Chartbrook v Persimmon Homes [2009]

in context:

the availability of pre-contract negotiations as an aid to the interpretation of a contract.

By

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**Introduction**

1. Chitty\(^1\) helpfully explains that:

   “The word “construction” refers to the process by which a court determines the meaning and legal effect of a contract…

   The object of all construction of the terms of a written agreement is to discover therefrom the common intention of the parties to the agreement.”

2. It goes on to explain that the task of ascertaining the common intention of the parties is to be approached objectively. What that does not mean is what one or other of the parties intended or understood by the words used, but:

   “…the meaning which the document would convey to a reasonable person having all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract.” Investors Compensation Scheme v West Bromwich Building Society [1998] 1 WLR 896, at 912.

3. Sir Kim Lewison is equally brief in his introduction to the subject in his book “The Interpretation of Contracts”\(^2\). He explains that the law about the interpretation of contracts “*may be summarised in 5 principles*…”. These are:

   1. Interpretation is the ascertainment of the meaning which the document would convey to a reasonable person having all the background knowledge which would reasonably have been available to the parties in the situation in which they were at the time of the contract.

   2. The background\(^3\) includes absolutely anything (assuming it to be reasonably available to the parties) which would have affected the way in which the language of the document would have been understood by a reasonable man.

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\(^1\) Chitty on Contracts, 30th Edition, 2008, Ch. 12-041


\(^3\) Reference is made to Lord Wilberforce’s “Matrix of fact” in Prenn v Simmonds [1971] 1 WLR 1381.
3. Excluded from the background are the previous negotiations of the parties and their declarations of subjective intent – which are admissible only in an action for rectification.

4. The meaning which a document (or statement) would convey is not the same as the meaning of words. Words are construed by reference to dictionaries and grammars; documents by reference to what the parties using the words, against the relevant background, would reasonably have been understood to mean.4 Lewison observes by reference to Mannai Investment Co Ltd v Eagle Star Life Assurance Co. Limited [1997] AC 749 that the background may enable a reasonable man not just to choose between words which are ambiguous, but also sometimes to conclude that the wrong words or syntax were used.

5. The “rule” that words should reflect their “natural and ordinary meaning” reflect the view that we do not readily accept that people make linguistic mistakes, especially in formal documents, but equally that it is not beyond the bounds of possibility and if something has gone wrong with the language used, then judges are not required to attribute to the parties, a meaning which they plainly could not have had.

4. These principles are summarised by reference to BCCI v Ali [2001] 2 WLR 735, and the speech of Lord Bingham:

“To ascertain the intention of the parties the court reads the terms of the contract as a whole, giving the words used their natural and ordinary meaning in the context of the agreement, the parties’ relationship and all the relevant facts surrounding the transaction so far as known to the

parties. To ascertain the parties’ intentions the court does not of course inquire into the parties’ subjective states of mind but makes an objective judgment based on the materials already identified.” AT 739 [D-F]

5. Having identified these principles over two or so pages, Lewison then says: “The lazy reader may stop here.” If only…

6. So what about Chartbrook, Lord Hoffmann’s final roll of the dice on this subject?

7. Chartbrook v Persimmon Homes is a case about the interpretation of contracts and rectification, which also provoked discussion in the House of Lords about the availability of pre-contract negotiations as an aid to the interpretation of a written contract.

8. It is a case which gave the House of Lords, and particularly Lord Hoffmann, the opportunity to revisit the rule in Prenn v Simmonds [1971] 1 WLR 1381 and the well known words of Lord Wilberforce when he said:

“in my opinion then, evidence of negotiations, or of the parties’ intentions and a fortiori of [the Plaintiff’s] intentions, ought not to be received, and evidence should be restricted to evidence of the factual background known to the parties at or before the date of the contract, including evidence of the “genesis” and objectively the “aim” of the transaction.”

Ibid at 1385.

9. The facts of the case in Prenn v Simmonds are not dissimilar to the Chartbrook case. On one view of the meaning of a term, Dr. Simmonds would be paid a substantial sum of money, and on another, nothing by reason of the failure to fulfil a condition precedent to the right to payment. Dr Simmonds claimed that the written agreement bore the meaning he contended for, or, in the alternative, that if it did not, it should be rectified. Counsel for Dr. Simmonds contended that in construing the agreement it was permissible to look at the prior negotiations of the parties as an aid to its construction. Unsurprisingly, Mr. Prenn disagreed.
10. In Prenn v Simmonds Lord Wilberforce expressed the view that evidence of prior negotiations was not excluded for technical reasons or even for convenience, he said that “It is simply that such evidence is unhelpful.” and that “It is only the final document which records a consensus.” In the event, since Dr. Simmonds was successful in his appeal on the construction of the document, the rectification point was not argued.

11. So has anything changed in the last 39 years? The Chartbrook case is about a dispute over the construction of a particular term in a development agreement. When stripped down, it is also a dispute about money. On one construction of the disputed term the landowner would receive something of the order of £4.5 million, and on the other, only £900,000.

12. Chartbrook’s claim was based on its (more generous) construction of the disputed term in the agreement. Persimmon contended for a more restrictive interpretation of the agreement, or, in the alternative, it claimed that the agreement should be rectified to reflect the interpretation that it contended for.

13. In the event, the House of Lords, without departing from the rule in Prenn v Simmonds, allowed Persimmon’s appeal on the basis of its construction of the agreement and therefore, although Lord Hoffmann expressed views on the rectification claim which, if Persimmon had failed on the construction argument, he would have allowed⁵, the case was not decided on that point.

The facts

14. In Chartbrook v Persimmon, the parties entered into a development agreement so that under licence from Chartbrook, Persimmon would obtain planning permission, take possession of Chartbrook’s site and carry out a mixed commercial and residential development on the land.

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⁵ As would the remaining law Lords if the case had been decided on the basis of the claim for rectification of the contract.
When the development was complete, Persimmon would sell the units on long leases and at Persimmon’s direction, Chartbrook would grant long leases to the buyers. Persimmon was to receive the sale proceeds from each of the buyers and was to pay Chartbrook an agreed price for the land. The contract provided a mechanism for the calculation of the price to be paid for the land which was split into a basic payment – the Minimum Guaranteed Residential Unit Value (“MGRUV”), and in addition, a balancing payment (the “Additional Residual Payment” – “ARP”) calculated by reference to the price achieved on the sale of each residential unit and expressed as:

“23.4% of the price for each Residential Unit in excess of the Minimum Guaranteed Residential Unit Value less the Costs and Incentives.”

15. The development went ahead and the units were built and sold by Persimmon. The parties fell into dispute over the calculation of the ARP. There was a difference of some £3.5 million between their respective views as to the proper construction of the term by which the ARP should be calculated.

16. Chartbrook argued that you take away the MGRUV and the Costs and incentives, and take 23.4% of the balance. Persimmon argued that you take the costs and incentives from the sale price, find 23.4% of that net price and then deduct the MGRUV, so that the ARP is the excess over the MGRUV.

17. At first instance and in the Court of Appeal, Chartbrook succeeded. In the Court of Appeal, Lawrence Collins LJ dissented. The House of Lords agreed with his dissenting judgment.

18. The leading judgment is that of Lord Hoffmann, possibly his last or one of his last judgments as a member of the House of Lords. This adds to the interest of the case. Lord Hoffmann also gave leading judgments in a number of important cases concerning the interpretation of contracts, whether written or oral, or both, including:
1. BCCI v Ali and others [2001] 2 WLR 735
2. Carmichael and Anr v National Power [1999] 1 WLR 2042

These cases feature in the judgment.

19. The general principles of construction, based as they are on the principles set out above, were not in contention before the House of Lords.

20. Lord Hoffmann took the view that while it took a strong case to persuade the court that something had gone wrong with the language used by the parties in the contract, it had done so in this case because to interpret the agreement in accordance with the ordinary rules of syntax (as had happened in the courts below) made no commercial sense. The ARP was clearly intended to be a contingent payment to share any bonus resulting from increasing land values but using Chartbrook’s construction, there was barely any contingency at all and an ARP would be payable on any sale of a residential unit above the value of £53,438. The idea that a flat in Wandsworth would not greatly exceed such a price was untenable.

21. Lord Hoffmann therefore agreed that the ARP must therefore mean the extent to which 23.4% of the achieved price, exceeded the MGRUV. He said:

“When the language used in an instrument gives rise to difficulties of construction, the process of interpretation does not require one to formulate some alternative form of words which approximates as closely as possible to that of the parties. It is to decide what a reasonable person would have understood the parties to have meant by using the language which they did. The fact that the court might have to express that

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In which Lord Hoffmann gave a powerful dissenting judgment.
meaning in language quite different from that used by the parties... is no reason for not giving effect to what they appear to have meant.” Para 21.

22. That was effectively the decision of the House of Lords on the construction point, sufficient at any rate to dispose of the appeal. However, the House also heard argument from Persimmon that as an aid to the construction of the agreement the court should revisit the rule in Prenn v Simmonds and have regard to evidence of prior negotiations. Persimmon also argued an alternative case that if it’s contentions as to the proper construction of the agreement failed, the agreement should be rectified. It is the first of these two arguments that are of particular interest here.

23. Lord Hoffmann noted that to allow evidence of prior negotiations would be to depart from a long line of existing authority and the “rule” which was that, save in defined exceptions, for example in the case of a claim for rectification or estoppel, such evidence was inadmissible as an aid to the construction of a written agreement.

24. Lord Hoffmann reviewed at some length, authorities and opinions on the subject but in the event concluded that he could find no clearly established case for departing from the exclusionary rule. In so doing he:

1. Accepted that it would not be inconsistent with the English objective theory of contractual interpretation to admit evidence of previous communications between the parties as part of the background which may throw light upon what they meant by the language they used. Referring to the BCCI v Ali case, he restated his view that there were no conceptual limits to what can properly be regarded as background. (para 33)

2. Commented that generally, as stated by Lord Wilberforce, inadmissibility of such evidence is normally based on irrelevance. (para 34)
3. Noted the view of some commentators who preferred to allow the document primarily to speak to itself with limited or no reference to background so that the law of contract fulfilled its primary function to enforce promises with a high degree of predictability. (para 37)

4. Expressed the view that pre-contract negotiations seemed capable of raising practical questions different from those created by other forms of background. Whereas the surrounding circumstances are, by definition, objective facts, and usually uncontroversial, statements in the course of pre-contract negotiations will be drenched in subjectivity and may, if oral, be very much in dispute. (para 38).

5. Accepted in principle that if the courts were to accept evidence of pre-contract negotiations, it would increase the risk that a third party may find that the contract did not mean what he thought it did.

6. Concluded the discussion by stating that the rule excluded evidence of what was said or done during the course of negotiating the agreement for the purpose of drawing inferences about what the contract meant. “It does not exclude the use of such evidence for other purposes, for example, to establish that a fact which may be relevant as background was known to the parties, or to support a claim for rectification or estoppel. These are not exceptions to the rule. They operate outside it.”

7. He went on to consider a group of cases which judges have found to be an exception to the exclusionary rule. In particular he took the view that the judgment of Kerr J in the case of the “The Karen Oltmann” [1976] 2 LLR 706, was an illegitimate extension of the “private dictionary” rule because there was no magical definition to be given to the word “after”!
Conclusion

25. So, is the decision a surprise, has it had, and will it have, any impact? How is it viewed a year on?

26. It is quoted in a number of recent decisions but there is absolutely nothing startling in the conclusions which have been reached. If there is scope for reference to prior negotiations beyond what was permissible before Chartbrook, it would seem to be in the area of reference to the negotiations as part of the background, see points 1 and 6 above. In future parties may have greater confidence, that they may deploy such evidence in this context, but apparently, not otherwise. That is not to say however that one should not try!

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