INSTITUTE OF MARITIME LAW

33rd Donald O'May Lecture

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"The construction of shipping and marine insurance contracts: why is it so difficult?"

1. Despite the fact that my talk this evening is taking place when a much more important event is about to kick off not so far away at Stamford Bridge, it is a great pleasure to be here. And I am very grateful to the Institute of Maritime Law for this opportunity to speak on a topic which is, I believe, very important[1].

2. As appears from the title, my focus this evening is the construction of shipping and marine insurance contracts. That was, of course, the focus of Donald O'May's work – and probably is the staple diet of many of you here this evening. However, there is, in truth, nothing special about these contracts. And if there are any generalists in the audience - much of what I have to say applies equally to most, if not all, commercial contracts.

3. Let me acknowledge at the outset the vast amount of academic learning that has been produced in recent years

[1] I am also particularly grateful to Mr Robert Veal, Senior Research Assistant for Law at the University of Southampton for his assistance in preparing this lecture.

on the general topic of the construction of commercial contracts. Quite apart from what appears in Chitty and the other standard textbooks on contract, there is, of course, Sir Kim Lewison's book, "*The Interpretation of Contracts"*[2] now in its 5th edition, weighing in at 862 pages and even more expensive than *Scrutton on Charterparties;* Richard Calnan's *"Principles of Contractual Interpretation"*[3]; John Carter's "*The Construction of Commercial Contracts*[4]– another magnum opus extending to some 716 pages; and a deluge of learned articles including a trilogy by Johan Steyn, *"The Role of Good Faith and Fair Dealing in Contract Law: A Hair-Shirt Philosophy?"*[5], "*Does Legal Formalism Hold Sway in England?"*[6] and *"Contract Law: Fulfilling the Reasonable Expectations of Honest Men"*[7]; Christopher Staughten's *"How do Courts Interpret Commercial Contracts?"*[8]; J Spiegelman*'s "From Text to Context: Contemporary Contractual Interpretation"*[9]; Lord Bingham's *"A New Thing under the Sun: The Interpretation of Contract and the ICS Decision"*[10]; Lord Grabiner QC's *"The Iterative Process of Contractual Interpretation"*[11] and, most recently, the extended essay by Paul Davis, *"The Meaning of Commercial Contracts"*[12]. In addition, there is, of course, a constant stream – indeed a veritable flood - of commentary available

[2] (2014) Sweet & Maxwell, now in its 5th Edition with 2nd Supplement
[3] (2013) OUP
[4] (2013) Hart Publishing
[5] (1991) Denning Law Journal 131
[6] (1996) CLP 43
[7] (1997) LQR 113
[8] (1999) 58 CLJ 303
[9] (2007) 81 Australian Law Journal 322
[10] (2008) Edinburgh Law Review 374
[11](2012) 28 LQR 41
[12](2015) *The Jurisprudence of Lord Hoffmann: A Festschrift in Honour of Lord Hoffmann* p215

on the internet. Hardly a week goes by without a new article being published on the topic.

4. You will be pleased to know that I do not intend to try to compete with this wealth of scholarship. In the short time available this evening, I would like to explore the very broad question: *Why is the construction of these contracts so difficult?* And, although not expressly included in the title, the follow-on question is, of course: *what, if anything, can be done to make it less difficult?* After all, it is, I think, a truth universally acknowledged that certainty in commercial contracts is a most desirable objective – and with difficulty comes uncertainty which is, I would suggest, a Bad Thing.

5. Virtually every case I have ever done – whether as Counsel or Judge – has involved some issue of construction which has to be resolved one way or another. And as I have wrestled with these problems in various cases, I have often posed these important questions to myself – and these are some of the answers that have occurred to me.

Lawyers

6. The first – and most obvious answer – is to blame the lawyers. And there is a long line of eminent individuals who have taken great pleasure in doing just that. Thus, in *Gulliver's Travels*, Jonathan Swift indicts lawyers *as*

"…a society of men . . . bred up from their youth in the art of proving by words multiplied for the purpose, that white is black and black is white, according as they are paid…"

Dickens is another who disliked lawyers intensely. Likewise Lord Denning who expressed his views most trenchantly in his celebrated Romanes lecture entitled "*From Precedent to Precedent"* delivered in Oxford in1959. Speaking of the meaning of words, he said that lawyers are:

> *"….the most offending souls alive….They will so often stick to the letter and miss the substance. The reason is plain enough. Most of them spend their working lives drafting some kind of document or other — trying to see whether it covers this contingency or that. They dwell upon words until they become mere precisians in the use of them. They would rather be accurate than be clear. They would sooner be long than short. They seek to avoid two meanings, and end — on occasions — by having no meaning. And the worst of it all is that they claim to be the masters of the subject."*

That is strong language indeed.

7. When Lord Denning was referring to "lawyers" – I am pretty sure that he was talking about them in their capacity as draftsmen or draftswomen. But, Judges are, of course, lawyers too. And it is fair to say that the Judges have not always got it right. For example, the decision of the Court of

Appeal in *The Laura Prima*[13] as to the meaning of the words *"reachable on arrival"* in a voyage charterparty is, if I may say so, a classic example of a bad decision. Thankfully, that decision was reversed without much difficulty by the House of Lords[14]. But that is not always the case. The decision of the Court of Appeal in *The World Symphony and World Renown*[15] concerning the proper construction of a standard clause in Shelltime 3 with regard to redelivery of the chartered vessel at the end of the charter is – if I am permitted to vent a little spleen - another bad decision. But – even worse - in that case, the House of Lords refused leave to appeal. I tried – valiantly - to persuade Lord Templeman in that case to grant leave to appeal. Although he was - in the course of the oral application for leave - prepared to acknowledge that there was at least a strong argument that the decision of the Court of Appeal was wrong, his response was that the question of construction in that case did not justify the grant of leave because it did not involve a point of public importance – and those concerned could, if they wished, always change the standard form. And that is exactly what happened[16] - but that was, of course, little consolation to the Owners in that case.

8. The difficulty of construction often arises because the parties have chosen to use a particular form of standard wording which is unsuitable for the particular transaction. A good

[13] [1980] 1 Lloyd's Rep 466
[14] [1982] 1 Lloyd's Rep 1 and [1989] 1 Lloyd's Rep 1
[15] [1992] 2 Lloyd's Rep 114
[16] See *The Kriti Akti* [2004] 1 Lloyd's Rep 712

example is *The Alexion Hope*[17] which concerned a claim by the claimant bank under a mortgagees' interest policy. One gets a flavour of the difficulties of construction in that case by the opening words of the Judgment of Lloyd LJ in the Court of Appeal:

> *"In this case we are concerned with a new type of insurance. It seems a pity, therefore, that the parties should have incorporated their contract in a form which was described as long ago as 1791 by Mr. Justice Buller as absurd and incoherent: Brough v. Whitmore, (1791) 4 T.R. 206 at p. 210…"*

Those difficulties were exacerbated because the case turned largely upon certain additional wording which originated from Sweden and had been inserted in translation into the standard form. Lloyd LJ's exasperation as to the task facing the Court is manifest in the second paragraph of his Judgment:

> *"The conditions of insurance which comprise the main terms of the contract are known as "Mortgagee's Interest Clause 1". Clause 1 consists of eight numbered paragraphs, to which I shall have to refer in a moment. We were not told whether there is a cl. 2. If there is, it was not incorporated, for which we should perhaps be grateful. What we were told is that cl. 1 is a*

[17] [1988] 1 Lloyd's Rep 311

translation from the Swedish, where these particular conditions originated. We were urged by both sides to give certain words in cl. 1 their plain and ordinary meaning. Whether they have a plain and ordinary meaning in Swedish I do not know. But they certainly have no plain or ordinary meaning in English."

Ordinary and natural meaning ?

9. This reference to the plain and ordinary meaning of words is a constant refrain in the cases. But, what is the plain and ordinary meaning is often somewhat elusive. That may be so for a number of reasons.

10. First, it may be clear that something has simply gone wrong with the language. That was the case in *Chartbrook Ltd v Persimmon Ltd*[18]*.* Another good example is the recent decision of the Court of Appeal in *Caresse Navigation Ltd v Zurich Assurances MAROC*[19] which concerned the incorporation of a charterparty jusridiction clause into a bill of lading.

11. Second, the parties may use an archaic form. Inevitably, this makes the task of construction all the more difficult - in particular where the form uses words which may have acquired a particular meaning. A good illustration of

[18] [2009] 1 AC 1101
[19] [2015] 1 Lloyd's Rep 256

that difficulty is *The Salem*[20]. In that case, a cargo of oil worth approximately US$ 60 million was loaded on board a vessel in Kuwait for carriage to Europe. As the vessel sailed on her laden voyage down the east coast of Africa, the Master (with the connivance of the shipowner) stole most of the cargo by discharging it to third parties at an SBM off Durban. After discharge, the vessel continued on the voyage and then was scuttled off the west coast of Africa. The original cargowners (Shell) made an insurance claim. The cargo was insured on the standard SG Policy Form and Institute Clauses which provided cover for a wide range of perils including *"takings at sea".* At first blush, those are relatively simple words which, one might think, have an obvious ordinary and natural meaning. At first instance[21], Mustill J held that Shell could recover on the basis that the loss fell within the words *"takings at sea".* He reached this conclusion having regard to the previous decision of the Court of Appeal in *The Mandarin Star"*[22] which was, of course, binding on him. However, in the House of Lords, *The Mandarin Star* was overruled on the basis that the standard forms of SG Policy did not cover theft or misappropriation of cargo by a shipowner and to construe "*takings at sea"* to cover such a loss was contrary to *"historic orthodoxy"*.

12. But putting aside for the time being all questions of historic orthodoxy or other similar baggage, the focus of

[20] [1983] 1 Lloyd's Rep 342
[21] [1981] 2 Lloyd's Rep 316
[22] [1969] QB 449

English contract law has, of course, always been an objective approach based upon what is often referred to as the ordinary and natural meaning of the language used by the parties.

13. For some considerable period, this was taken to require a literalist approach. I do not know but I suspect that literalism was influenced at least in part by the approach of theologians to the interpretation of religious texts. For example, in earlier times, the presumption against surplusage appears to have been a strong factor in the construction of contracts. When the text is sacred that is perhaps understandable. But in construing private contracts, that is much less so with the result that the modern view is that in the interpretation of commercial contracts, the presumption against surplusage is of little value and that there is therefore no need – or at least less need – to strive to find meaning in every single word of the document.

14. Certainly, the search for the meaning of words and the proper approach to be adopted in that context has exercised the minds of theologians for a very long time. Thus, in the Jewish context, a famous Rabbi – Rabbi Ishmael ben Elisha otherwise known as the Ba'al Habaraita – devised a system of halachic exegesis almost 2000 years ago based upon 13 rules – or principles of construction which had a very profound influence on both Jewish and Christian theology. But that is a lecture for another day.

15. But what is literalism? That was the question Lord Steyn posed in the House of Lords in *Sirius*[23] and which he answered as follows:

> *"What is literalism? It will depend on the context. But an example is given in The Works of William Paley (1838 ed), Vol III, 60. The moral philosophy of Paley influenced thinking on contract in the 19th century. The example is as follows: The tyrant Temures promised the garrison of Sebastia that no blood would be shed if they surrendered to him. They surrendered. He shed no blood. He buried them all alive. This is literalism."*

16. As Lord Steyn went on to say, literalism should be resisted in the interpretative process. In modern times, we have all come to accept that this is not only desirable but axiomatic. But this is very much a modern view. The counter-argument, of course, is that literalism has the merit of promoting certainty – or, at the very least, greater certainty. I should emphasise that I am not suggesting for one moment the reinstatement of the literalist approach – but I do think that it is important to recognize that "resistance" to it often leads to potential uncertainty and therefore difficulty in the interpretative process; and, in the commercial context, that is inherently undesirable.

[23] *Sirius International Insurance Company v General Insurance Limited* [2004] 1 WLR 3251

17. In modern times, the abandonment of the literalist approach has, of course, been confirmed in a number of cases all of which are frequently cited *ad nauseum* in virtually every skeleton argument in the Commercial Court – *Schuler v Wickman*[24], *The Antaios*[25], *Chartbrook v Persimmon*[26] and, of course, *Rainy Sky*[27].

18. I do not propose to trawl through the various general statements in these cases. Nor do I propose to rehearse the arguments for and against the literalist approach. That is now a matter of history; and I am keen to look forward not back.

19. But it is, I think, worth briefly reminding ourselves of the specific issue in *The Antaios* which turned on the proper construction of a withdrawal clause in a time charter. The wording was in standard form in effect giving the owner the right to withdraw the vessel in the event of non-payment of hire or – and these were the important words – "any other breach". On the face of it, those are wide words. However, it was held that the words "any other breach" were to be construed as not meaning "any other breach" but as being limited to repudiatory breaches. If there were any doubt before *The Antaios*, that decision must mark the final death of literalism in favour of an approach based on business common sense. Whilst not seeking to criticise the conclusion reached in *The Antaios*, it seems to me a very good example

[24] [1974] AC 235
[25] [1985] 1 AC 191
[26] [2009] 1 AC 1101
[27] [2011] 1 WLR 2900

of a case where the ordinary and natural meaning of the words used by the parties has been trumped by the Court's view as to business common sense.

20. The best recent example of the death of literalism must be the decision of the House of Lords *in Premium Nafta Products & Ors v. Fili Shipping Company Ltd & Ors*[28]. Ever since the speech of Lord Porter in *Heyman v Darwins*[29], shipping[30] and insurance[31] lawyers had a field day in drawing narrow distinctions between particular words used in arbitration clauses – in particular, the distinction between disputes "arising under" and "arising out of" the agreement. But all of this was swept away by the House of Lords in that case. Lord Hoffmann proclaimed that these distinctions reflect no credit upon English commercial law; and that a "fresh start" was justified.

21. So it seems relatively clear that literalism is not only to be resisted - but is well and truly dead. Any possible lingering doubts have surely been extinguished by the recent decision of the Supreme Court in *Arnold v Britton*[32] which concerned the proper construction of a clause in a number of leases providing for the payment of a service charge. Although not a shipping or insurance case, the main speech by Lord Neuberger contains important statements as to the proper

[28] [2008] 1 Lloyds Rep 254
[29] [1942] AC 356, 399
[30] see eg *Union of India v E B Aaby's Rederi A/S* [1975] AC 797
[31] see eg *Mackender v Feldia AG* [1967] 2 QB 590; *Overseas Union Insurance Ltd v AA Mutual International Insurance Co Ltd* [1988] 2 Lloyd's Rep 63, 67,
[32] [2015] 2 WLR 1593 at [15] quoting Lord Hoffmann in *Chartbrook* at [14]

approach to the construction of contracts. Thus, at paragraph 15, Lord Neuberger stated:

> *"…..When interpreting a written contract, the court is concerned to identify the intention of the parties by reference to "what a reasonable person having all the background knowledge which would have been available to the parties would have understood them to be using the language in the contract to mean"……. And it does so by focussing on the meaning of the relevant words…in their documentary, factual and commercial context. That meaning has to be assessed in the light of (i) the natural and ordinary meaning of the clause, (ii) any other relevant provisions of the lease, (iii) the overall purpose of the clause and the lease, (iv) the facts and circumstances known or assumed by the parties at the time that the document was executed, and (v) commercial common sense, but (vi) disregarding subjective evidence of any party's intentions."*

22. Lord Neuberger then goes on to emphasise 7 factors. I do not propose to consider all these factors in detail. At this stage, it is sufficient to note that perhaps unsurprisingly, Lord Neuberger emphasises the importance of the language of the provision which is to be construed.

23. Nor do I propose to say much about Lord Neuberger's first three factors ie the ordinary and natural meaning of the words, the relevance of other contractual provisions and the overall purpose of the clause. These topics are addressed at

length in the many books and articles that I have already referred to.

24. Sometimes, a consideration of these three factors will provide a clear pointer to the construction of the words in question. But, more often than not, this will not be so. What then?

25. Well, sometimes one should I think simply acknowledge that there is no necessarily clear-cut answer – and that legitimate views may differ. A good example of such a case is *The Niobe*[33]*.* The main issue in that case concerned the proper construction of clause 11 of the Norwegian Saleform which, in effect, required the sellers to notify the Classification Society of *"…any matters coming to their knowledge prior to delivery which would lead to the withdrawal of the vessel's class or to the imposition of a recommendation relating to her Class.…"* The simple question in that case was whether the effect of such provision was to impose an obligation on sellers to notify Class of relevant matters which came to their knowledge prior to the date of the contract. In the Court of Appeal, it was held not so – and that, in effect, the obligation to notify related only to matters coming to the sellers' knowledge after the date of the contract. But this was overturned in the House of Lords – it being held that there was no *terminus a quo* and that the sellers were obliged to inform Class before

[33] *Niobe Maritime Corporation v Tradax Ocean Transportation SA* [1995] 1 Lloyd's Rep 579

delivery of all relevant matters whenever such matters may have come to their knowledge. It is perhaps comforting to know that even Lord Bingham and Lord Justices Beldam and Saville are not always right !!

Factual Matrix

26. So I turn briefly to the fourth factor identified by Lord Neuberger – that is "..*the facts and circumstances known or assumed by the parties at the time that the document was executed..*" That is, of course, what is generally referred to as the *"factual matrix".* The origin of this phrase would seem to be the speech of Lord Scarman in *Bunge v Tradax*[34] referring to the speech of Lord Wilberforce in *Prenn* v *Simmonds*[35] when the latter stated:

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

27. Here starts what seems to me the first main difficulty in the process of construction particularly since, as stated by Lord Hoffmann, in *ICS v West Bromwich*[36] and as further explained by him in *BCCI v Ali*[37]*,* this phrase is to be taken

[34] [1981] 1 WLR 711
[35] [1971] 1 WLR 1381 at pp. 1383H-1384A and, to similar effect, Lord Wilberforce's speech *in the Reardon Smith case* [1976] 1 W.L.R. 989, at pp.995E-997D.
[36] [1998] 1 WLR 896
[37] [2002] AC 251

as including, and I quote, *"…..absolutely anything which would have affected the way in which the language of the document would have been understood by a reasonable man"*.

28. These are wide words. I have no difficulty with them as a matter of legal principle. However, there is a real practical difficulty for two main reasons.

29. First, the distinction between what is and what is not admissible may not be straightforward. Thus, as stated by Lord Clarke in *Oceanbulk Shipping & Trading v TMT*[38]

"….Trial judges frequently have to distinguish between material which forms part of the pre-contractual negotiations which is part of the factual matrix and therefore admissible as an aid to interpretation and material which forms part of the pre-contractual negotiations but which is not part of the factual matrix and is not therefore admissible. This is often a straightforward task but sometimes it is not."

30. Second, one or both parties will often seek to introduce at trial a large amount of evidence – both documentary and factual - under the guise of *"factual matrix"*. This can take up much Court time and lead to substantial additional costs.

[38] [2011] 1 AC 662

31. Let me briefly give you two examples from trials which I conducted in the Commercial Court – one from the shipping context and one from the insurance context. The first is *The Falkonera*[39] which concerned the proper construction of various clauses in a charterparty as to whether the charterer was entitled to order the ship – which was a VLCC - to perform a ship-to-ship transfer to a much smaller ship. On that issue, the charterers sought to rely - by way of factual matrix evidence - on various oral discussions between the parties' representatives some weeks prior to the charterparty at a restaurant and then at the Lantern Bar at the Fullerton Bay Hotel, Singapore. As you will all know, the Lantern Bar is a lively open-air establishment with live music.

32. The second example comes from the insurance field: *Ted Baker v Axa & Others*[40]. This was an insurance claim brought by Ted Baker, the well-known retailer, against its insurers arising out of goods stolen from its warehouse in London by its own employee warehouseman. The policy included loss by "theft" but the underwriters sought to argue that the term "theft" had a narrow meaning and that it did not include theft by an employee. In support of that argument, they sought to adduce what was said to be factual matrix evidence relating to the conduct of the parties over a number of years.

[39] [2013] 1 Lloyd's Rep 582
[40] [2012] EWHC 1406 (Comm)

33. The further details of these two cases do not matter. For present purposes, it is sufficient to note that in both cases, I had to hear a very considerable amount of evidence on the basis that it allegedly formed part of the "factual matrix". In the event, I held that it was all inadmissible – but only after much time and considerable expense. It would be inappropriate for me to comment further on these two particular cases – but I can, I think, say, that they reflect what has become a common and significant problem in the conduct of modern commercial litigation.

34. In my view, the answer is clear. Any question of "factual matrix" evidence should be raised and addressed at the earliest opportunity long before the trial by active and robust case management. With that in mind, I would draw specific attention to the new requirement contained in para C1.2(h) of the Commercial Court Guide:

"(h) Where proceedings involve issues of construction of a document in relation to which a party wishes to contend that there is a relevant factual matrix that party should specifically set out in his pleading each feature of the matrix which is alleged to be of relevance. The "factual matrix" means the background knowledge which would reasonably have been available to the parties in the situation in which they found themselves at the time of the contract/document."

35. I wonder how many of you here are aware of this new requirement. In any event, you know it now. For my part, I

very much hope that it will be rigorously enforced; and, if it is, I would also hope that the difficulty I have referred to will be eliminated or at least reduced in the future.

Commercial Common Sense

36. Lord Neuberger's fifth factor is *"commercial common sense".* This is the big one ! In modern times, the importance of this factor has a long pedigree going back again to *Prenn v Simmonds* and beyond. In the shipping context, of course, the most famous – and certainly most notorious – expression of this factor is the statement of Lord Diplock in *The Antaios*[41] (at 201):

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

I say notorious because, in my experience, this passage is frequently wheeled out triumphantly in virtually every case involving an issue of contractual construction. – often by both parties in support of their own particular construction !

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[41] *Antaios Compania Naviera SA v Salen Rederierna AB* [1985] AC 191. To similar effect is the other oft-quoted statement by Lord Steyn in *Mannai Investment Co Ltd v Eagle Star Life Assurance Co Ltd* [1997] AC 749 at p771A-B: *"In determining the meaning of the language of a commercial contract . . . the law . . . generally favours a commercially sensible construction. The reason for this approach is that a commercial construction is more likely to give effect to the intention of the parties. Words are therefore interpreted in the way in which a reasonable commercial person would construe them. And the standard of the reasonable commercial person is hostile to technical interpretations and undue emphasis on niceties of language."*

According to *BAILII*, this passage would appear to have been quoted virtually verbatim in over 250 reported cases.

37. Again, I have no difficulty in principle with such proposition or other similar propositions. However, in my experience, it is often difficult – indeed very difficult - to apply in practice. The difficulty is that a Judge is often faced with competing arguments by both parties that their own particular construction is the one which best accords with business common sense and that the other party's suggested construction was commercially unreasonable; and I am doubtful that the Judge – even a Commercial Judge – is very well equipped properly to weigh these competing arguments.

38. In some cases, the construction which is commercially reasonable may be relatively obvious. Take, for example, the recent decision of the Court of Appeal in the *Valle di Cordoba*[42] where the essential issue was that loss by piracy falls within an *"In-Transit Loss"* clause in a voyage charterparty. At its simplest, the charterer's argument was that the pirates caused the loss; so there was a loss; and the loss occurred during the voyage i.e. in transit. Hey presto ! That is, it was said, the ordinary and natural meaning of the words. And viewed in isolation out of context, one can perhaps see force in that argument. But, that meaning was rejected for a whole host of reasons – in particular the

[42] *Trafigura Beheer BV v Navigazione Montanari SPA* [2015] EWCA Civ 91

reason that, if the charterer were right in that case, it would mean that the owner was, in effect, the insurer of the goods during the voyage.

39. But, in many cases, the question of what is commercially reasonable is much more uncertain. A good illustration of this is *The Kyzikos*[43] where the question arose as to the proper meaning of the acronym "wibon" - *"whether in berth or not"* - in the context of a berth charterparty. Simply stated, a ship arrives in a port and gets as near as she can to the designated berth. Although the berth is free, the ship cannot get to it because of some physical obstruction – in that case fog. Who bears the risk of the waiting time until the fog lifts and the ship can proceed to the berth In standard form? In that case, the charterparty provided that the ship could serve a notice of readiness "whether in berth or not". On the face of it, one might think that the ordinary and natural meaning of those words permitted the shipowner to serve a valid notice of readiness when the vessel gets as far as she can. And so held by both the arbitrator and the Court of Appeal. But this was rejected by Webster J at first instance and, ultimately, by the House of Lords. However, what is really interesting about the case is the clash of views between, on the one hand, Lord Justice Lloyd, in the Court of Appeal and, on the other hand, Lord Brandon, in the House of Lords. Two great lawyers with huge experience of shipping law. But they were at daggers drawn

[43] [1987] 2 Lloyd's Rep 122

as to the meaning of the words. In the Court of Appeal, Lord Justice Lloyd said that the traditional view of the effect of the phrase “wibon” had always been that the phrase became operative so as to enable a valid notice of readiness to be given as soon as the vessel has arrived in the port provided that the other conditions of a valid notice are satisfied. In other words, the effect of the “wibon” provision was to turn the berth charterparty into a port charterparty. But Lord Brandon – and the other Law Lords - disagreed. There was, he said, no such traditional view. According to Lord Brandon, the answer to the issue in that case depended upon two considerations, viz. first, the meaning given to the words by the authorities and, second, the context in which the acronym was used.

40. In my view, the decision of the Court of Appeal in *The Kyzikos* provides a good illustration of the real danger of assuming that the question of construction can be resolved by ignoring historic orthodoxy and the words used by the parties and applying some perceived abstract general notion of the reasonable expectations of honest men – or women !

41. For my part, I do not think that *Arnold v Britton* says anything particularly new or dramatic. If I have any observation, I would perhaps express disappointment that there appears to be nothing in Lord Neuberger’s speech with regard to established principles of construction. In particular, I would respectfully suggest that in many cases questions of construction are best resolved by reference to such

principles and against the background of “historic orthodoxy” or what might be described as “presumptions of law” which the courts apply in determining what is to be taken as the intention of the parties[44]. In any event, *Arnold v Britton* is a useful and timely reminder that “commercial common sense” is not necessarily the overriding criterion. This is also reflected in other recent cases including, for example, *BMA Special Opportunity Hub Fund v African Minerals Finance[45],* where *Aikens LJ said:*

“…I would agree with the statements of Briggs J, in Jackson v Dear[46] first, that "commercial common sense" is not to be elevated to an overriding criterion of construction and, secondly, that the parties should not be subjected to "…the individual judge's own notions of what might have been the sensible solution to the parties' conundrum". I would add, still less should the issue of construction be determined by what seems like "commercial common sense" from the point of view of one of the parties to the contract.”

42. The recent clash of judgments as to whether the obligation to pay hire under a time charter is, or is not, a “condition” has given rise to similar arguments based on what is said to be business common sense. As you will know, in *The Astra[47],* Flaux J concluded that the obligation to

[44] See, for example, *Scottish Power UK Plc v BP Exploration Operating Company Ltd & Ors* [2015] EWHC 2658 (Comm) at para [23].
[45] [2013] EWCA Civ 416 at [24].
[46] [2012] EWHC 2060
[47] *Kuwait Rocks Co v AMN Bulkcarriers Inc.* [2012] EWHC 865 (Comm)

pay hire was a condition. However, earlier this year, in *Spar Shipping*[48]*,* Popplewell J concluded that it was not. I do not propose to consider here the various arguments and counter-arguments save with regard to one advanced by Lord Phillips speaking extra-judicially in the Cedric Barclay Lecture at the ICMA Conference in Hong Kong earlier this year[49] where he expressed the view that the Judgment of Flaux J was to be preferred because the Judgment of Popplewell J does not lead to a *"sensible commercial result"*. For present purposes, I would only note two points.

43. First, Lord Phillips' argument against Popplewell J's conclusion is founded in part on the notion that the obligation to pay hire must be treated as a condition because – and I quote - the owner *"…may otherwise be uncertain whether the stage has been reached at which the charterer's defaults amount to renunciation or repudiation."* However, that argument is similar to the one which the House of Lords rejected in *The Antaios.* To recall, the main argument in that case was that the words "any other breach" should be given their ordinary and natural meaning because any narrower meaning would result in uncertainty i.e. it would be uncertain as to whether the charterer's breaches amounted to renunciation or repudiation. But, as I say, that argument was rejected by the House of Lords. As it seems to me, this

[48] *Spar Shipping SA v Grand China Logistics Holding (Group) Co. Ltd* [2015] EWHC 718 (Comm)

[49]http://chinasymposium.com/articles/Shipping_Law/THE%20CEDRIC%20BARCLAY%20LECTURE%202015.pdf

highlights the difficulty – indeed the danger – of seeking to invoke what might appear to be a sensible commercial result.

44. Second, and perhaps more fundamentally, the English common law has always proceeded – so far as possible - on the basis of principle. I warmly welcome the abandonment of a literalist approach; but its abandonment has left a lacuna. In my view, that lacuna is not necessarily filled by saying, for example, that contracts should be construed in accordance with the reasonable expectations of honest men or commercial common sense. No one could possibly disagree with that broad objective but in many cases it provides little assistance in identifying what those reasonable expectations might properly be said to be; or what is, in any particular case, “commercial common sense”.

45. Let me return to the clash between *The Astra* and *Spar Shipping*. In that specific context, what is “commercial common sense” ? The truth is: I have no idea. From the owner’s point of view, it may well be commercial common sense that the charterer should pay the hire due on time – and not a minute or even a second late; and that any failure to pay by the due date should entitle the owner to bring the charter to an end and claim substantial damages. From the charterer’s point of view, it may well be commercial common sense that if, for example, the hire is late by a very short period due to no fault of his own (eg some fault in the banking system), such failure should not amount to a

repudiation so as to entitle the owner to bring the charter to an end and claim substantial damages.

46. As in many cases, the “commercial common sense” test does not provide the answer. Indeed, I would go further: the danger is that in many cases it gives – or at least may give - the wrong answer.

47. Rather, it seems to me that the answer whether or not the obligation to pay hire is or is not a condition is a matter of construction capable of being determined by reference to the application of the well-established principle summarized by Lord Scarman in *Bunge v Tradax*[50] viz. that unless the contract makes it clear that a particular stipulation is a condition or only a warranty, it is an innominate term, the remedy for a breach of which depends upon the nature, consequences and effect of the breach. That seems to me an important and clear principle of construction which eliminates or at least reduces uncertainty and is easy to apply in practice. If that is right, the attempt to invoke arguments as to what may or may not be perceived as commercially sensible introduces difficulties which are, I would suggest, unnecessary.

48. None of this is rocket science – and we will presumably be told the answer to this particular problem when the Court of Appeal delivers its Judgment in *Spar Shipping* some time

[50] [1981] 1 WLR 711

next year. The appeal is, I understand, due to be heard in June.

49. To be clear, I do not say that the "commercial common sense" test is irrelevant or to be ignored. All I am saying is that, in many cases, the proper construction of a contract is best ascertained by reference to the words used by the parties and the application of well-established principles of construction. As stated by Hobhouse J in *E E Caledonia v Orbit Valve*[51] with regard to the proper construction of an indemnity clause:

"….it also has to be borne in mind that commercial contracts are drafted by parties with access to legal advice and in the context of established legal principles as reflected in the decisions of the Courts. Principles of certainty, and indeed justice, require that contracts be construed in accordance with the established principles. The parties are always able by the choice of appropriate language to draft their contract so as to produce a different legal effect. The choice is theirs…."

50. Owners and charterers are, of course, perfectly entitled and able to make the obligation to pay hire a condition. It is easy-peasy. They can, I think, do so by saying that "time shall be of the essence" as was done, for example, in *The Mahakam*[52]. But absent language of such kind, there is in my

[51] [1993] 2 Lloyd's Rep 418
[52] *Parbulk Ii A/S v Heritage Maritime Ltd SA* [2011] EWHC 2917 (Comm)

view, no warrant for the Court, in effect, to insert those words in the charterparty under the banner of commercial common sense.

51. I turn finally to consider briefly two further matters which lurk in the background of the construction of commercial contracts – and occasionally pop their heads up above the parapet. The first is the question of implied terms; and the second is the question of "good faith". Again, both these topics are considered extensively in the books and articles which I have referred to. And you will be pleased to know that I do not propose to carry out a full-scale analysis of them here tonight. But I think it is important to say something with regard to these two points by reference to a number of recent cases.

52. So far as implied terms are concerned, the law was relatively clear until at least the decision of the Privy Council in *A-G v Attorney General of Belize & Ors v Belize Telecom Ltd & Anor (Belize)*[53]. If one looks, for example, at the editions of *Chitty* before that case and as every student of law knew, a term may be implied in two situations i.e. first where it is necessary to give business efficacy to the contract; and second, where the term implied represents the obvious, but unexpressed, intention of the parties. In *Belize*, Lord Hoffmann made plain that the implication of a term is no more than an exercise in the construction of the instrument

[53] [2009] 1 WLR 1988

as a whole. There is, he said, only one question: is that what the instrument, read as a whole against the relevant background, would reasonably be understood to mean? In one sense, such formulation is unobjectionable. But it has provoked much academic debate. In particular, the danger of such formulation is the underlying suggestion that a term may be implied simply because it is "reasonable"; and there is no doubt that it has caused real difficulty as appears from a number of cases including, for example, in the shipping context, *The Reborn*[54] where Lord Hoffman's analysis is considered in some detail. For present purposes, it is sufficient to note Lord Clarke's observation[55] that although Lord Hoffmann was emphasising that the process of implication is part of the process of construction of the contract (which is again unobjectionable) he – i.e. Lord Hoffmann - was not in any way resiling from the often stated proposition that it must be necessary to imply the proposed term; and that it is never sufficient that it should be reasonable. It is also perhaps noteworthy that in Singapore, the Court of Appeal has declined to follow *Belize*[56]*.*

53. Whilst recognizing that there is ultimately only one question as to the meaning of a contract, recent cases continue to emphasise the "necessity" test[57] in the context of the implication of terms. To my mind, that is important not

[54] *Mediterranean Salvage & Towage Ltd v Seamar Trading & Commerce Inc* [2009] 2 Lloyd's Rep 639
[55] at [15].
[56] *Foo Jong Peng & Ors v Phua Kiah & Or* [2012] 4 SLR 1267
[57] See, most recently, *Mr H TV Ltd v ITV2 Ltd* [2015] EWHC 2840 (Comm) at [40]-[41].

only because it is part of the historic orthodoxy of English law but because it avoids the suggestion that a term should be implied simply because it may seem reasonable to do so; and thereby promotes commercial certainty.

54. Return again to the clash between *Astra* and *Spar*. The charterparties in those cases said nothing expressly about the remedies available to the owner in case of late payment by the charterer. In truth, the argument that the owner should be entitled to bring the charters to an end even if an instalment of hire is a second late is tantamount to an argument that the Courts should imply a term to that effect. But why ? In my view, any such implied term is certainly not necessary to make the charter work. And, if that is right, there is no reason in principle why the Courts should imply such a term or construe the charters in such a way on the altar of commercial common sense. On the contrary, to do so would, in my view, be contrary to the well-established principle which I have already referred to and involve an unjustified and unprincipled rewriting of the parties' agreed bargain.

55. Finally, I turn briefly to the question of good faith. Again, this is a topic with a very broad canvas which has been considered by academics notably Professor McKendrick in his Contract Law[58] where he describes the so-called traditional English hostility towards any general

[58] 9th Edition pp221-222.

doctrine of good faith. The concept of good faith has, of course, an important place in the law of insurance and many contracts – even contracts outside that field - expressly provide for the parties to perform their obligations in good faith[59]. It has also been considered in a number of recent cases including *Emirates Trading Agency Llc v Prime Mineral Exports Private Ltd*[60] where Teare J reviewed the relevant authorities and concluded that a time limited obligation to seek to resolve a dispute in good faith should be enforceable.

56. The relevant case-law – in particular with regard to the exercise of contractual discretions[61] - was also reviewed by Leggatt J in *Yam Seng Pte v International Trade Corp Ltd*[62]*;* and he concluded that there is, in fact, nothing novel or foreign in recognising an implied duty of good faith in the performance of contracts.

57. One of the cases Leggatt J refers to is the decision of the House of Lords in *HIH Casualty v Chase Manhattan Bank*[63]*.* In that case a contract of insurance contained a clause which stated that the insured should have "no liability of any nature to the insurers for any information provided". A question arose as to whether these words meant that the

[59] See eg. *The Federal Mogul Asbestos Personal Injury Trust v Federal-Mogul*[1014] EWHC 2002 (Comm)
[60] [2014] EWHC 2104 (Comm)
[61] See eg *The Vainquer José* [1979] Lloyd's Rep 557; *The Product Star* [1993] 1 Lloyd's Rep 397; *Barclays v Unicredit* [2014] 1 Lloyd's Rep 59; *Braganza v BP* [2015] 2 Lloyd's Rep 240
[62] [2013] 1 Lloyd's Rep 526
[63] [2013] 2 Lloyd's Rep 61

insured had no liability even for deceit where the insured's agent had dishonestly provided information known to be false. The House of Lords affirmed the decision of the courts below that, even though the clause read literally would cover liability for deceit, it was not reasonably to be understood as having that meaning. Of course, the notion that there is a general duty of good faith in any insurance contract is unsurprising. But the importance of the case lies in the general observations made in certain of the speeches. As Lord Bingham put it at [15]:

> *"Parties entering into a commercial contract ... will assume the honesty and good faith of the other; absent such an assumption they would not deal."*

To similar effect, Lord Hoffmann observed at [68] that parties "contract with one another in the expectation of honest dealing", and that:

> *"... in the absence of words which expressly refer to dishonesty, it goes without saying that underlying the contractual arrangements of the parties there will be a common assumption that the persons involved will behave honestly."*

58. Leggatt J may well be right in the conclusion that he reached in *Yam Seng*. But his observations in another recent

case, *MSC Mediterranean Shipping Co v Cottonex Anstalt*[64] are, I would respectfully suggest, much more controversial. The main issue there was whether an owner could, in effect, claim demurrage as a debt indefinitely; or whether the owner was, in effect, obliged to accept the delay as a wrongful repudiation, bring the contract to an end and claim damages. The remedies available in such circumstances are ultimately a matter of construction. Applying what are now well-established principles, Leggatt J concluded that the owner had no legitimate interest in keeping the contracts alive indefinitely and was, in effect, obliged to bring them to an end and claim damages. That analysis would seem unobjectionable.

59. However, he went on to say that the principle can be seen in a wider context viz that the right to decide whether or not to bring a contract to an end is, in effect, equivalent to a contractual discretion which must be exercised in good faith. I would respectfully suggest that that is a step too far. In my view, ever since the decision of the House of Lords in *White & Carter (Councils) v McGregor*[65]*,* English law on this toipic has evolved over the last 50 years – as the common law does – on the basis of principle. The principle which is now well-established limits the supposed right of election and, in effect, obliges the innocent party to bring the contract to an end if he has no "legitimate interest" in keeping it alive. In my view, such an approach is one which can be readily

[64] [2015] EWHC 283 (Comm)
[65] [1962] AC 413

understood and applied; and that to replace it with one of good faith – or to view such test as an aspect of a general duty of good faith in contractual dealing - is not only unnecessary but would tend to introduce further uncertainties in this important area of the law.

60. Moreover, if Males J is right that the question of whether or not an innocent party is entitled or indeed bound to bring a contract to an end depends – or may depend – on good faith – why not the owner's right of withdrawal under a time charter ? But we know from the decision of the House of Lords in *The Scaptrade*[66] that there is no relief against forfeiture in equity - which is perhaps difficult to square with the importation of a duty of good faith in these circumstances.

Conclusion

61. How do these various strands fit together ? In my view, the answer is relatively clear. Inevitably, there will be contracts – as there have always been – which lack clarity or are otherwise badly drafted. That is a difficulty which we will have to live with – and trust the arbitrators and the Courts to do the best they can.

62. Although literalism has been abandoned, the recent confirmation – or reconfirmation – of the importance of the

[66] [1983] 2 Lloyd's Rep 253

words used by the parties in *Arnold v Britton* is certainly most welcome. However, in my view, there remains a real danger of losing sight of well-established principles of construction which potentially undermines the certainty of commercial contracts generally – and shipping and insurance contracts in particular. The constant plea for commercial common sense often does not eliminate that danger; and, in some instances, increases it. Rather, as stated by Hobhouse J in the passage which I have already quoted: "*Principles of certainty, and indeed justice, require that contracts be construed in accordance with the established principles."* Such an approach lies at the heart of English law and it should not be – must not be - forgotten. That is the message which I would leave with you this evening.

Thank you.