touching upon the controversy concerning the admissibility of extrinsic evidence were, necessarily *obiter*. There were three judgments, the relevant passages of each of which are worthy of examination.

32 Kiefel and Keane JJ wrote (citations omitted, emphasis added):

> 107 A construction of the words "deriving title" in cl 24(iii) as meaning a chain of title analogous to that in systems of land registration could only be arrived at by placing undue emphasis upon those words to the exclusion of other words. In any event the possibility that such a meaning could have been intended is negated by reference to the circumstances surrounding the meaning of the 1970 Agreement and in particular the facts known to the parties. To the extent that there is any ambiguity arising from these words it is resolved in favour of the construction referred to above.
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> 108 That regard may be had to the mutual knowledge of the parties to an agreement in the process of construing it is evident from *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales*. Mason J, with whom Stephen and Wilson JJ agreed, accepted that there may be a need to have regard to the circumstances surrounding a commercial contract in order to construe its terms or to imply a further term. In the passages preceding what his Honour described as the "true rule" of construction, his Honour identified "mutually known facts" which may assist in understanding the meaning of a descriptive term or the "genesis" or "aim" of the transaction. His Honour had earlier referred to the judgment of Lord Wilberforce in *Prenn v Simmonds*, where it was said that:
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> > "[t]he time has long passed when agreements … were isolated from the matrix of facts in which they were set and interpreted purely on internal linguistic considerations."
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> 109 In a passage from *DTR Nominees Pty Ltd v Mona Homes Pty Ltd*, to which Mason J referred, it was said that the object of the exercise was to show that "the attribution of a strict legal meaning would 'make the transaction futile'". In *Electricity Generation Corporation v Woodside Energy Ltd*, French CJ, Hayne, Crennan and Kiefel JJ explained that a commercial contract should be construed by reference to the surrounding circumstances known to the parties and the commercial purpose or objects to be secured by the contract in order to avoid a result that could not have been intended.
>
> 110 **The "ambiguity" which Mason J said may need to be resolved arises when the words are "susceptible of more than one meaning." His Honour did not say how such an ambiguity might be identified. His Honour's reasons in Codelfa are directed to how an ambiguity might be resolved**.
>
> 111 In reasons for the refusal of special leave to appeal given **in *Western Export Services Inc v Jireh International Pty Ltd*, reference was made to a requirement that it is essential to identify ambiguity in the language of the contract before the court may have regard to the surrounding circumstances and the object of the transaction. There may be differences of views about whether this requirement arises from what was said in *Codelfa*. This is not the occasion to resolve that question**.
>
> 112 It should, however, be observed that **statements made in the course of reasons for refusing an application for special leave create no precedent and are binding on no one**. An application for special leave is merely an application to commence proceedings in the Court. Until the grant of special leave there are no proceedings *inter partes* before the Court.
>
> 113 **The question whether an ambiguity in the meaning of terms in a commercial contract may be identified by reference to matters external to the contract does not arise in this case and the issue identified in Jireh has not been the subject of submissions before this Cour**t. To the extent that there is any possible ambiguity as to the meaning of the words "deriving title through or under", it arises from the terms of cl 24(iii) itself.

33 The following observations may be made about this passage:

(a) Their Honours implicitly acknowledge that *Codelfa* remains binding authority for other Australian Courts. Their Honours seem also to acknowledge the existence, presently, of an ambiguity threshold.

(b) They made three points about *Jireh*.

(c) First, *Jireh* had referred to a requirement that it was essential that the requisite ambiguity be identifiable in the language of the contract (as opposed to being demonstrable by extrinsic evidence).

(d) Second, they thought that there might be differences of view as to whether that requirement did arise from what was said in *Codelfa*. It was plain that their Honours regarded that question as not yet resolved by the High Court.

(e) Third, they observed about *Jireh* that statements made in the course of reasons for refusing an application for special leave create no precedent and are binding on no one.

(f) The point about which their Honours thought there might be differences of view is probably to be regarded as at least a reference to latent ambiguity i.e. cases where ambiguity becomes apparent only when the language is applied to the factual situation. The concept was explained by Lord Wrenbury in *Great Western Railway and Midland Railway v Bristol Corporation*[59] in these terms (citations omitted):

> The words of the instrument may be perfectly plain and unambiguous - for example, "My nephew, Joseph Grant" or "fair market price", but if, from the surrounding circumstances, when you come to apply the instrument, you find that there are two persons who will satisfy the words "my nephew Joseph Grant", or two markets to which the parties may have been referring, there is a latent ambiguity.

(g) It is to be doubted, however, that their Honours were limiting the proposition to latent ambiguity in that sense. Their reference to *DTR Nominees Pty Ltd v Mona Homes Pty Ltd*[60] suggests they may contemplate the admissibility of such evidence to demonstrate that giving language its strict legal meaning would be to make the transaction futile. The passage from *DTR Nominees Pty Ltd v Mona Homes Pty Ltd* to which they referred was this:[61]

> A court may admit evidence of surrounding circumstances in the form of "mutually known facts" "to identify the meaning of a descriptive term" and it may admit evidence of the "genesis" and objectively the "aim" of a transaction to show that the attribution of a strict legal meaning would "make the transaction futile" (*Prenn v Simmonds*). But it cannot receive oral evidence from one party as to its intentions and construe the contract by reference to those intentions.

(h) The result is that the judgment accepts *Codelfa* but suggests that it is unresolved whether it is possible to demonstrate the existence of ambiguity by reference to extrinsic evidence.

34 French CJ, Nettle and Gordon JJ wrote (citations omitted, emphasis added):

> 46 The rights and liabilities of parties under a provision of a contract are determined objectively by reference to its text, context (the entire text of the contract as well as any contract, document or statutory provision referred to in the text of the contract) and purpose.
>
> 47 In determining the meaning of the terms of a commercial contract, it is necessary to ask what a reasonable businessperson would have understood those terms to mean. That enquiry will require consideration of the language used by the parties in the contract, the circumstances addressed by the contract and the commercial purpose or objects to be secured by the contract.
>
> 48 Ordinarily, this process of construction is possible by reference to the contract alone. **Indeed, if an expression in a contract is unambiguous or susceptible of only one meaning, evidence of surrounding circumstances (events, circumstances and things external to the contract) cannot be adduced to contradict its plain meaning**.

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59 (1918) 87 LJ Ch 414 at 429.
60 (1978) 138 CLR 423.
61 *DTR Nominees Pty Ltd v Mona Homes Pty Ltd* (1978) 138 CLR 423 at 429.

> 49 However, sometimes, recourse to events, circumstances and things external to the contract is necessary. It may be necessary in identifying the commercial purpose or objects of the contract where that task is facilitated by an understanding "of the genesis of the transaction, the background, the context [and] the market in which the parties are operating". It may be necessary in determining the proper construction where there is a constructional choice. **The question whether events, circumstances and things external to the contract may be resorted to, in order to identify the existence of a constructional choice, does not arise in these appeals**.
>
> 50 Each of the events, circumstances and things external to the contract to which recourse may be had is objective. What may be referred to are events, circumstances and things external to the contract which are known to the parties or which assist in identifying the purpose or object of the transaction, which may include its history, background and context and the market in which the parties were operating. What is inadmissible is evidence of the parties' statements and actions reflecting their actual intentions and expectations.
>
> 51 Other principles are relevant in the construction of commercial contracts. Unless a contrary intention is indicated in the contract, a court is entitled to approach the task of giving a commercial contract an interpretation on the assumption "that the parties ... intended to produce a commercial result". Put another way, a commercial contract should be construed so as to avoid it "making commercial nonsense or working commercial inconvenience".
>
> 52 **These observations are not intended to state any departure from the law as set out in *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* and *Electricity Generation Corporation v Woodside Energy Ltd*. We agree with the observations of Kiefel and Keane JJ with respect to *Western Export Services Inc v Jireh International Pty Ltd***.

35 The following observations may be made about this passage:

(a) Their Honours explicitly acknowledged (at [52]) that *Codelfa* remains binding authority for other Australian Courts, in terms which suggested that nothing in *Woodside* could be regarded as overruling anything in *Codelfa*.

(b) Their Honours explicitly restated (at [48]), the statement from *Codelfa* which articulates the ambiguity threshold. However, curiously, in stating that rule, they made footnote references both to the relevant passage from *Codelfa* and to the paper to which I have earlier referred in which Sir Anthony Mason retreated from the ambiguity threshold. The former reference supports the statement about an ambiguity threshold. The latter does not.

(c) Moreover, their Honours expressly agreed with what Kiefel and Keane JJ had said about *Jireh*. Evidently, they too thought there was room to argue whether ambiguity had to be identifiable in the language of the contract (as opposed to being demonstrable by extrinsic evidence). They made the same point themselves explicitly in their observation as to construction choice (at [49]).

36 Bell and Gageler JJ wrote (citations omitted, emphasis added):

> 118 **These appeals do not raise** an important question on which intermediate courts of appeal are currently divided. That **question is whether ambiguity must be shown before a court interpreting a written contract can have regard to background circumstances**.
>
> 119 Until that question is squarely raised in and determined by this Court, the question remains for other **Australian courts to determine on the basis that *Codelfa Construction Pty Ltd v State Rail Authority of New South Wales* remains binding authority. That point, which of itself says nothing about the scope of the holding in Codelfa**, was made in the joint reasons for judgment in *Royal Botanic Gardens and Domain Trust v South Sydney City Council*. The point was reiterated, but taken no further, in the joint reasons for refusing special leave to appeal in *Western Export Services Inc v Jireh International Pty Ltd*. It should go without saying that reasons for refusing special leave to appeal in a civil proceeding are not themselves binding authority.

> 120 The question whether ambiguity must be shown before a court interpreting a written contract may have regard to background circumstances does not arise for determination in these appeals because the parties agree that the terms "MBM area" in cl 2.2 and "through or under" in cl 3.1 of the 1970 Agreement are ambiguous. The parties also agree, consistently with numerous recent statements of principle in this Court, that the proper interpretation of each of those terms is to be determined by reference to what reasonable businesspersons having all the background knowledge then reasonably available to the parties would have understood those terms to have meant as at 5 May 1970.

37 The following observations may be made about this passage:

(a) Their Honours' view seems to be that the question whether ambiguity must be shown before a court interpreting a written contract can have regard to background circumstances is a question which has not yet been squarely raised and determined by the High Court.

(b) Their Honours' acknowledgement of the continued binding authority of *Codelfa* and statement that making that point "says nothing about the scope of the holding in *Codelfa*" must be construed in light of that expression of view. This seems to be an acceptance of the proposition that *Codelfa* is not to be regarded as binding authority that there is an ambiguity threshold.

(c) Their Honours' observations that *Jireh* is not binding authority must be accepted, but their suggestion that *Jireh* went no further than to say that *Codelfa* was still authority, seems, with respect, wrong: cf *Jireh* at [2] to [3] quoted at [23(d)] above. It was, in any event, inconsistent with the observations by Kiefel and Keane JJ (with whom French CJ, Nettle and Gordon JJ agreed) about *Jireh*.

38 Where does that leave the current state of the debate?

39 The following propositions may be advanced:

(a) *Codelfa* remains binding authority. Nothing in *Woodside* (or, for that matter, *Pacific Carriers Ltd v BNP Paribas* or *Toll (FGCT) Pty Ltd v Alphafarm Pty Ltd*) should be regarded as overruling anything in *Codelfa*.

(b) But just what *Codelfa* is binding authority for (in this area of discourse), is much more debatable.

(c) The *Codelfa* "true rule" that if an expression in a contract is unambiguous or susceptible of only one meaning, evidence of surrounding circumstances (events, circumstances and things external to the contract) cannot be adduced to contradict its plain meaning, should presently be regarded as authoritative.

(d) However, the High Court has not yet resolved the question whether –

(i) an ambiguity in the meaning of terms in a commercial contract; or

(ii) the existence of a constructional choice,

may be identified by reference to matters external to the contract. Accordingly, at least in these respects (and Bell and Gageler JJ may go further) that is a question for courts below to resolve.

(e) In at least these regards, the High Court has expressly removed the brake on development of the law in the courts below which had been perceived to have been imposed by the *Jireh* decision.

40 Have intermediate courts of appeal which have adverted to the *Mount Bruce* decision yet resolved these questions?

41 As at 16 May 2016, the New South Wales Court of Appeal had not found it necessary by reference to the *Mount Bruce* decision to consider whether ambiguity might be identified by reference to matters external to the contract. However in *Mainteck* and *Newey* the Court had earlier and expressly reached that conclusion. There is no reason to think that the position in New South Wales will change.

42 That proposition receives at least some confirmation in *Todd v Alterra at Lloyds Ltd)*,[62] a decision of the Full Court of the Federal Court. In that decision, Beach J expressed the view that *Mount Bruce* recognised, at least implicitly, that *Codelfa* may not rule out an approach which first uses context to ascertain otherwise latent textual uncertainty or ambiguity. (The two other members of the Court did not find it necessary to examine this issue.) His Honour then expressed agreement with the approaches taken earlier by Allsop P (as he then was) in *Franklins Pty Ltd v Metcash Trading Ltd*,[63] Leeming JA's analysis in *Mainteck*,[64] and *Stratton Finance Pty Ltd v Webb*[65] per Allsop CJ, Siopis and Flick JJ.

43 In Victoria, the Court of Appeal has (as at 16 May 2016) not found it necessary to consider whether ambiguity might be identified by reference to matters external to the contract:

(a) In *Schreuders v Grandiflora Nominees Pty Ltd*,[66] Kyrou, Ferguson and McLeish JJA restated the *Codelfa* exclusionary proposition, citing *Codelfa* and the relevant passages from the judgment of French CJ, Nettle and Gordon JJ's in *Mount Bruce* that I have outlined above, but took the matter no further.

(b) In *Regreen Asset Holdings Pty Ltd v Castricum Brothers Australia Pty Ltd*,[67] Warren CJ, Kyrou and McLeish JA acknowledged the debate about the current status of the *Codelfa* rule but did not consider it necessary to discuss the debate further.

(c) In *Eureka Operations Pty Ltd v Viva Energy Australia Pty Ltd*,[68] Santamaria, Ferguson and McLeish JJA acknowledged that ambiguity might still have a role to play when considering the admissibility of matters external to the contract, but did not find it necessary to consider the matter further.

44 As far as may be ascertained as at 16 May 2016, the Courts of Appeal of Western Australia and the Queensland have not sought to resolve the question or to develop the law otherwise than they already had.

45 The division in authority earlier identified still exists. And there are practical problems in the prospects of the division ever being resolved as part of the *ratio decidendi* of a High Court decision. For that to happen one would have to have a contract which truly was unambiguous and in respect of which courts below had rejected the admissibility of extrinsic evidence by the application of an ambiguity threshold. The problem is exacerbated by the fact that ambiguity is a low threshold and not many cases in which the contract is truly unambiguous are worth taking to the High Court.

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62 [2016] FCAFC 15.
63 (2009) 76 NSWLR 603 at [14] to [17].
64 *Mainteck Services Pty Ltd v Stein Heurtey SA* (2014) 89 NSWLR 633 at [71] to [80].
65 (2014) 314 ALR 166 at 174 [40].
66 [2015] VSC 443.
67 [2015] VSCA 286 at [77].
68 [2016] VSCA 95 at [48].

The limits on the use of extrinsic evidence

46 What can presently be said about the use of extrinsic evidence, putting to one side the question whether ambiguity is still a prerequisite?

47 The Victorian Court of Appeal decision of *Retirement Services Australia (RSA) Pty Ltd v 3143 Victoria St Doncaster Pty Ltd*[69] identified the following principal exceptions to the parol evidence rule:

(a) First, extrinsic evidence which tends to establish objective background facts known to both parties.

(b) Second, extrinsic evidence which assists in the identification of the subject matter of the contract.

(c) Third, where the parties have refused to include in their contract a provision which would give effect to something which is subsequently suggested to be the presumed intention of persons in their position, evidence of that refusal is admissible with a view to negativing the alleged presumed intention.[70]

(d) Fourth, the "private dictionary" principle, in which evidence is admissible that the parties habitually used words in an unconventional sense in order to support an argument that words in their contract should bear a similar unconventional meaning.[71]

(e) Finally, of course, cases which are properly to be regarded as outside the operation of the rule because they involve pursuit of extra-contractual remedies, such as estoppel or rectification (or, it would follow, remedies under statute).

48 A category of cases which is difficult to fit within those exceptions and which strikes one as anomalous is cases concerning the construction of general words in releases. Recently, in *IBM v State of Queensland*,[72] Martin J discussed those cases and followed high authority which, despite acknowledging that the ordinary rules of construction apply to releases, nevertheless permitted reference to what was in the actual contemplation of the parties in order to construe general words in a release. The anomaly is, no doubt, strongly influenced by the necessary application of equitable principle applicable to releases. In *Grant v John Grant & Sons Pty Ltd*,[73] Dixon CJ, Fullagar, Kitto, and Taylor JJ stated:

> …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

49 That principle aside, the cases recognise that there is a clear distinction between legitimate and illegitimate use of extrinsic evidence in aid of construction. It is the

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69 (2012) 37 VR 486.

70 *Gee Dee Nominees Pty Ltd v Ecosse Property Holdings Pty Ltd* [2016] VSCA 23 at [93] to [97] per McLeish JA with whom Santamaria JA agreed is a good recent example of this.

71 Similarly, cases in which extrinsic evidence is admissible to establish that a word or phrase has a particular or technical meaning in a trade or business in which the contract was made (eg *Technomin Australia Pty Ltd v Xstrata Nickel Australasia Operations Pty Ltd* (2014) 48 WAR 261 at [178] per Murphy JA) or that it has a customary meaning in a particular locality or among a particular class of persons (see eg Lewison and Hughes, *The Interpretation of Contracts in Australia* (2012, Lawbook Co) at [5.09] and the cases cited therein).

72 [2015] QSC 342.

73 (1954) 91 CLR 112 at 129 to 130.

objective theory of contract which provides the theoretical underpinnings for the drawing of this distinction. The point can be made as a statement about permissible use of evidence and as a statement about impermissible use of evidence.

50 **As to the former**, the objective theory of contract operates to identify the scope of the extrinsic evidence that is admissible in aid of construction of the contract. In *Mount Bruce*, French CJ, Nettle and Gordon JJ said:[74]

> Each of the events, circumstances and things external to the contract to which recourse may be had is objective. What may be referred to are events, circumstances and things external to the contract which are known to the parties or which assist in identifying the purpose or object of the transaction, which may include its history, background and context and the market in which the parties were operating.

51 In other words, admissible extrinsic evidence is evidence of objective events, circumstances and things:

(a) which are known to the parties; or

(b) which assist in identifying the purpose or object or genesis of the transaction,

and which, once proved, may be used in aid of construction of the contract. An example is found in the list of the surrounding circumstances which were relevant in the *Royal Botanic Gardens* case, as identified at [23(b)] above.

52 **As to the latter**, it is another corollary of the objective theory of contract (disregarding as it does consideration of the subjective intention of either or both of the parties), that regard may still **not** be had to evidence of the antecedent negotiations and expectations of the parties in order to construe the contract. In this respect, the distinction explained in *Codelfa* is undoubtedly still the law: see *Mount Bruce* per French CJ, Nettle and Gordon JJ.[75] (And this is so regardless of the controversy about ambiguity as a threshold.) Even if extrinsic evidence is admissible, there are limits on the way in which it may be used. Thus in *Franklins Pty Ltd v Metcash Trading Ltd*:

(a) Allsop P observed (emphasis added):[76]

> … **What is impermissible is evidence, whether of negotiations, drafts or otherwise, which is probative of, or led so as to understand, the actual intentions of the parties. Such evidence might be legitimate, however, if directed to one of the legitimate aspects of surrounding circumstances**. The distinction can be subtle in any particular case. As Macfarlan JA and I said in *Kimberley Securities Ltd v Esber* (2008) 14 BPR 26,121; [2008] NSWCA 301 at [5]:
>
> > "The possible subtlety of the distinction can be seen in Lord Wilberforce's reasons in *Prenn v Simmonds* ... at All ER 240; WLR 1384-1385, and the recognition that the objective commercial aim may, possibly, be ascertained from some aspect of what has passed between the parties. The distinction can also be seen in what Mason J said in *Codelfa* at CLR 352; ALR 374-5 about prior negotiations and their legitimate use 'to establish objective background facts which were known to both parties and the subject matter of the contract', and their inadmissibility 'in so far as they consist of statements and actions of the parties which are reflective of their actual intentions or expectations' ..."

(b) Giles JA observed (emphasis added):[77]

> Regard can not be had to evidence of "the antecedent oral negotiations and expectations of the parties" in order to construe the contract: *Secured Income Real Estate (Australia) Ltd v St Martins Investments Pty Ltd* (1979) 144 CLR 596 at 606; 26 ALR 567 at 576 ; [1979] HCA 51,

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74 *Mount Bruce Mining Pty Ltd v Wright Prospecting Pty Ltd* (2015) 89 ALJR 990 at [50].
75 *Mount Bruce Mining Pty Ltd v Wright Prospecting Pty Ltd* (2015) 89 ALJR 990 at [50].
76 *Franklins Pty Ltd v Metcash Trading Ltd* (2009) 76 NSWLR 603 at [24].
77 *Franklins Pty Ltd v Metcash Trading Ltd* (2009) 76 NSWLR 603 at [51].

taken up by Mason J in Codelfa at CLR 352; ALR 374-5. His Honour there said, in part of a passage cited by Campbell JA:

> "... **Obviously the prior negotiations will tend to establish objective background facts which were known to both parties and the subject matter of the contract. To the extent to which they have this tendency they are admissible. But in so far as they consist of statements and actions of the parties which are reflective of their actual intentions and expectations they are not receivable**. The point is that such statements and actions reveal the terms of the contract which the parties intended or hoped to make. They are superseded by, and merged in, the contract itself. The object of the parol evidence rule is to exclude them, the prior oral agreement of the parties being inadmissible in aid of construction, though admissible in an action for rectification.
>
> Consequently when the issue is which of two or more possible meanings is to be given to a contractual provision we look, not to the actual intentions, aspirations or expectations of the parties before or at the time of the contract, except in so far as they are expressed in the contract, but to the objective framework of facts within which the contract came into existence, and to the parties' presumed intention in this setting. We do not take into account the actual intentions of the parties and for the very good reason that an investigation of those matters would not only be time consuming but it would also be unrewarding as it would tend to give too much weight to these factors at the expense of the actual language of the written contract."

53 It remains to make two further points.

54 First, evidence of surrounding circumstances (and this conception covers objective background facts existing when the contract was made and includes evidence of the "genesis" and objectively of the "aim" of the transaction and other like terms), will not be receivable as an aid to construction, unless the circumstances are known to both parties (although knowledge may be presumed if the facts are notorious).[78]

55 Although some of the English cases refer to the admissibility of "all the background knowledge which would reasonably have been available to the parties", unless and until the High Court overturns *Codelfa*, it remains necessary for a party seeking to tender evidence of facts known to both parties to demonstrate, either by direct proof or inference, that both parties had actual knowledge of the facts relied upon.[79] In *Mount Bruce*, Bell and Gageler JJ[80] used language similar to the English authorities, but in *Simic v Land and Housing Corporation (NSW)*,[81] Emmett AJA (with whom Bathurst CJ and Ward JA) explained that their Honours were not to be taken to have changed the law in this respect.[82]

56 Second, evidence of post-contractual conduct is not admissible in aid of construction of the contract. As to this:

(a) *Cross on Evidence* summarises the law in this passage (emphasis added):[83]

> Evidence of acts of the parties to an agreement in writing, performed in pursuance of the agreement, are, generally speaking, not admissible as an aid to construing the contract. This conclusion follows from the well-established principle that the task of construing a written agreement is not an investigation of the actual intent, expectation or aspiration of the parties to the agreement; it is an enquiry into their presumed intention as evidenced in the document.

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78 *Codelfa Construction Pty Ltd v State Rail Authority (NSW)* (1982) 149 CLR 337 at 352 per Mason J; *Movie Network Channels Pty Ltd v Optus Vision Pty Ltd* [2010] NSWCA 111 at [97] to [106] per Macfarlan JA with whom Young JA and Sackville AJA agreed.

79 See, for example, *Peabody (Wilkie Creek) Pty Ltd v Queensland Bulk Handling Pty Ltd* [2015] QCA 202 at [42] to [43] per Fraser JA (with whom Douglas and North JJ agreed).

80 *Mount Bruce Mining Pty Ltd v Wright Prospecting Pty Ltd* (2015) 89 ALJR 990 at [120].

81 [2015] NSWCA 413.

82 *Simic v Land and Housing Corporation (NSW)* [2015] NSWCA 413 at [95].

83 J D Heydon, LexisNexis, *Cross on Evidence*, vol 1 (at Service 183) at [39290].

> Thus, evidence of the actual intentions of the parties as shown in the antecedent negotiations is excluded. **The subsequent acts of the parties in pursuance of the agreement at best will show only what they understood its terms to be. This belief may be mistaken; it may be the result of incorrect legal advice as to the correct interpretation of the contract or it may be that the acts were the results of an act of grace or indulgence to promote good relations rather than to insist on strict legal rights. In any such event the acts are irrelevant to the construction of the document.**

(b) High Court authority presently supports this approach.[84]

The proper policy setting of the law

57 Would there really be anything wrong with moving towards the policy setting mentioned at [9] above, in which "[a]ll evidence that is relevant to identifying and interpreting the terms of a contract is admissible, including evidence of each party's actual intention" and the meaning of a contractual term would be that "intended by the parties, having regard to", amongst other things, "the parties' statements and other conduct before and after the contract was made"?

58 I confess that asking that question sets up an Aunt Sally. The most obvious problem is that such a policy would be contrary to the theoretical underpinnings of contract law in this country. A policy requiring the reinvention of that particular wheel should be rejected for that reason alone. It is not a realistic prospect.

59 Let the hypothesis be modified somewhat.

60 Would there be anything wrong with a policy which:

(a) accepted the requirement of the objective theory of contract that one should investigate what the terms would convey to a reasonable person in the position of the parties; but

(b) posited that better and more accurate decisions as to the meaning of contractual terms would be obtained if, **as a matter of course**, the Courts admitted the full gamut of such evidence as would paint a realistic picture of the circumstantial context known to the parties and in which they arrived at their signed written agreement?

61 In order to answer that question, one should first identify the policy goals which should influence the policy choice. I suggest that there are at least four.

62 **First**, the policy should promote the likelihood that better and more accurate decisions as to the meaning of contractual terms would be achieved.

63 **Second**, legislatures in this country explicitly recognise as a desirable policy goal that the Courts should seek to facilitate the just, efficient, timely and cost-effective resolution of the real issues in dispute between litigants.[85] Whilst a "just" resolution no-doubt has cross-over with the first policy goal, what is presently significant is the explicit recognition of the importance of efficiency, delay and cost-effectiveness. If such considerations are desirable policy goals for all litigation in the Courts, then it is

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84 *Agricultural and Rural Finance Pty Limited v Gardiner* (2008) 238 CLR 570 at [35], cited recently in *Regreen Asset Holdings Pty Ltd v Castricum Brothers Australia Pty Ltd* [2015] VSCA 286 at [133].

85 See Commonwealth: s 37M of *Federal Court of Australia Act* 1976 (Cth); Queensland: r 5 of the *Uniform Civil Procedure Rules* 1999 (Qld); Victoria: s 7 of the *Civil Procedure Act* 2010 (Vic); New South Wales: s 56 of the *Civil Proceeding Act* 2005 (NSW); Western Australia: Order 1, r 4A of *Rules of the Supreme Court* 1971 (WA); South Australia: rr 3 and 116 of the *Supreme Court Civil Rules* 2006 (SA); Australian Capital Territory: s 5A of the *Court Procedures Act* 2004 (ACT).

obvious that they are desirable policy goals for disputes which involve working out the meaning of a contractual term.

64 **Third**, the policy should be consistent with the intentions of the contracting parties themselves. As to this:

(a) In terms of their intentions as to the way in which any disputes between them should be conducted and resolved, their intentions must be taken to be consonant with the overarching policy that their disputes be resolved in a just, efficient, timely and cost-effective way. The law requires them to act in that way. I also posit that the actual intentions of genuine litigants (at least if they are determined before taking into account the tactical exigencies of a particular day) accord with their duty.

(b) But, *ex hypothesi*, something is also known - or at least may be presumed - about the parties' intentions at the time they entered into their contract concerning what should be examined in order to work out what they meant by their bargain.

(c) It is at least true to say that their presumed intention is that the whole of their agreement is contained in a written contract document (that must be so because the parol evidence rule would not apply unless it was first determined that the terms of the agreement were wholly contained in writing).[86]

(d) Professor Carter has observed:[87]

> … the question of what terms comprise a contract … is by definition distinct from the question of what those terms mean … Fundamentally, the document is a statement of the bargain; it is not a statement of what the bargain means. Therefore, the fact that a document is found to supersede the parties' negotiations, so that all the terms of the bargain are embodied … in the document, says nothing about what evidence should be available (as a matter of law) to construe those terms.

(e) The logic of these propositions is impossible to gainsay. However, we are presently considering policy questions and, insofar as that is relevant, what contracting parties may be taken to have intended.

(f) In my experience, at least in commercial contexts, parties who have negotiated and executed the terms of a written contract generally do seek to formulate the wording of their bargain so that the final form of their bargain does reflect what they mean. They generally do so intending to eliminate the need to go anywhere other than their written bargain to work out their meaning. That is the whole point of what they are trying to do.

(g) There are at least three reasons why that is so:

(i) First, the contracting parties seek to create certainty for their relationship going forward.

(ii) Second, they recognise that their contracts are often implemented by their employees or agents who were not themselves privy to the circumstantial context in which the contract was struck.

(iii) Third, and whether by assignment or novation, contracts often become relevant to the determination of the rights and liabilities of parties other

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86 *State Rail Authority of New South Wales v Heath Outdoor Pty Ltd* (1986) 7 NSWLR 170 at 191 per McHugh JA and *Nemeth v Bayswater Road Pty Ltd* [1988] 2 Qd R 406 at 413 per McPherson J.

87 J W Carter, "Context and Literalism in Construction" (2014) 31 Journal of Contract Law 100 at 106.

than the original contracting parties and "it is only the document that can speak to the third person".[88]

(h) There are models of agreement – many building and construction contracts for example – where the parties annex (or at least cross-refer to) some parts of their negotiations, with a view to shedding some light on their intentions in relation to the operation of some other part of their contract. But these models are not an exception to the proposition because it is the wording of such bargains themselves that points to the extent to which externality is relevant.

(i) It may be acknowledged that sometimes one party accepts language in a term which does not accord with what they want the term to mean, because they know or suspect that if they proposed language which was more explicit, the other contracting party would not agree to it. In those context, the first party accepts ambiguity with a view to giving rise to a potential negotiation at a future time. To my mind, however, this does not gainsay the proposition that the parties' intention is to look to the wording of the executed contract to work out what the bargain means, whatever it is.

65 **Fourth**, there is also a public interest to be recognised, namely that people who do intend that the whole of their bargain is reduced to writing should be encouraged to express that bargain so that its final form does in fact reflect what they really mean.

66 In my view it is plain that a policy in which, **as a matter of course**, the Courts admitted the full gamut of such evidence as would paint a realistic picture of the circumstantial context known to the parties and in which they arrived at their signed written agreement, would be a policy which pursued the uncertain prospect of advantage in relation to the first policy goal at the expense of certain and significant disadvantage in relation to the second, third and fourth policy goals.

67 The common experience of trial lawyers and trial judges supports that conclusion. The summary determination of issues involving contractual points would become impossible because of the extent alone of the material which would have to be considered, to say nothing of factual disputes concerning the assertions made in the material. The cost and length of trials would increase. The time taken in argument and the time taken in actually writing the judgment would increase. And, usually, for no particular advantage in outcome.

68 No one could gainsay the proposition that there are occasions in which recourse to extrinsic material will be both helpful and determinative and where the exclusion of such material would be to privilege unjustly the other policy goals mentioned above at the expense of the first one. But those cases will be exceptional rather than usual. A consideration of the policy goals identified suggests the proper policy setting of the law must tend against admission of such evidence as a matter of course, but be flexible enough to permit of the admission of such evidence when it is of utility.

69 The law as presently formulated does seek to reflect such a policy, albeit, and probably necessarily, imperfectly. It does so by the creation of a number of filters through which proposed extrinsic evidence much pass in order to be admissible.

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88 See *Wilson v Anderson* (2002) 213 CLR 401 at [7] to [10] per Gleeson CJ citing an extra-judicial observation by Lord Devlin and also the same comment made by the High Court in *Pacific Carriers Ltd v BNP Paribas* (2004) 218 CLR 451 at [22].

70 The first filter is the ambiguity threshold, to the extent that it exists. Of course, given the relative ease with which the threshold is crossed where it exists, its effectiveness may be doubted.

71 But if the ambiguity threshold is removed, how will the law operate to avoid the problems of cost, delay and uncertainty to which reference has been made in the foregoing discussion of policy?

72 One filter which would still operate would be the exclusion of proof of pre-contractual negotiations probative of, or led so as to understand, the actual intentions of the parties, unless the proof is directed to one of the legitimate aspects of surrounding circumstances. However, if the law is expressed to permit of admissibility of extrinsic evidence in order to establish ambiguity, one wonders how easy it will be to distinguish between legitimate and illegitimate reference to such evidence.

73 Much will turn on how developments in the substantive law are expressed in the intermediate courts of appeal, and, eventually in the High Court. In my view, the potential law reform which I criticised at the outset, was, with respect, an example of an occasion where a pursuit of theoretical purity has occurred with insufficient attention to feasibility and practical consequences. I would not have the temerity to suggest that such lack of attention has occurred in our intermediate courts of appeal or in the High Court.

74 Whichever direction is taken in the development of the substantive law, one filter which will inevitably remain will be the filter which applies to all evidence tendered in court, namely the filter of relevance. In this area of discourse, the proposition of relevance which must be demonstrated is the tendency of the tendered evidence to prove a fact which, if proved, would assist the determination of a question of law, namely the meaning of a contractual term.

75 The final section of this paper adverts to courses which might assist the management of the evidence and at least promote clear thinking about the purpose of its tender. If that occurs, it is to be hoped that the task of trial and appellate judges will be made easier.

Procedural courses which may assist the efficient management of attempts to use extrinsic evidence

76 It is the hypothesis of this paper that the "just and expeditious resolution of the real issues in civil proceedings at a minimum of expense"[89] will be promoted by adopting procedural courses which have the effect of requiring parties –

(a) to focus early and specifically on:

(i) whether or not they intend to rely on extrinsic evidence in aid of construction of the contract which is the subject of their dispute; and

(ii) if they do, on how they might do so in a way which involves the legitimate use of the evidence; and

(b) to determine the extent to which they are in disagreement about the matters said to be proved by the extrinsic evidence.

77 Two possible procedural courses are open:

(a) First, requiring the pleading of the events, circumstances and things external to the contract:

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89 Cf *Uniform Civil Procedure Rules* 1999 (Qld) r 5.

(i) which are known to the parties; or

(ii) which assist in identifying the purpose or object or genesis of the transaction.

(b) Second, obtaining directions which will flush out each side's position on any disputed matters well before the hearing.

Pleadings and extrinsic evidence

78 Let it be assumed that a party seeks to litigate a case in which it seeks to rely on extrinsic evidence in aid of construction of the contract with which the dispute is concerned. In particular, the party thinks that there is something which can be said about events, circumstances and things external to the contract which, if accepted, would assist a court to construe the contract in the way for which the party contends.

79 Is this something which should find any reflection in a pleading?

80 The following are the relevant rules of pleadings in Queensland:

(a) UCPR r 149:

(i) each pleading must be as brief as the nature of the case permits;

(ii) each pleading must contain a statement of all the material facts on which the party relies but not the evidence by which the facts are to be proved;

(iii) each pleading must state specifically any matter that if not stated specifically may take another party by surprise;

(iv) in a pleading, a party may plead a conclusion of law or raise a point of law if the party also pleads the material facts in support of the conclusion or point;

(b) UCPR r 150:

(i) without limiting r 149, the following matters must be specifically pleaded … (k) motive, intention or other condition of mind, including knowledge or notice;

(ii) any fact from which [any of the matters which must be specifically pleaded] is claimed to be an inference must be specifically pleaded;

(iii) in a defence or pleading after a defence, a party must specifically plead a matter that … (c) if not specifically pleaded might take the opposite parties by surprise; or (d) raises a question of fact not arising out of a previous pleading;

(c) UCPR r 157: a party must include in a pleading particulars necessary to define the issues for, and prevent surprise at, the trial; and enable the opposite party to plead and support a matter specifically pleaded under r 150; and

(d) UCPR rr 162 and 171, pleadings and particulars may be struck out if they have a tendency to prejudice or delay the fair trial of the proceeding or are unnecessary.

81 It is difficult to see how one could legitimately contend that any of the matters referred to in [78] are material facts. Material facts are facts necessary for the purpose of formulating a complete cause of action. If there is a cause of action, the pleading of it is likely to be complete without the need to plead matters which might be used in aid of construction of the subject contract. The pleading of conclusions of law is optional but not essential to pleading a complete cause of action.

82 However, there are three rules which justify and indeed may be regarded to compel pleading those matters:

(a) UCPR rr 149(1)(c) and 150(4)(c) which both require pleading of any "matter" which is capable of taking the other party by surprise;

(b) UCPR r 150(1)(k) which requires knowledge to be specifically pleaded and, if the allegation of knowledge turns on inference, the facts from which knowledge is to be inferred; and

(c) UCPR r 157 which requires particulars necessary to define issues for and to prevent surprise at trial.

83 If a party contemplates asking a court to find that there were events, circumstances and things external to the contract which are relevant to its construction, then that is likely to be a matter which is capable of taking the other party by surprise and which should be specifically pleaded. It is not an objection to that possibility that pleading and particularising the matter might go beyond the **ordinary** articulation of material facts. In *UI International Pty Ltd v Interworks Architects Pty Ltd*[90] Daubney J acknowledged that this rule could justify pleadings which go beyond the material facts which might be strictly necessary for the claim.

84 If the view is taken that these are matters which can and should be pleaded, then they will have to be articulated and responded to in the usual way by plaintiff and defendant. That the parties knew the alleged facts will have to specifically pleaded. And if there is an inferential case of knowledge the particular facts justifying knowledge will have to be pleaded.

85 The foreseeable consequences include:

(a) avoidance of surprise at trial;

(b) the possibility that some or all of the alleged facts might be admitted, thereby eliminating the need to examine the evidence which might prove those facts (or from which the knowledge might be inferred); and

(c) an earlier focus on the legitimacy or illegitimacy of the proposed recourse to extrinsic evidence with the result that:

(i) some obviously illegitimate attempts to rely on such material might be capable of being resolved at an interlocutory stage by requests for particulars followed by strike out applications; and

(ii) attention could be given to the efficient resolution at trial of any necessary admissibility rulings by the Court.

86 It is difficult to see any compelling reason why a properly drawn pleading should not plead the kind of "matter" under discussion. The most likely problem might be that incompetent pleaders would end up merely pleading the steps taken in negotiation followed by an "in the premises of the foregoing the proper construction of the contract is …". Such a pleading may well be objectionable and liable to being struck out. The requirement to plead fact not evidence should, if complied with, require a real focus on what fact it is that the extrinsic evidence might prove. It would invite the pleader both to plead that fact rather than the evidence by which it will be proved and also to have already formulated an answer to the question which the trial judge will inevitably ask,

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90 [2010] QSC 280.

namely "why would acceptance of the existence of that fact assist in reaching the construction of the contract for which you contend?"

87 Accordingly the first hypothesis of this part of the paper is that if a litigant thinks that there is something which can be said about events, circumstances and things external to the contract which if accepted would assist a court in reaching a particular construction of the contract, that is a matter which can and should be pleaded, albeit with care.

Court intervention and extrinsic evidence

88 There is no doubt that the UCPR confers sufficient power on the Court to make appropriate directions to manage a case in which a party does or might seek to introduce extrinsic evidence: see UCPR r 367.

89 Directions are often made which require parties to identify in advance of a hearing how they propose to advance their case (both in relation to evidence and argument):

(a) So far as testimonial evidence is concerned, this is conventionally done by directions requiring the filing of affidavit evidence or directions requiring the identification of witnesses and the filing of documents disclosing the substance of the evidence that the witnesses are expected to give.

(b) So far as documentary evidence is concerned, this is conventionally done by directions requiring:

(i) the preparation of bundles of documents; and

(ii) the parties to articulate and then respond to objections to admissibility of documents.

(c) So far as argument is concerned, this is conventionally done by directions requiring the delivery before trial of written submissions on all or some particular parts of the case.

90 In a case which calls for it, the second hypothesis of this paper is that consideration should be given to directions aimed at assisting the Court's capacity to manage any debate which might exist about the admissibility of extrinsic evidence in aid of construction. At the least, a party who is resisting the tender of such evidence should consider seeking a direction which requires the party seeking to tender the evidence to articulate with precision (for example):

(a) the objective background fact of which the evidence is said to be probative; and

(b) how the alleged background fact would assist the Court in resolving the disputed construction of the contract.

91 Unless a party can so articulate its case, the party is probably trespassing into an impermissible examination of extrinsic evidence. An unfocussed assertion that evidence is admissible because it forms part of the "factual matrix" or "surrounding circumstances" is insufficient. If that is all the tendering party can say, then the submission will be given the treatment it deserves. But even if there are objective facts which were undoubtedly known to the parties at the time they entered into the contract, that is not sufficient to justify admitting evidence of those facts. To justify the relevance of the evidence, the tendering party will have to be able to say why, if received, the evidence would assist the determination of a question of law, namely the meaning of a contractual term.

92 A question arises as to how to deal with evidence where its admissibility is in contest even after it has been managed in the way suggested.

93 As to this, in *McCourt v Cranston*,[91] Pullin JA observed:

> 25 If a trial judge decides that the contract under examination is not ambiguous or susceptible of more than one meaning, and rules that evidence of surrounding circumstances is not admissible, and an appeal court then decides that decision to be in error, then the case will have to be reheard, because relevant evidence will have been excluded. If, however, the trial judge receives evidence of surrounding circumstances and evidence of the object or aim of the transaction, and if the trial judge's construction is found to be in error, then the Court of Appeal will be able to remedy that on appeal without sending it back for retrial.
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> 26 Until the High Court says more about the subject, it would be wise for trial judges, in cases where a party reasonably contends that the contract is ambiguous or susceptible of more than one meaning and there is relevant evidence of objective relevant surrounding circumstances known to both parties or objective evidence of the aim or object of the transaction, to allow that evidence in provisionally, even if the trial judge considers that his or her likely conclusion will be to reject the argument of the party contending that the agreement is ambiguous or susceptible of more than one meaning.

94 That proposition was advanced in relation to the current controversy about the existence of an ambiguity threshold. It is not a recipe for the resolution of every attempt to tender extrinsic evidence. No approach suitable to all circumstances can be articulated. If the contract is relevantly ambiguous and the evidence is of narrow compass, a trial judge might well admit the evidence provisionally. On the other hand, if the evidence could not be so characterised, a trial judge might well rule one way or the other at the outset, perhaps well before trial. One advantage of having the parties commit themselves to clear propositions justifying the tender as part of the management of the case might be that they are held to those positions, in the event of any appeal.

Conclusion

95 The rules regulating the admissibility of extrinsic evidence in aid of construction of contracts are well known, but still cause difficulty.

96 There is a current controversy as to whether the *Codelfa* rule that existence of ambiguity in the relevant terms of the contract is a pre-requisite to admissibility of the evidence is still good law.

97 Unless and until the High Court provides further direction, the continued application of the *Codelfa* rule is appropriate. But the questions treated as open by the High Court in *Mount Bruce* still await examination in many jurisdictions.

98 Quite apart from that controversy, it is suggested that the efficient management of cases which involve reliance on extrinsic evidence would be improved if parties took the view that the proposition that there are events, circumstances and things external to the contract which are relevant to its construction was a "matter" which should be specifically pleaded.

99 Consideration should also be given to obtaining directions aimed at ensuring the parties have sufficiently focussed their attention on this issue before hearings in Court begin.

John Bond

26 May 2016

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91 [2012] WASCA 60.