High Court guidance on contract interpretation

Ecosse Property Holdings Pty Ltd v Gee Dee Nominees Pty Ltd [2017] HCA 12

Roger Walter | April 2017 | Insurance & Financial Services

Summary

In *Ecosse Property Holdings Pty Ltd v Gee Dee Nominees Pty Ltd* the High Court provided a little further guidance on how to construe contracts that, if read literally, might, due to some drafting error or ambiguity, produce a commercially absurd or odd result.

Background

A regular source of error and confusion, even for lawyers with the training and skills required to interpret contracts, is the extent to which surrounding circumstances can properly be considered when interpreting a written agreement. A consideration of matters other than the text of a disputed clause and a reading of the entire agreement is often either overlooked or undertaken incorrectly.

The difficulties in this regard are often associated with technical rules about what is and what is not admissible evidence in the process of interpretation. Then there are restrictions on the extent to which evidence of surrounding circumstances, if admissible at all, can be employed to arrive at the meaning of the text.

In the present case the court had to decide which of two competing interpretations of a clause best suited the commercial objects of the agreement. This required reference to the text of the agreement and the circumstances in which it was created, even though the parties who did create it had long since sold their interest on.

Facts

The dispute concerned a 99-year lease agreement formed in 1988 in respect of a block of rural land with no separate title. The parties to the agreement wanted to transfer it between them for an agreed sum of $70,000, which was considered to be the value of the freehold.

Importantly, a receiver represented the would-be seller of the block and the larger parcel containing it, which could not be subdivided at the time. The lease agreement provided for upfront payment of $70,000 in rent. The document used to create the agreement was a standard form farm lease, which the parties modified, somewhat clumsily.

The original contracting parties had (respectively in 1993 and 2004) transferred their interest in the lease to the parties that came before the court in the dispute.

In 2011 a separate title was issued in respect of the block, from which point it was assessed separately for rates and land tax.

The trial judge was satisfied that the parties to the lease agreement were intent on producing a conveyance of the freehold title, knowing that it was not technically possible to do so at the time. His Honour proceeded on that basis to reason that an ambiguous clause (clause 4) requiring the payment of rates and taxes should not be construed as requiring the lessor to pay. The lessor (Ecosse Property) won at first instance, but lost on appeal in a split decision, in the Victorian Court of Appeal.

The essential question, as framed in the High Court by Gageler J in allowing the appeal from the Victorian Court of Appeal was whether clause 4 of the lease 'obliges the Lessee to pay all rates, taxes, assessments and outgoings

in respect of the leased land or instead only obliges the Lessee to pay those rates, taxes, assessments and outgoings that are levied on the Lessee.'

The majority in the Victorian Court of Appeal focused on drafting considerations and how the desired effect of clause 4 for which the lessor was contending might have been achieved by an amendment that the parties could have made, but did not make, before executing the agreement. Another key aspect of the approach taken by the Victorian Court of Appeal in preferring the lessee's interpretation (and overturning the decision of the trial judge) was the attention paid to objective commercial considerations such as the absence of any option to renew or purchase; this approach is reflected in this statement about commerciality:

> Above all, the lessee is required to return the land at the end of the term. In those circumstances, there is no warrant for presuming that the parties intended cl 4 to operate so as to approximate the position under a sale and purchase.

The High Court Ruling

On 29 March 2017 the High Court, in another split decision, allowed the lessor's appeal.

The High Court plurality of Kiefel, Bell and Gordon JJ, in their reasons allowing the appeal observed that clause 4 read as follows, once deleted wording from the standard form farm lease provision was extracted:

> AND [the Lessee] also will pay all rates taxes assessments and outgoings whatsoever which during the said term shall be payable by the tenant in respect of the said premises.

It was accepted that this clause is ambiguous. Ecosse Property as lessor preferred the interpretation requiring all outgoings to be paid by the lessee, Gee Dee Holdings.

In allowing the appeal, the plurality said (omitting footnotes about the High Court's earlier (2014) decision in *Electricity Generation Corporation v Woodside Energy Ltd):*

> [16] It is well established that the terms of a commercial contract are to be understood objectively, by what a reasonable businessperson would have understood them to mean, rather than by reference to the subjectively stated intentions of the parties to the contract. In a practical sense, this requires that the reasonable businessperson be placed in the position of the parties. It is from that perspective that the court considers the circumstances surrounding the contract and the commercial purpose and objects to be achieved by it.
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> [17] Clause 4 is to be construed by reference to the commercial purpose sought to be achieved by the terms of the lease. It follows, as was pointed out in the joint judgment in *Electricity Generation Corporation v Woodside Energy Ltd*, that the court is entitled to approach the task of construction of the clause on the basis that the parties intended to produce a commercial result, one which makes commercial sense. It goes without saying that this requires that the construction placed upon cl 4 be consistent with the commercial object of the agreement.

A similar disposition was conveyed by Gageler J in his separate reasons citing *Gollin & Co Ltd v Karenlee Nominees Pty Ltd* (1983) 153 CLR 455 at 464; [1983] HCA 38:

> [51] Clause 4 can only be so construed for what it is: a clumsily tailored variation of an ill-fitting off-the-shelf precedent. To bring linguistic and grammatical precision to its construction would be to burden the clause with more weight than its jumble of words will bear.
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> [52] The competing constructions of cl 4 being open on its language, and the textual indications in favour of each being at best equivocal and at worst conjectural, the choice between them comes down to deciding which is more reasonable considered as a matter of "commercial efficacy or common sense".

In his reasons for dissenting in the High Court, Nettle J, favoured the approach taken by the majority in the Victorian Court of Appeal. His Honour adopted a more textual approach, having more regard to the document and objective commercial considerations about its effect and purpose. His Honour was less inclined to be influenced by the circumstances of its genesis in finding that the meaning favoured by the lessor was 'significantly removed from the natural and ordinary meaning of the terms of the clause' and that the lessee's interpretation was to be preferred in that it was 'a plain, ordinary and commercially not irrational meaning' and more in accordance with other provisions of the agreement.

Implications

The High Court, in the reasons given by the majority on this appeal, has again reminded us that:

(a) commercial common sense will often be the critical consideration in arriving objectively at the meaning of a disputed clause of an agreement;

(b) while the subjective intentions of a party to an agreement are not considered in deciding the meaning of its text, it is often necessary to resolve ambiguity by having regard to the genesis and objects, objectively determined, of an agreement;

(c) these issues are sometimes very finely balanced and sometimes require very close and careful scrutiny.

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